

22
number

2016 economic report



CAMBRA
DE COMERÇ
INDÚSTRIA I SERVEIS
D'ANDORRA

With the support of



Andorran Banking
Associació de Bancs Andorrans

EDITED BY

The Chamber of Commerce, Industry
and Services of Andorra

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PRELIMINARY NOTE

In accordance with Article 16 of the Law for the creation of the Andorran Chamber of Commerce, Industry and Services, on 3 September 1993, the Chamber is obliged to prepare, publish and transmit annually to the Andorran government an economic report that describes the development in and prospects for economic activities inside Andorran territory.

The preparation and collection of the data that appear in this report has involved contributions from companies, which collaborate with the Chamber by answering the periodical overall surveys, and also from the central government, Comu governments and other institutions and business associations which, through their provision of information, make our work possible and simpler. To all these, we would express our thanks, in the confidence that our work will be of use for understanding the economic reality of our country.

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Introduction

In 2016, the international context continued to spring surprises related to episodes of political instability. The UK referendum that decided to leave the European Union was a wholly unexpected result. This and the election surveys carried out in other countries led to contagion within the European Union and was an instability factor. Then, in 2017, both Netherlands and France elected leaders with pro-Europe views, easing the fears about the fragility of European unity. In parallel, in 2016, the US elected Donald Trump as president, against all expectations. On the other hand, the terrorist phenomenon (basically of jihadi origin) hit countries such as Germany, France, the UK, Turkey, Belgium and, at the time of writing, Spain (Barcelona and Cambrils). Phenomena such as Brexit, Trump's victory and rising votes for extremist parties are partly linked to economic factors that originate in job insecurity, unemployment and the waning middle classes, which need to be kept in sight. In international relations, questions are raised about the interactions between the US, China and Russia, mainly, with risks of trade frictions if protectionist measures materialise. All these phenomena bring uncertainties and risks which may affect developments in the global economy over the next few years.

Macroeconomic data published by the IMF, in July 2017, confirm a slowdown in global GDP growth in 2016. Specifically, growth was 3.2%, two tenths less than in 2015 which, moreover, is the lowest since 2009. By economic areas, different performances are recorded between the advanced and emerging economies. The moderation in growth in the global economy was mainly due to a lower contribution from advanced economies, while emerging and developing economies maintained the same rate of growth as in 2015. In any case, this same body considers that the lowest level was seen in 2016 and that from 2016, a turning point will cause the trend in the global economy to rise. However, there are still uncertainties. Among the economic and financial unknowns are notably the slowdown in international trade which, since 2012, has resulted in growth rates that are lower than the average of recent decades. Equally, there are concerns about the reappearance of financial weaknesses in advanced economies and especially China.

In 2016, the advanced economies grew a modest 1.7%, clearly lower than the increases recorded in 2014 and 2015, although they are predicted to grow 2% in 2017, more in line with growth in previous years. For these economies, as a whole, the main driving force of economic growth in 2016 was family consumption. On the other hand, the rate of progress of these advanced economies shows different intensities according to areas. For example, in the US, GDP growth was 1.6%, one point lower than in 2015, while in the Eurozone as a whole, it resisted the episodes of financial instability and political events of 2016 well, already seeing GDP growth of 1.8%, only two tenths less than in the previous year. Outside the Eurozone, Sweden's good growth rate (3.3%) stands out, contrasting with the slower growth in the UK (1.8%) and Japan (1.0%).

These growths have allowed a slow, gradual decrease in unemployment, which stood at 10% for the whole of the Eurozone in 2016, despite major differences. So, in Spain, the unemployment rate reached 19.6%; in France, 10% and in Germany, 4.2%.

In 2016, the emerging and developing economies together grew 4.3%, exactly the same as in the previous year, but halting a downward trend that had occurred since 2011. By country, growth was also variable. So, India maintained significant growth (7.1%), while the GDP of Latin America shrank 1%, representing the worst trend among the major global regions. On the other hand, the Russian economy also shrank (-0.2%) and the growth rate of the Chinese economy continued to decrease slowly, to reach 6.7%.

Regarding our neighbouring economies, according to OECD data, it appears that there was a general slight improvement in 2016.

In the case of France, GDP grew 1.1%, a very similar variation to 2015 (1.2%) and well below that of 2013 and 2014. This slow growth was the result, especially, of the favourable behaviour in domestic demand; on the other hand, the foreign sector made a negative contribution, caused by the lack of momentum in exports. The unemployment rate reached 10%, lower than in the period 2013-2015, where it stabilised at about 10.3% and 10.4%. The public deficit has fallen progressively: in 2016, it was -3.4%, contrasting with 2009, when it was -7.9%. Public debt already represents 96.6% of GDP.

In the case of Spain, the economy grew 3.2% (the same as in 2015), well over the average for the Eurozone (1.7% according to the OECD), with the added value that this is the third consecutive year of expansion. Initially, the recovery was driven by exports and then transferred gradually to domestic macroeconomic magnitudes. In this context, the unemployment rate reached 19.6% with progressive decreases since 2013, in which a high of 26.1% was reached. For its part, the public deficit is also falling: in 2016, it was -4.5% of GDP and in 2012, it reached -10.5%. Despite the decrease, public deficits have accumulated and in 2016 the Spanish public debt represented 99.4% of GDP.

Within this context of progressive improvement in the economic environment, in 2016, Andorra continues the economic recovery that was started in 2013, with a slight acceleration in activity, although still far from the levels of the previous expansionary period. This moderately positive trend became evident in an improvement in the main available indicators of activity, although levels were still discreet. This is the fourth consecutive year of Andorran economic growth, despite being lower than that of the Spanish economy and the EU as a whole, and equal to that of the French economy.

The recovery in the Andorran economy observed in recent years has been favoured, to a large extent, by the progressive improvement in the international context, above all in the Eurozone and more specifically in Spain. The GDP estimate published by the Government shows growth of 1.2% in real terms, higher than the increase of 0.8% seen in 2015. It should be specified that the trend in the Andorran economy over the last two years was affected by a domestic financial crisis, based on the BPA affair, and also the effect of fiscal transparency which mostly affects banking activities so, if we exclude the financial sector, the growth rate of the real economy (non-financial GVA) was 2.4%, double the aggregate real growth for all sectors together.

The total nominal GDP of Andorra was 2,584.1 million euros, the highest value since 2009, and GDP per capita reached 35,348 euros in nominal terms, a similar level to 2015.

The Andorran recovery can be seen in the upward trend in the great majority of indicators of activity and demand. Among the most relevant are the increases in imports without fuels (7.5%), the number of visitors (2.6%) and employment (1.9%), all higher in 2015. Also significant was the dynamic in car registrations (10.5%) and industrial vehicles (30%), the number of businesses (5%) and establishments (5.6%) and electricity consumption (2.8%). Equally notable was wage growth (4.3%) and the major reduction, for the third consecutive year, in the number of job seekers (-15.7%). The negative note in 2016 is still the trend in lending, although the interannual rate of decline eased to -0.4%, after the adjustments in the banking sector resulting from the BPA affair in 2015. In conclusion, the recovery in the Andorran economy continued to progress slowly in 2016 and is expanding progressively to all economic activities.

The agricultural sector had growth in real GVA of 0.5%, after three years of very strong falls in activity. So, this is low growth, which may indicate a change in trend. A 4.5% increase in the number of employees occurred, in a context in which the useful agricultural surface area and the tobacco harvest also grew (0.9% and 0.6%, respectively). In contrast, the number of livestock fell for the

second consecutive year (-5%), but is still in line with the historical average observed since 1995 (about 5,200 heads). In any case, it should be noted that the percentage of the primary sector of the economy is very small (0.5%), so its impact on total GDP is very limited. However, the qualitative value of the sector is important. Its existence helps to conserve the landscape and the good image for tourism. The sector is making efforts to create niches in the market with the Andorran brand both in relation to livestock products (such as quality meat) and agricultural products (such as wine, among others).

The industry and manufacturing sector is made up, on the one hand, of basic industry, essentially based on energy production and distribution and, on the other hand, manufacturing, which is the most significant activity – in 2015, it concentrated 71% of GVA from secondary activities (2016 data are not available). The real GVA for the whole of the industry and manufacturing sector fell in 2016 by 1.1%. This weakness in overall activity that was observed in 2016 also resulted in a reduction in the number of sector businesses (-0.7%) and a slowdown in the rate of job creation (1.5%) and energy consumption (1.2%). However, a trend has also been observed towards a slight improvement in confidence in the sector, reflected in the replies from businesses to the Chamber's surveys. Specifically, the confidence indicator recovered a positive balance in the second half of the year, after almost twelve consecutive years on very negative ground. In this context, industrial businesses have indicated an average increase in turnover of 3.6%, higher than in 2015, and a rise in investment (5.1%), which contrasts with the decreases in previous years.

Regarding the construction sector, it was already highlighted in the 2015 report that this was showing the first signs of improvement. This year, the positive contribution from construction to the national economy can already be affirmed. The sector saw growth in real GVA of 1.2%, contrasting with the near stagnation which marked it in 2015 (0.2%). This increase is significant because it arrives after nine years of steep falls in GVA which, in 2015, left it 60% below the high achieved in 2006. As a result, construction currently represents 5.8% of total GVA, compared with the 12.6% it represented just before the crisis. The signs of improvement in construction can also be seen in the trend in most available indicators of activity for the sector. So, in 2016, there was an acceleration in the rate of job creation (2.1%), the number of businesses (1.9%) and the average sector wage (1.5%). On the other hand, 35 construction permits for new builds were granted, with a total authorised surface area of 41,677 square metres, figures which show an 8.1% decrease in the number of square metres of authorised new builds against 2015. So, the rate of progress in activity is still modest and suffers from very low levels. The future correlation of this sector with public investment is also an unknown. In 2016, the public sector reduced its investment volume (-17%), after two years of growth. This factor, which improves public finances, limits reactivation of the sector. In contrast, measures such as the Renova Plan, consisting of aid to promote remodelling of properties, improvements in building energy efficiency and the use of renewable energy are a stimulus to the sector. Along the same line, the results of the Chamber's surveys show that construction has reached a turning point and left behind the strong contraction, with new signs of reactivation. So, business activity has turned upward, with three consecutive weeks on positive ground, while businesses' replies about developments in contracted and executed works have started to show signs of improvement, if at still very low levels.

The performance of the services sector is significant within the global volume of the Andorran economy. In 2016, it represented 88.8% of GVA and saw real growth of 1.4%, being the sector that grew most. Nevertheless, we must differentiate between subsectors: in 2016, real GVA of the commerce, hotels & catering, transport, information and communications subsector increased 4.4%, while that of the financial, real estate, professional and technical activities subsector fell 0.7%, and that of public administrations, education, health, social and personal services increased a moderate 0.7%. However, this still modest momentum is based on the improvement in activities linked to commerce and, above all, tourism. This positive trend continued, driven by the increasing

number of tourists (6.3%) and a slight recovery in same-day visitors (0.7%), with the consequent increase in commercial sales and hotel occupancy. The upward trend in tourism was also evident in the progress in imports of goods (4.9%) and the increase in ski days sold (1.3% in the 2016-2017 season) and the number of overnight stays (2.6%). Altogether, this resulted in an increase in the number of employees by 3.3% in hotels and catering and 1% in commerce, the latter after ten consecutive years of decline. The progressive recovery of tourism and commercial activity was also reflected in the Chamber's surveys, with assessments of business activity that were better than in 2015. The surveys also indicate an acceleration in the growth in turnover in hotels (6.1%) and a small increase in commerce (0.9%), which had not happened since 2001.

The finance subsector was the only branch of services which saw a negative trend, as already happened in 2015. Official GDP figures in 2016 show a 0.7% fall in GVA in the financial, real estate, professional and technical activities subsector, added to the fall of 0.5% seen in 2015 and contrasting with the strong growth – of about 10% p.a. in the financial and insurance branch – that it saw in the period 2012-2014. Weak activity was seen in a reduction in net lending to customers (-0.4%) and deposits (-2%), resulting in a fall in profits in the banking sector, for the third consecutive year, by 7.5%, and a cut in employment for the whole of the financial and insurance sector (-0.7%). In any case, we must look at this within the special context that marked the sector over the last two years, regarding Banca Privada d'Andorra (BPA) being put into administration by the Andorran National Institute of Finance (INAF), after 10 March 2015, when the US administrative authority, the Financial Crimes Enforcement Network (FinCEN) classified Banca Privada d'Andorra, SA (BPA) as a “financial institution of primary money laundering concern”. This started the process of ordered resolution of the entity, which ended in May 2016 with its liquidation and the transfer of clean assets to Vall Banc. In any case, it can be said that the Andorran banking system has withstood all these difficulties very well and that, despite the complex national and international economic environment, the sector demonstrated its soundness and solvency throughout 2016.

The contribution of the public sector to activity in 2016 was marked by the more restrictive fiscal policy of the general administration, unlike in 2015. Specifically, growth in operating costs slowed nine tenths to 2.8%, to which was added real investment (-3.2%). This factor, together with growth in revenue, resulted in a change in direction in the settled budget balance, going from a deficit (-0.5% of GDP) to surplus (0.9% of GDP). In parallel, the communes also adopted a clearly contractionary policy, with a drop in non-financial expenses of 11.8%, among which are notably the major cut in real investment (-51.5%). As a result, the aggregate non-financial surplus of the communes almost doubled, to represent 1.7% of GDP. In this way, aggregate public sector real investment (central government plus communes) fell 17%, and growth in aggregate operating costs slowed six tenths to 2%. Therefore, the performance of the public sector as a whole was clearly restrictive, contrasting with the expansionism of 2015.

In 2016, contributions to CASS increased 2 points, going from 20% to 22%. Nevertheless, the Government warned that within the next few years it will be necessary to raise the contributions. Actuarial studies of the pension branch highlight low contributions compared with the allocated pensions. On the other hand, in the general branch, costs increase every year and the corresponding deficits are financed through transfers from the Government or increased contributions. Moreover, the demographic structure does not favour the trend in either of the two branches. Over the next few years, the population will age consistently, with the corresponding repercussions of ever-greater financing needs both in the social health field and the pensions field.

The Pension Reserve Fund had assets of close to 1,168 million euros, on 31 December. With these reserves, it is considered that the Government will have to make the first contributions from its own budget towards paying public pensions in around 2023. Spain is already doing this

in 2017, but it would be a mistake to assume that the position is convenient. A large country always has more fiscal resources than a country like Andorra, which also has tax competitiveness as a strategic position.

Our tax burden reached 25.3% of GDP in 2016. This tax burden is in line with that of other European countries. In 2015, Ireland had a tax burden of 24.4% and Switzerland 28.1%, and other countries, like Latvia and Lithuania, were above 30%. In recent years, the tax burden has been increasing as various tax systems have been put in place. This process is deemed to have ended with the IRPF (Personal Income Tax) in 2015. With balanced government annual finances and the communes, if they follow the current trend, balancing their finances and even entering a phase of cutting debt, the tax burden could remain at current levels, depending on the above-mentioned spending risks linked to financing health and pensions and any additional public investment needs that might occur.

As for the prospects for the Andorran economy in 2017, the results of the Chamber's surveys suggest another, moderate improvement, allowing for confidence in the gradual consolidation of the economic recovery. By sectors, it is expected that the improvement trend will reach all branches of activity, but with different intensities. The hotel sector will continue to lead the recovery, while the rate of activity will pick up more slowly in commerce and industry. So, in all three sectors, positive replies about the trend in turnover and investment in 2017 exceed negative ones, with a more notably favourable difference in the case of hotel activity. For its part, construction is the sector which still poses doubts about the future, even though growing dynamism in the rest of the economy should also encourage activity in this sector.

In 2017, we can also trust that the impetus from the foreign sector will continue to favour Andorran economic activity, considering the high level of dynamism predicted in the Spanish economy and, to a lesser extent, in other European countries. In this context, it is expected that Andorra's economy will see a new increase in GDP in 2017, which will probably exceed the growth rate in 2016.

GDP data for the first quarter are consistent with this forecast, as they show acceleration in the interannual growth rate to 1.9%, seven tenths more than in the previous quarter. The improvement has been generalised over the sectors, except agriculture, and the growth leader is still the subsector of commerce, hotels & catering, transport, information and communications (4.8% interannual). Also positive is the upturn in financial, real estate, professional and technical activities (0.6%), after seven consecutive negative quarters.

Developments in the available main indicators of activity for the first few months of 2017 also support a forecast of higher economic growth, with a quite generalised upward trend, although within still moderate levels. Employment grew close to 3% over the first four months of the year, more than the 1.6% increase seen in the same period of 2016, with a notable contribution from the hotel sector. Along the same line, total imports, those of building materials and car registrations accelerated until June. Moreover, growth in the number of visitors, another key indicator for assessing Andorran economic activity, continued to be positive in the first half of the year, although the rate slowed a little against 2016. Only energy consumption stands out with a slightly negative trend, which could be influenced by other factors not directly linked to the economic cycle.

So, the overall view allows us to conclude that the recovery in the Andorran economy will continue to become more sound over the whole of 2017, led by the tourism sector and favoured by the good performance of the European economy, especially Spain.

Finally, as in every year, I would like to express my thanks personally and as president of the Chamber, to all those who make the preparation and editing of this report possible, which this year reaches its twenty-second edition. The report is born of both the legal obligation of the Chamber and its

desire to serve the national economy. Many thanks, therefore, to the businesses whose periodical, constant collaboration provide the Chamber with relevant information about the business climate and business activity. Our thanks also to the Government and the communes for the information they provide, especially statistics, and the institutions and associations for the same reasons. Thirdly, our thanks to the internal and external experts who gather all the information and draw up this report. Finally, many thanks to all the media for diffusing the content of this document.

Marc Pantebre Palmitjavila
President

The Principality of Andorra

The aim of this introductory chapter is to describe features which, although normal for Andorrans, may appear unusual to visitors or entrepreneurs from other countries who settle in Andorra. The quality of life in Andorra is not just a matter of economic development. The surroundings, climate, cultural integration, composition of the population, education systems, citizen security, infrastructures, environment and a whole range of other factors are essential to making Andorra a good place to live in and pursue economic activities.

Andorra's origins and history have made it unique.

In recent years, this country has been making a major effort to adapt to international standards and become an attractive centre for entrepreneurs who value not only the above-mentioned elements but also Andorra's other strong points, such as legal certainty, institutional stability, the safety and internationalisation of the financial system, tax competitiveness that is compatible with double taxation agreements, etc. Many of these matters are dealt with in detail in the *Economic Report*.

To a large extent, Andorra's singularity is the product of its origins and history, which have enabled Andorra to avoid the upheavals suffered by the rest of Europe over the centuries. Few countries, or possibly no other country in Europe, have kept their frontiers intact and safe from war throughout their history.

This first chapter therefore serves as an introduction, to situate readers who do not know our country and awaken their interest to discover more about it.

Territory and population

The Principality of Andorra lies between Spain and France. On the Spanish side, Andorra borders Catalonia, and on the French side, the Occitanie region. The nearest large cities in Spain and France are Barcelona and Toulouse, at a distance of 197 km and 185 km, respectively.

The territory of Andorra covers an area of 468 km², with a population of 73,105. Most of the population is concentrated in Andorra la Vella and Escaldes-Engordany. The population density is low, but being an enclave in the Pyrenean mountains, it is mostly high mountain, so people tended to build towns only at the bottom of valleys.

POPULATION, SURFACE AREA AND DENSITY BY PARISH 2016

	Estimated population	Surface area km ²	Density inhob/km ²
Canillo	3,670	121	30
Encamp	10,963	74	148
Ordino	4,577	89	51
La Massana	9,318	65	143
Andorra la Vella	21,672	12	1,806
Sant Julià de Lòria	8,857	60	148
Escaldes-Engordany	14,048	47	299
Total	73,105	468	156

The valleys are Y-shaped and follow the bed of the rivers Valira d'Orient (in the parishes of Canillo and Encamp) and Valira del Nord (in the parishes of Ordino and La Massana), which flow together at Escaldes-Engordany to become the river Gran Valira, or just Valira, which then continues south through the parishes of Andorra la Vella and Sant Julià de Lòria and into Spain.

Andorra is a mountainous country, mostly oriented towards the Mediterranean. This, together with its height, endows the country with a very pleasant climate. Temperature extremes

are softened in summer and winter by the dry climate, which is balanced by abundant water from numerous springs and the melting snow that accumulates over winter. The central parishes, where most of the population is concentrated, are at a height of around 1,000-1,100 metres, although there are also towns at about 900 metres, such as Sant Julià de Lòria, near the Spanish border, and at 2,100 metres, such as Pas de la Casa, near the French border.

The administrative divisions of Andorra are seven parishes and the parish administration is called *Comú*. They own the immense majority of the land and, in the past, held most of the administrative powers. They currently possess political and administrative prerogatives as a local government body, although they still bear an important political weight, and political balances also take territorial balances into account.

As for the population, for centuries and until the beginning of the 20th century, Andorra had between 5,000 and 6,000 inhabitants, but the migratory flows that started with economic growth, based on commerce and tourism, in the middle and at the end of the 20th century, led to major demographic growth. Andorra had poor connections to the outside world until well into the 20th century, with subsistence and livestock farming, needing “concessions” from neighbouring countries to avail itself of some essential goods. In those years, Andorrans emigrated to Spanish and French cities.

The registered population at the end of 2016 was 78,264, although it is estimated that the real population is 73,105. By nationality, Andorran nationals predominate, representing half of the estimated population (50%). Other large groups of nationals are the Spanish (24.7%) and Portuguese (12.6%). The French represent 4.1% of the total and other nationalities make up the other 8.6%.

The capital of the Principality is Andorra la Vella and the official language is Catalan. Spanish and French are also spoken, both for demographic and geographical reasons and because three public education systems exist side-by-side (the Andorran, Spanish and French). For demographic reasons, Portuguese is also often used. Andorra's official currency is the euro but, as it has never had its own currency, the Andorran financial system is adapted to any currency.

GEOGRAPHICAL LOCATION OF ANDORRA



MAP OF ANDORRA'S TERRITORY



Origins and institutional organisation

Although it is difficult to pinpoint its origins in history, the Greek historian, Polybius, in the year 150 B.C., wrote about the battles fought by the Carthaginian conqueror, Hannibal, on his way through the Pyrenees, and mentioned the “Andosins”.

Historically, it is told that the unique political status of Andorra evolved in the 13th century, when two agreements were signed in 1278 and 1288, called *Pariatges*, ending the rivalries that existed between the Bishop of Urgell and the Count of Foix over ownership of the Andorran lands.

Traditionally, it originated several centuries before the signing of the *Pariatges*. The national anthem of the Principality of Andorra begins: "Great Charlemagne, my father, will free me from the Saracens" and later states: "I am the only remaining daughter of the Carolingian empire".

In Andorran tradition, great importance is given to the figure of this emperor, although history tells that it was his grandson who started to take decisions about the Andorran territory and institutions.

On the southern frontier of the empire, Charlemagne reconquered a series of territories from the Saracens (Arabs) and created the counties of Rosselló, Empúries, Besalú, Barcelona, Cerdanya, Pallars and Urgell. This series of territories was known as the Spanish March. On the death of Charlemagne, his son Louis I, the Pious, succeeded him and after him, the empire was divided between his children (Charlemagne's grandchildren) in the Verdun treaty in 843. France of today and the area bordering the Arabs was assigned to Charles II of France (Charles the Bald).

Sunifred I of Urgell, Count of Urgell during the years 838 - 848, foiled an offensive started by the Arabs in 842 with the intention of conquering territories up to Narbonne, so Charles the Bald made him count and marquis of a whole series of territories, from Barcelona to Agde and confirming his position as Count of Cerdanya and Urgell. These were the links between Charlemagne, the expulsion of the Arabs and the counts of Urgell.

At the act of consecration of the Cathedral of Urgell in 839, among the 279 territories belonging to the Bishopric appear the six original Andorran parishes, plus Santa Coloma, so the parishes of Andorra already existed at least 1,178 years ago.

When the Carolingian dynasty expired, the County of Urgell (and Barcelona) acquired true independence and, over time, the counts of Barcelona focussed their attention on their southern border, fighting the Arabs and ceding rights over the Pyrenean territories to barons and viscounts and also the Bishopric of Urgell. In 1133, the Count of Urgell, Ermengol VI, ceded all his rights over Andorra to the bishop, Pere Berenguer.

The Bishop of Urgell infeudated his rights to the trusted Viscount of Caboet but, over the years, these rights passed through marriage alliances to the House of Castellbò first, and then the House of Foix.

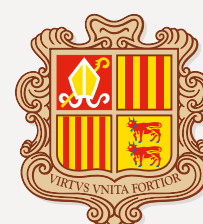
Throughout the 13th century, there were disputes between the Bishop of Urgell and the Count of Foix over the Andorran territory. Finally, to solve the dispute, they made a "parity deed" by signing the *Pariatges* in 1278.

In the 14th century, the houses of Foix and Bearn were joined. The Count of Foix, Roger Bernat III, married the daughter of the Viscount of Bearn and their son inherited the rights to the houses of Caboet, Castellbò, Foix and Bearn. It was then that the series of heraldic symbols were combined into the Andorran coat of arms: the Bishopric of Urgell, County of Foix, the Catalan counts and the Viscount of Bearn.

FLAG OF ANDORRA



COAT OF ARMS OF ANDORRA



The Pariatges of 1278 gave the country the status of indivisible condominium of the two lords (the Bishop of Urgell and the Count of Foix), a situation that has endured until today, although the rights of the Count of Foix passed first to the King of France and then to the President of the French Republic.

An example of political stability, at the heart of Europe, throughout the centuries.

We have emphasized Andorra's long history here because it was the co-principality's genesis that enabled Andorra to remain a neutral country over the centuries, under the protection of the two great surrounding countries.

In 1419, the *Consell de la Terra* (Council of the Land) was created, one of the oldest parliaments in Europe, in which the parishes were represented. More than 400 years later, in 1866, the so-called New Reform was passed, which democratized the institution. With these changes, the Council came to be composed of four councillors for each parish and all heads of house had the right to vote (until then, only the grand families could). In 1933, all male Andorrans over the age of 25 gained the right to vote. Women were given the right to vote in 1970. The legal age became 21 in 1971 and 18 in 1985.

At the beginning of the 20th century, Andorra's communications with the outside world were poor. It was not until 1913 that the road from La Seu d'Urgell to Andorra la Vella was opened, and surfaced in 1949. In 1935, electricity production began under the condition that the company holding the concession (FHASA) was to build a road from Andorra la Vella to the French border, which was surfaced in 1959, and the road from Andorra la Vella to La Massana and Ordino.

From the 1930s on, the arrival of the first foreign visitors heralded a certain amount of transit on Andorra's roads and the first hotels and shops opened. When the two neighbouring wars broke out, the Spanish Civil War and the war in Europe, many refugees arrived and crossed the country, fleeing from one side to the other, given Andorra's neutral status. The flow of visitors increased, but until 1959, it was not easy to cross Andorra from one border to the other. Then, the tourism phenomenon began in earnest, which is still the basis of the Andorran economy today.

Despite the problems of access, Andorra's name was well-known everywhere thanks to Radio Andorra, which opened in 1939 and broadcast until 1981. Its power and commercial programming meant that people listened to it far and wide.

SOME SIGNIFICANT DATES AND EVENTS WHICH SHAPED THE ANDORRA OF TODAY:

- In 1956** the first ski-lift is installed at Pas de la Casa and a few years later others are installed at Grau Roig (1959) and Soldeu (1963).
- In 1967** the Andorran Telecommunications Service (STA) is set up, now called Andorra Telecom.
- In 1968** the Andorran Social Security System (CASS) is set up, which finances public health and pensions through contributions from workers and businessmen.
- In 1973** Arinsal ski resort opens.

- In 1978** the *quart* (administrative sub-division) of Escaldes-Engordany separates from the parish of Andorra la Vella and Escaldes-Engordany becomes the seventh parish of the Principality.
- In 1982** Pal ski resort opens.
- In 1983** Ordino-Arcalís ski resort opens.
- In 1988** the Government buys FHASA (Forces Hidroelèctriques d'Andorra, SA.), the private company which brought electricity to the country in the 1930s and built the road to the French border and the valley of La Massana and Ordino, and creates its own company FEDA (Forces Elèctriques d'Andorra).
- In 1991** the Customs Union Agreement with the European Economic Community is signed. This agreement is still in force, although it is currently in a phase of negotiation for an association agreement which would grant Andorra the right to participate in the EU's domestic market, horizontal policies and accompanying measures, and above all, will bring Andorra into the main nucleus based on the four freedoms of movement (goods, persons, services and capital).
- In 1993** the Constitution is approved. The Andorran people assume full sovereignty and the co-princes see a reduction in their powers, despite being the joint, indivisible head of state. Andorra is bestowed with a Constitution that institutionalises the system of parliamentary co-principality and defines the separation of the three powers: legislative power, exercised by the Consell General; executive power, exercised by the Government, and judicial power, headed by the Supreme Council of Justice. In the same year, Andorra becomes part of the UN.
- In 1994** Caldea spa opens. This is now a major tourist attraction.
- In 2003** the trilateral agreements between Andorra, France and Spain come into force, regulating the entry, movement, residence and settlement of their nationals, and movement and residence of nationals from third-party states. Also in 2003, the operating company for La Rabassa snow resort is set up (Camprabassa, SA).
- In 2004** the Agreement on taxation of savings income is signed between the European Community and the Principality of Andorra. This agreement will cease to be effective from 2017.
- In 2005** the European Social Charter enters into force.
- In 2008** the Convention with Portugal relating to the entry, movement, residence and settlement of its nationals, and the Convention between Andorra and the Holy See come into force.
- Over the period 2009-2011** Andorra signs bilateral tax information exchange agreements with nineteen countries, including Spain and France. On 30 June 2011, the Principality of Andorra signs the monetary agreement with the European Union to make the euro Andorra's official currency.
- In 2012** Law 10/2012 on foreign investment in the Principality of Andorra is passed, opening up foreign investment. In the same year, Andorra signs a tax information exchange agreement with Poland.
- In 2013** a Double Taxation Agreement (DTA) is signed with France and a tax information exchange agreement with the Czech Republic.
- In 2014** Andorra coins its first Andorran euros. A DTA with Luxembourg and two tax information exchange agreements with Switzerland and the Republic of Korea are signed.
- In 2015** a tax information exchange agreement is signed with Italy and four DTAs, with Spain, the U.A.E., Portugal and Liechtenstein. Andorra's first agreement on the mutual protection of investments is signed with the U.A.E.
- In 2016** the DTA with France is implemented (from January 1) and the DTA with Spain (from 26 February). On February 12, Andorra and the European Union sign an automatic tax information exchange agreement. On 20 September, a DTA is signed with Malta.

The main Andorran institutions are:

Head of State (the Co-Princes): the Constitution defines the figure of the Co-Princes as the joint, indivisible Head of State of Andorra. They are, personally and exclusively, the Bishop of Urgell and the President of the French Republic. They are the symbol and guarantee of Andorra's independence and its equal treatment in relations with the neighbouring states. They are arbitrators and moderators of public power and the institutions. Currently, the episcopal Co-Prince is Mons. Joan Enric Vives Sicília, and the French Co-Prince is Mr Emmanuel Macron.

The Parliament (*Consell General* or *General Council*): This is the legislative assembly of Andorra, the supreme representative body of the people, made up of a single chamber. Members of parliament are elected by universal suffrage for a period of four years. Currently, parliament consists of 28 members, who are elected through a mixed system: half are parish candidates and the other half are national candidates.

The body which governs the Council is the *Sindicatura*, headed by the *síndic* and *subsíndic*. The current *síndic general* is Mr Vicenç Mateu Zamora and the *subsíndic general* is Ms Mònica Bonell Tuset.

The Executive (*Govern*): holds the State's executive power. It directs Andorra's national and international policy and administration of the State. Its mandate is four years. It consists of the Head of Government (elected by the General Council and appointed by the co-princes), and the ministers (appointed by the Head of Government). The current Head of Government is Mr Antoni Martí Petit.

The communes (*Comú* /pl. *Comuns*): These are the local authorities in each parish. Andorra is made up of seven parishes: Canillo, Encamp, Ordino, La Massana, Andorra la Vella, Sant Julià de Lòria and Escaldes-Engordany. Communes are public corporations with broad local powers. They are run by the *cònsol major* (mayor), *cònsol menor* (deputy mayor) and councillors.

Justice: Judicial power is exercised through three jurisdictions – civil, administrative and criminal. Decisions made by first instance courts – *Batlles* (magistrates) and the *Tribunal de Corts* (Criminal Court) – can be appealed at a second instance court, the Supreme Court of Justice, which is the highest instance in Andorra's judicial system.

Foreign investment

On 19 July 2012, Law 10/2012 on foreign investment in the Principality of Andorra entered into force, which involved opening up and liberalising the Andorran economy to foreign investment, with the aim that Andorra would become a competitive, attractive destination for investors. This Law, among other aspects, suppressed the sectoral restrictions provided in the previous Law 2/2008, of 8 April, on foreign investment in the Principality of Andorra. This meant, in practice, opening up all activities to foreign capital, while protecting Andorra's strategic interests, so the Government can refuse foreign investment, as long as it provides legal grounds.

Taxation and social security

The Andorran taxation system is intended to be easily implemented and offer competitive rates compared with other jurisdictions. The liberalisation of foreign investment, combined with the signing of double taxation agreements and application of a more advantageous direct and indirect tax system than surrounding countries, is intended to position the Andorran economy where it can compete with neighbouring economies, making Andorra an attractive destination for new sectors and businesses.

At national level, the current taxes are:

Company tax (IS): Direct tax on the income of legal persons. The general rate is 10%. There are deductions for double taxation, job creation and investment. The dual domestic-international tax on shares in profits from other entities is eliminated.

Personal income tax (IRPF): Direct personal tax on income obtained by resident natural persons based on the amount and their personal and family circumstances. The general rate is 10%, with total exemption up to 24,000 euros and a partial discount between 24,000 and 40,000, at a rate of 5%.

Tax on non-residents' income (IRNR): Direct tax on non-resident natural and legal persons. The general rate is 10% (5% in the case of royalties) for residents in countries with which no double taxation agreement has been signed.

Indirect general tax (IGI): Indirect consumption tax on deliveries of goods and provisions of services carried out by businessmen or professionals, and also on imports of goods. The general rate is 4.5%. For specific transactions, the following rates are applied: "super-reduced" (0%), reduced (1%) or a special rate (2.5%). There is also a higher rate (9.5%) for transactions provided by banking and financial services.

Indirect tax on insurance services (ISI): Tax on the provision of insurance services covering risks of all kinds, at a rate of 4%. The social security system and capitalisation products, such as pension funds, retirement plans and other such products, are not subject.

Savings income tax: Tax at source on interest payments made by paying agents established in the Principality of Andorra to beneficial owners who are natural persons resident in one of the member states of the European Union. 35% withholding tax is applied. This tax will be withheld for the last time in 2017 (applied on income obtained in 2016), as it will disappear with the arrival of full tax transparency with European Union countries.

Special taxes: Applied to specific products, such as alcohol, tobacco and fuels. These taxes are applied to imports and manufacturing (domestic market) of these products. The tax varies according to the product.

Property transfer tax (ITP): Tax on transfers of assets *inter vivos* for or without a consideration. The tax base is the real value of the assets which are transferred or assigned. The rate is 4% (3% to the Comú and 1% to the state).

Capital gains tax on property transfers: Tax on the increase in value of property which appears on *inter vivos* property transfers for or without a consideration, and on setting up or assigning in rem rights over the properties. The tax rate varies according to the number of years which the property has been owned by the taxpayer (from 15% for up to one year to 0% over 10 years).

Consumption tax (Customs regime): Customs right applied to agricultural products imported into Andorra (products 1 to 24 of the harmonised system, which are not covered by the Customs Union agreement). The amount payable varies from 0% to 3% according to the imported good. There are some products with higher tax rates, such as some live animals, alcohol and tobacco.

Other taxes: tax on the Registry of Owners of Economic Activities, vehicle ownership tax and Trademark Registry tax.

At Comú level, the main taxes and rates are:

Traditional *Foc i Lloc*: Tax on residence in a parish. Paid by natural persons, aged between 18 and 65, registered in a parish. The tax liability is a fixed amount that varies according to the parish.

Tax on built property: This taxes ownership of a built property or in rem right of use of the property. Calculated from the m² surface area of the property and its location (tax applied per m² built varies according to the parish).

Tax on rental income: Tax on income from property rental. A percentage of the total value of the income obtained in a year (varies according to the parish).

Tax on location of commercial, business and professional activities: Tax on commercial, business or professional activities. Calculated on the basis of the type of activity, location of the establishment and m² surface area used.

Rates: The Comú may establish taxes, within their tax regulations, for providing public services for public health, lighting, maintaining public spaces, towing services, drains and drinking water connections, etc. They may also set up taxes for carrying out the following administrative functions: planning permissions, licences for opening businesses, issuing certificates, etc.

On the social scale, obligations are:

Affiliation to the Social Security System (CASS) is mandatory for all waged and self-employed workers.

Employees contributions involve a charge of 22%, 6.5% of which is paid by the employee and the other 15.5%, by the employer. Contributors over the age of 65 who choose to continue working despite receiving the pension only pay the general branch, with a charge of 10%, 3% of which is paid by the employee and 7% by the employer.

Self-employed contributions involve a charge of 22% of the monthly global average wage paid by employees to the CASS in the previous calendar year (10% if working while in receipt of their pension and only paying the general branch).



The external environment of the Andorran economy

Developments in the global economy

1. The main features of economic development in 2016

In 2016 and the first few months of 2017, analyses of the international environment combine two aspects: firstly, macroeconomic

The rate of world economic growth has slowed two tenths, to 3.2%.

forecasts suggest a gentle improvement in the prospects of recovery in terms of indicators of gross national product, after 2016 data showed a certain trough compared with previous years. On the other hand, circumspection and warnings are frequent about the risks and fragility of the recovery, owing to financial economic, sociopolitical and geostrategic considerations. An additional aspect is a certain turning point in trends, which had been downward until then, including the behaviour of interest, inflation and developments in international trade. The title of the OECD *Interim Economic Outlook* in March 2017, *Will risks derail the modest recovery?*, was explicit about financial vulnerabilities and political risks. Also evident is the change in perceptions between the title of the IMF's *World Economic Outlook* in April 2016, *Too slow for too long*, focussing on the weakness and delay in the recovery, and the more positive tone of the April 2017 issue's title *Gaining momentum?*, despite the question mark. In June 2017, the World Bank highlighted the fragility of the recovery in its *Global Economic Prospects*, contrasting the improvement in trade with investment weaknesses.

So, in relation to macroeconomic data, the updated data in the IMF's *World Economic Outlook* in July 2017 gauged growth in the global economy in 2016 at 3.2% - two tenths lower than in 2015, and the lowest since 2009 - also below the predictions made by international bodies at the beginning of 2016. However, outlooks indicated a certain turning point, predicting 3.5% for 2017 and 3.6% for 2018. In general, these estimates agree with those prepared by the OECD in June 2017: 3.0% for 2016, 3.5% for 2017 and 3.6% for 2018.

Table 1.1 shows the IMF figures and outlooks for the global economy as a whole, and also the breakdown of advanced economies in comparison with emerging and developing economies. The slowdown in 2016 would have been mainly due to the smaller contribution from advanced economies, especially in the first part of the year. In 2016, this helped to reverse the trend of previous years, narrowing the gap between both groups of economies.

GLOBAL ECONOMIC GROWTH 2012-2018 (% of GDP)

	2012	2013	2014	2015	2016	2017 (p)	2018 (p)
Global economy	3.5	3.4	3.5	3.4	3.2	3.5	3.6
Advanced economies	1.2	1.3	2.0	2.1	1.7	2.0	1.9
Emerging and developing economies	5.4	5.1	4.7	4.3	4.3	4.6	4.8

(p) projections

Source: IMF, *World Economic Outlook*, July 2017.

Figure 1.1 shows two trends: on the one hand, as in 2016, it shows a certain trough at which a turning point is expected, with global GDP rising slightly. On the other hand, some stabilisation in the contributions to growth from the advanced economies and a degree of recovery in the role of emerging and developing economies (EMDE) which, beyond any debate about China's deceleration, mentioned below, are seeing a degree of revival.

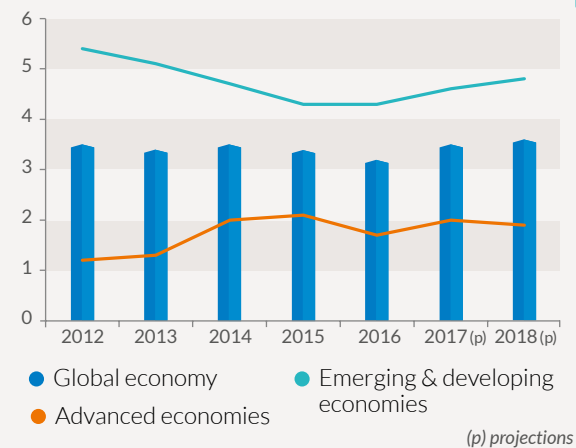
But these moderately optimistic figures are being taken cautiously with regards to increased uncertainties and risks.

Among the economic and financial unknowns are notably a slowdown in international trade that has been seen in growth rates since 2012, well below the average of recent decades, and also certain doubts about the subsistence and potential reappearance of financial fragility in advanced economies, especially China.

Among the social and political unknowns, we must consider that frictions and social discontent led to results that some felt surprising, such as the positive result of the referendum for the United Kingdom to leave the European Union, and the election of Donald Trump as president of the United States. These events have created expectations about what could happen in 2017, although the results of elections in the Netherlands and France were more reassuring. Questions also arise over the interactions between the United States, China and Russia mostly, with risks of trade friction in the event of protectionist or other measures materialising. It is notable how the main studies

GLOBAL GROWTH: ADVANCED AND EMERGING ECONOMIES (% of GDP)

Figure 1.1



Source: IMF, *World Economic Outlook*, July 2017.

Box 1.1

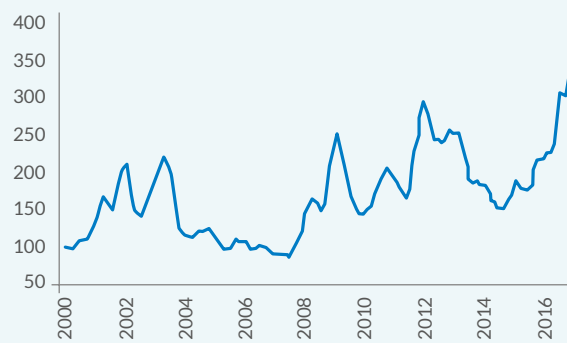
MEASURING UNCERTAINTIES

The World Bank report *Global Economic Prospects 2017*, published in January of this year, includes a diagram showing an uncertainty index, which stands at highs at the end of 2016 and start of 2017, even when compared with other delicate moments since the beginning of the 21st century.

From the reports published every half-year by the IMF, in April 2017 the Fiscal Monitor also included a specific reference to the concept of uncertainty based on the "Economic Policy Uncertainty" index formulated by Baker, Bloom and Davis (2016). The authors' proposal showed the impacts of uncertainties, measured by their indicator, on market volatility and on particularly sensitive components of demand. The website <http://www.policyuncertainty.com/> provides a continuous follow-up of the results of applying the index.

UNCERTAINTY INDEX, ACCORDING TO THE WORLD BANK

Index, Jan. 2000 = 100



Source: World Bank, *Global Economic Prospects 2017*, January 2017, p. 6.

by international bodies since the start of 2017 systematically include not only references to the high levels of uncertainty but also proposals to quantify them, as can be seen in box 1.1.

As for inflation, the most notable recent trend is the progress towards *normalisation* in advanced economies, after a few years in which they bordered negative rates, with the spectre of deflation in some countries. As shown in figure 1.2, the most recent data (2016 and outlooks for 2017) indicate modest positive values. The IMF's outlook update in April 2017 indicates a consumer price variation of 2.0% in 2017 for all advanced economies, significantly higher than the 0.3% in 2015 and 0.8% in 2016. This normalisation of inflation rates is also one of the arguments for speaking of *normalisation* in monetary policy, especially in the United States.

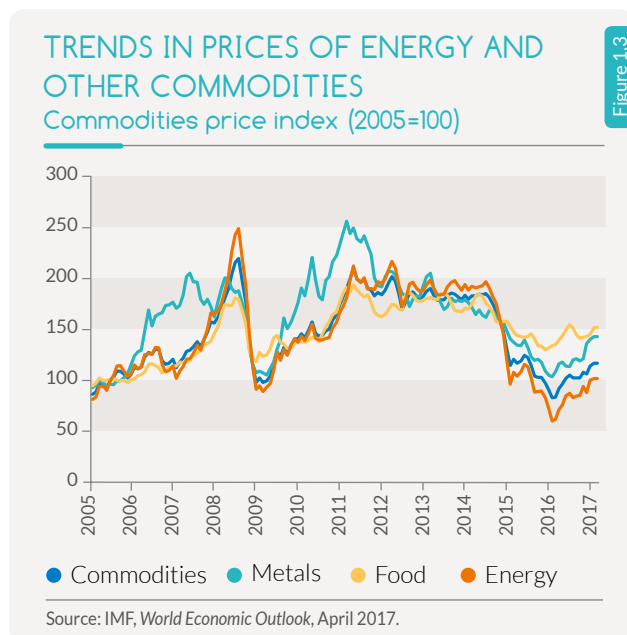
One of the factors that may be encouraging the return to normal levels of inflation rates is a degree of recovery in oil prices and other commodities since 2016, shown in figure 1.3. The technological and geopolitical factors which, added to strictly economic ones, lie behind the behaviour of oil prices in recent years, make it difficult to make forecasts, but continuity in these moderate price figures may also encourage a moderate inflation dynamic, avoiding deflationary risks.

The low prices of oil and other major commodities for production processes have been defined as one of the components of the "tailwinds" which support a recovery in the global economy. The risk of a sudden reversal, upwards, of these prices, converting them into a feared "headwind", seems unlikely, although they are one of the elements of potential risk associated with geostrategic tensions.

2. Developments in the major advanced countries and the EU

The major trends in the global economy as a whole and in the major groups of advanced and emerging economies show developments with notable variations. So, among the advanced economies, after 2016, in which GDP growth was a modest 1.7% - down from 2.1% in 2015 - the figures expected for 2017 are 2.0% (IMF), with forecasts a tenth lower for 2018.

Advanced economies have grown 1.7%, lower than the increases recorded in 2014 and 2015.



substantially with the European Central Bank's projections (2017), of 1.9% for 2017 and 1.8% for 2018. As for the United Kingdom, growth of 1.8% in 2016 was also lower than in 2015, although analysts highlight the fact that the initial impacts of the vote in favour of Brexit – in June 2016 – were not as negative as expected. Nevertheless, the forecasts of lower economic growth remain. This also occurs in the case of Japan.

For advanced economies, as a whole, the main economic driving force in 2016 was family consumption. This was the case of the Spanish economy. In contrast, France showed different behaviour, as commented below, with difficulties reactivating investment. The forecasts for 2017 are, on the whole, for more similar contributions from these two large items of private demand (consumption and investment).

In the case of the United States, there is anticipation about how the economic policies of the Trump Administration will materialise: most analysts anticipate more expansionary fiscal policy with stimulus impacts from growth in the short term, but there is a greater division of opinion regarding the medium and long-term impacts on public sector debt.

We must also watch the impacts on the dollar exchange rates – which began to appreciate after the November 2016 elections – and whether they might affect the competitiveness of products from the United States, as occurred at the beginning of the 1980s. The appearance of protectionist measures is another feature that coincides with the current forecasts clearly formulated by the new Administration.

IMF ECONOMIC OUTLOOKS FOR THE GLOBAL ECONOMY (%)

	2015	2016	2017 (p)	2018 (p)
Advanced economies	2.1	1.7	2.0	1.9
United States	2.6	1.6	2.1	2.1
Eurozone	2.0	1.8	1.9	1.7
United Kingdom	2.2	1.8	1.7	1.5
Japan	1.1	1.0	1.3	0.6
Emerging economies	4.3	4.3	4.6	4.8
China	6.9	6.7	6.7	6.4
India	8.0	7.1	7.2	7.7
Russia	-2.8	-0.2	1.4	1.4
ASEAN-5 ⁽¹⁾	4.9	4.9	5.1	5.2
Latin America	0.1	-1.0	1.0	1.9
Sub-Saharan Africa	3.4	1.3	2.7	3.5
Global economy	3.4	3.2	3.5	3.6

(1) Philippines, Indonesia, Malaysia, Thailand and Vietnam.
(p) projections

Source: Prepared from the Database of the World Economic Outlook, IMF, July 2017.

Regarding unemployment, the recovery after large rises in unemployment in the 2008-2009 crisis is notable, but the gap is also notable between the United States which has practically returned to pre-crisis levels and a Eurozone where – despite improvements in 2014 – a still significantly higher level of unemployment prevails. On this subject, we comment in box 1.2 on the risks of underestimating the labour factor.

Box 1.2

UNEMPLOYMENT AND THE UNDERESTIMATION OF THE LABOUR FACTOR IN ADVANCED ECONOMIES

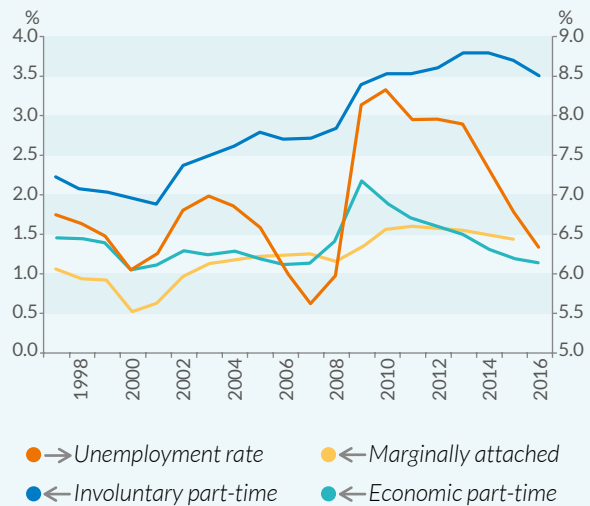
Developments in unemployment are important both economically and sociopolitically. From an economic perspective, unemployment is the most obvious symptom of underutilisation of resources with productive potential; but, moreover, high unemployment rates cause dissatisfaction, unrest and potential social and political friction.

One of the specific reasons for the growing attention to developments in unemployment is the realisation that, despite recent improvements in aggregate data, neither upward pressure on wages nor a proportional improvement in some social welfare indicators can be seen.

In response, in recent months all bodies have come together to present measurements of utilisation of the labour factor – specifically underutilisation of this factor – going beyond the traditional unemployment rate. Normally these additional indicators refer to aspects such as “discouraged” or just “marginally attached” workers (those who are willing to work but no longer try if the outlook is pessimistic, and therefore do not figure as unemployed) and currently, in a special way, refer to the population in involuntary part-time work, i.e., who want to work full-time but are unable.

Among all the abundant recent sources on these focuses, the following diagram depicts the indicator formulated by the OECD which, as well as the unemployment rate, presents data on the “marginally attached” population and, above all, differentiates between part-time economic employment (justified by the characteristics of the jobs and persons occupying them) and involuntary part-time employment which,

INDICATORS OF LABOUR UNDERUTILISATION IN OECD COUNTRIES



Source: OECD, *Economic Outlook*, June 2017.

as shown in the figure, recently reached very high levels in all OECD countries.

These broader indicators of the situation in the labour markets are gaining ground for the above-mentioned reasons: a) they offer more fundamental information about the degree of underutilisation of potential labour productivity; b) they enable interpretation of the situation of continued oversupply in labour markets that limits wage raises; and c) they help to explain why the recovery in some classic macroeconomic indicators, such as GDP or the unemployment rate, does not result in the elimination or proportional reduction of unrest and/or sociopolitical friction.

Every year, the World Bank prepares the *Doing Business* ranking, evaluating the ease of doing business in 190 countries through the regulations applied to small and medium-sized businesses throughout their life. This ranking is made by considering 10 variables that measure “ease of doing business”.

In table 1.3 we have included major countries in different geographical areas. The highest value in this sample in 2017 was the United Kingdom in 7th place. The top six in the 2017 ranking are, in this order: New Zealand, Singapore, Denmark, Hong Kong, South Korea and Norway.

DOING BUSINESS RANKING 2017

Table 1.3

Country	Ease of doing business (ranking)	1 2 3 4 5 6 7 8 9 10									
		1	2	3	4	5	6	7	8	9	10
United Kingdom	7	16	17	17	47	20	6	10	28	31	13
USA	8	51	39	36	36	2	41	36	35	20	5
Germany	17	114	12	5	79	32	53	48	38	17	3
Portugal	25	32	35	50	27	101	70	38	1	19	7
France	29	27	20	25	100	82	32	63	1	18	24
Spain	32	85	113	78	50	62	32	37	1	29	18
Japan	34	89	60	15	49	82	53	70	49	48	2
Russia	40	26	115	30	9	44	53	45	140	12	51
Mexico	47	93	83	98	101	5	53	114	61	40	30
Italy	50	63	86	51	24	101	42	126	1	108	25
China	78	127	177	97	42	62	123	131	96	5	53
Brazil	123	175	172	47	128	101	32	181	149	37	67
India	130	155	185	26	138	44	13	172	143	172	136

1: Starting a business; 2: Dealing with construction permits; 3: Getting electricity; 4: Registering property; 5: Getting credit; 6: Protecting minority investors; 7: Paying taxes; 8: Trading across borders; 9: Enforcing contracts; 10: Resolving insolvency.

Source: World Bank.

We now focus our analysis on the economic situation in the European Union, taking five macroeconomic factors for reference: GDP growth, unemployment, current account balance, deficit and public debt, and observing how the data in six economies has evolved: Germany, France, Spain, Italy, Portugal and the United Kingdom.

Table 1.4 shows the trend in growth in these economies, taking GDP as an indicator. As can be seen, the European economy continues to progress, despite uncertainty. Growth in the Eurozone has resisted the episodes of financial instability and political developments of 2016 well. However, uncertainty regarding the outlook scenario is still high, especially about political risk. All the Eurozone economies recorded positive growth in 2016. GDP growth accelerated in Germany (1.8%), Netherlands (2.2%) and Austria (1.5%). In contrast, a certain cooling was seen in Belgium (1.2%), France (1.1%) and Portugal (1.4%). Spain maintained one of the highest growth rates in the Eurozone (3.2%). Outside the EMU, growth in Sweden (3.3%) and the United Kingdom (1.8%) were notable.

GDP GROWTH 2010-2018 (real variation %)

Table 1.4

	2010	2011	2012	2013	2014	2015	2016	2017 (p)	2018 (p)
Eurozone	2.0	1.6	-0.9	-0.2	1.2	1.5	1.7	1.8	1.8
Germany	3.9	3.7	0.7	0.6	1.6	1.5	1.8	2.0	2.0
France	1.9	2.1	0.2	0.6	0.7	1.2	1.1	1.3	1.5
Spain	0.0	-1.0	-2.9	-1.7	1.4	3.2	3.2	2.8	2.4
Italy	1.6	0.7	-2.9	-1.7	0.2	0.7	1.0	1.0	0.8
Portugal	1.9	-1.8	-4.0	-1.1	0.9	1.6	1.4	2.1	1.6
United Kingdom	1.9	1.5	1.3	1.9	3.1	2.2	1.8	1.6	1.0

(p) projections

Source: OECD Economic Outlook, June 2017.

These levels of GDP growth should enable very gradual absorption of unemployment, even if rates remain at very mixed levels among the major economies, as can be seen in table 1.5. So, Germany and the United Kingdom have unemployment rates under 5%; in France, it is double at 10%, and in Spain almost five times this figure at 20%, at which it ended 2016.

UNEMPLOYMENT TRENDS 2010-2018 (%)

Table 1.5

	2010	2011	2012	2013	2014	2015	2016	2017 (p)	2018 (p)
Eurozone	10.1	10.2	11.3	12.0	11.6	10.9	10.0	9.3	8.9
Germany	6.9	5.8	5.4	5.2	5.0	4.6	4.2	3.8	3.7
France	9.2	9.1	9.7	10.3	10.3	10.4	10.0	9.7	9.6
Spain	19.9	21.4	24.8	26.1	24.4	22.1	19.6	17.5	16.0
Italy	8.3	8.4	10.7	12.1	12.6	11.9	11.7	11.5	11.2
Portugal	10.8	12.6	15.5	16.2	13.9	12.4	11.0	9.7	8.9
United Kingdom	7.9	8.1	8.0	7.6	6.2	5.4	4.9	4.8	5.3

(p) projections

Source: OECD Economic Outlook, June 2017.

Another notable trend is the consolidation of highly positive current account balances, as a result of the fact that the countries which had major deficits before the crisis – such as in southern Europe – corrected them substantially (even in cases such as Italy and Spain, these have become surpluses), while the traditional countries with surpluses (such as Germany and Netherlands) have increased their positive balances. More difficulties in reducing foreign deficits can be seen in the case of France.

CURRENT ACCOUNT BALANCE 2010-2018 (in % of GDP)

Table 1.6

	2010	2011	2012	2013	2014	2015	2016	2017 (p)	2018 (p)
Eurozone	0.4	0.8	2.2	2.8	3.1	3.8	3.6	3.3	3.4
Germany	5.4	6.0	7.1	6.8	7.6	8.6	8.3	7.5	7.4
France	-0.8	-1.0	-1.2	-0.9	-1.1	-0.2	-0.9	-1.2	-1.3
Spain	-3.9	-3.2	-0.2	1.5	1.1	1.4	2.0	2.1	2.1
Italy	-3.4	-3.0	-0.4	1.0	1.9	1.4	2.6	2.1	2.3
Portugal	-10.1	-6.0	-1.8	1.6	0.1	0.1	0.8	0.4	0.8
United Kingdom	-2.7	-1.8	-3.7	-4.4	-4.7	-4.3	-4.4	-3.9	-3.8

(p) projections

Source: OECD Economic Outlook, June 2017.

As for public finances - table 1.7 - in the EMU as a whole, the public deficit fell from 2.1% of GDP in 2015 to 1.6% in 2016, and improved in all EMU countries, except Austria and Belgium. However, the situation was still mixed, as the number of countries with a fiscal surplus increased while the deficit remained very high in other countries. For example, in 2016 the surplus in Germany was 0.8% of GDP, in Luxembourg 1.6%, in Greece 0.7% (despite being 5.9% in 2015) and in Malta 1.0%; in contrast, the deficit continued to be very high in Spain (4.5% of GDP, the highest figure among European countries) and France (3.4%) and, to a lesser extent, in Belgium (2.6%), Italy (2.4%) and Portugal (2.0%).

BUDGET BALANCES 2010-2018 (in % of GDP)

Table 1.7

	2010	2011	2012	2013	2014	2015	2016	2017 (p)	2018 (p)
Eurozone	-6.2	-4.2	-3.6	-3.0	-2.6	-2.1	-1.6	-1.2	-0.9
Germany	-4.2	-1.0	0.0	-0.2	0.3	0.7	0.8	0.7	0.6
France	-6.8	-5.1	-4.8	-4.0	-3.9	-3.6	-3.4	-3.0	-2.8
Spain	-9.4	-9.6	-10.5	-7.0	-6.0	-5.1	-4.5	-3.1	-2.3
Italy	-4.3	-3.7	-2.9	-2.9	-3.0	-2.7	-2.4	-2.1	-1.4
Portugal	-11.2	-7.4	-5.7	-4.8	-7.2	-4.4	-2.0	-1.5	-1.0
United Kingdom	-9.6	-7.7	-8.3	-5.7	-5.6	-4.3	-3.3	-3.1	-2.4

(p) projections

Source: OECD Economic Outlook, June 2017.

These differences in terms of budget balance are reflected in the levels of public debt. So, in Germany a gradual reduction is occurring which could leave values close to 60% of GDP at the beginning of 2019, while France and Spain show levels closer to 100% of GDP, and Italy and Portugal easily exceed this percentage.

PUBLIC DEBT 2010-2018 (in % of GDP)

Table 1.8

	2010	2011	2012	2013	2014	2015	2016	2017 (p)	2018 (p)
Eurozone	84.4	87.1	91.7	93.8	94.5	92.8	91.7	90.4	88.9
Germany	81.1	78.8	79.9	77.4	74.8	71.2	68.4	65.3	62.8
France	81.7	85.2	89.5	92.3	95.2	96.2	96.6	98.0	98.8
Spain	60.1	69.5	85.7	95.5	100.4	99.8	99.4	99.0	98.6
Italy	115.5	116.5	123.4	129.0	131.7	132.1	132.5	131.8	130.6
Portugal	96.2	111.4	126.2	129.0	130.6	129.0	130.4	128.6	126.5
United Kingdom	76.0	81.6	85.1	86.2	88.1	89.0	89.3	88.7	88.1

(p) projections

Source: OECD Economic Outlook, June 2017.

3. Developments in the major emerging and developing countries

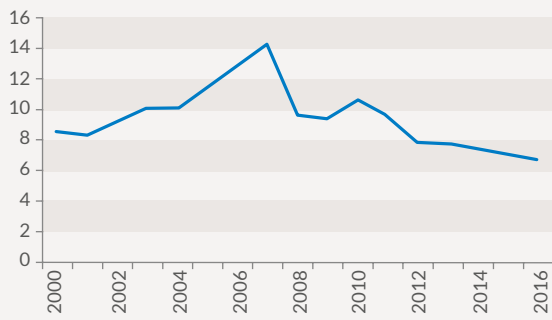
In 2016, the emerging and developing economies grew an overall 4.3%, the same figure as in 2015 which, nevertheless, halts a downward trend which occurred since 2011. The continued deceleration of China, gentler than feared at the beginning of 2016, and the problems of some major economies in Latin America, as well as of some oil and raw material exporters, are among the main factors explaining this trend, to some extent contrasted by cases of improvement in some of the so-called new driving forces of growth: including India, Bangladesh, Myanmar, Philippines or Tanzania.

Developments in China have been of particular interest. In 2016, growth was 6.7%, continuing the deceleration which began at the start of the second decade of the 21st century, as shown in figure 1.4. For 2017, forecasts for China stand at 6.7%, while for 2018, after some recent upward revisions, they stand at 6.4%.

The Chinese government insists that this is a gentle slowdown, the collateral effect of the change in model adopted after the global crisis, that it wants to give more importance to domestic demand, especially in consumption and not just investment, with an emphasis on services and not just goods. The foreign sector's contribution to growth is still positive but the size of China's foreign surplus has been falling.

GROWTH OF THE CHINESE ECONOMY (% GDP)

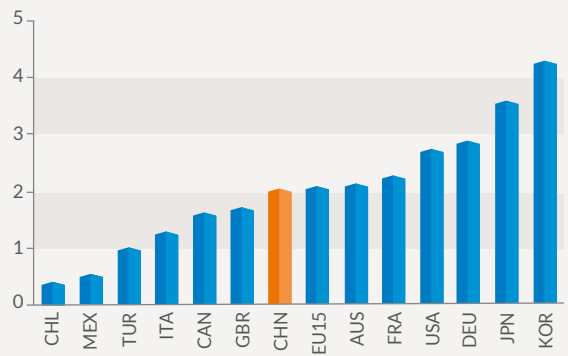
Figure 1.4



Source: OECD (2017), *Economic Survey: China*, OECD, March 2017.

SPENDING ON R+D AS A PERCENTAGE OF GDP

Figure 1.5



Source: OECD (2017), *Economic Survey: China*, OECD, March 2017.

A driving force behind the change in direction is opting for activities that generate more added value inside the country, not just coupling activities but also involvement in global value chains, with a greater contribution of *added value*. A vital part of this new strategy is, therefore, greater spending on research and development activities. The March 2017 OECD report on China includes and highlights the diagram reproduced as figure 1.5, which shows how the weighting of Chinese R+D is already on a level with the EU-15 and greater than the major western economies. The debate about the future implications of these new realities gains ground over comparative competitive positions of the major global economic agents.

In 2016, emerging and developing economies together grew 4.3%.

One of the implications of China's change of model is that its development affects the trend in international trade figures and influences the debates about the slowdown in global trade flows observed between 2012 and 2016, with the added unknown of the effect that the protectionist vision announced by the Trump administration could have, as commented in the following section.

In the case of Latin America, this region had already seen economic deceleration in the years up to the said slowdown, due to the negative effects of the collapse in prices of raw materials (many countries are exporters). In 2016, the situation in this area worsened and regional GDP fell 1.0%, the worst trend among the major global regions. Brazil, which is the leading economy in the area, continued in deep recession (with GDP falling 3.6%), causing a negative contagion to the whole area. Also notable were the falls in GDP in Argentina and Venezuela. Despite the generally negative tone, the differences between economies were significant, for example, countries such as Columbia or Mexico saw growth of 2.0% and 2.3% respectively.

For its part, the trend in GDP of the Russian economy, much punished by the low price of oil and raw materials, improved in comparison with 2015, although it remained negative (-0.2%). On the other hand, the Middle Eastern economies, North Africa and Pakistan saw growth accelerate to 3.9%, despite the trend in oil prices and the geopolitical tensions affecting the region. Finally, sub-Saharan Africa grew 1.4%, with notable deceleration compared with 2015 (when it had grown 3.4%).

4. The present and future of international trade

Since 2012, the evolution of international trade shows growth rates below the average of the decades before the crisis. Figures stand at about 2-3%, whereas they were about 5% before the crisis. References to the slowdown in trade have risen among the ranking of concerns of

Since 2012, the trend in international trade shows growth rates below the average in the decades before the crisis.

international bodies and analysts. In 2016, the OECD accompanied one of the editions of its *Economic Outlook* with a monograph on this issue in which it asked whether this was a “cardiac arrest” or simply a “dizzy spell”. The

World Trade Organisation recorded that the figures for 2016 were especially low – with growth of 1.3%, according to the press release published in April 2017 – although some symptoms seemed to indicate that the trend was improving. Its outlooks for 2017 quoted a reference figure of 2.4%.

Unusually, the WTO announced this outlook as central in a broad range of 1.8 to 3.6%, which it justified due to the deep uncertainties. Advance indicators used by the World Trade Organisation – through the *WTO World Trade Outlook Indicator*, introduced for the first time in July 2016 – also indicated a gentle improvement at the end of 2016 and beginning of 2017.

The IMF coincided with this estimate, as it valued the volume of international trade in goods and services at 2.3% in 2016, but made a projection of reaching 4.0% in 2017. Naturally, all these estimates are conditioned by the major unknown of if and how the protectionist measures proposed by the US administration could materialise, which could then result in other restrictive trade responses by other countries, especially if China is affected.

The IMF’s *Global Outlook Report* in October 2016 contained a simulation of “tariff scenarios” in which it was considered that an escalation in trade restrictions raising import prices by 10% could generate trade contraction by 15% and a reduction in global GDP of about 2%. The OECD report in March 2017 contains similar estimates.

So, with these last interpretations, the real risk to international trade would derive less from the apparently modest figures of recent years, which would be more the result of other factors than factors of concern, and more from potential tensions from trade conflicts in the near future. If these tensions do not materialise, the continuity of a certain upturn in the dynamic of global trade could contribute to a *new normality* in international trade flows. A question of a wider scope is whether any reversion of *delocalisation* operations – as proposed by some governments – could be associated more with the new incentives generated by the growing possibilities of automation than with the traditional focus of wage cost comparisons – or other focuses such as fiscal or environmental - in various locations.

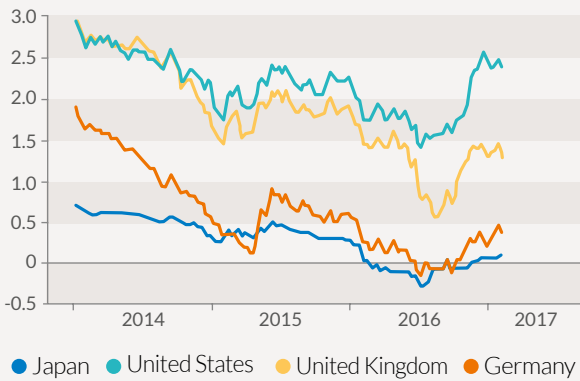
5. Developments in the financial markets

It is well known that the crisis of 2008-2009 has meant that the monetary policies adopted by the major central banks have entered relatively unheard-of situations, combining cuts in reference interest rates to practically zero levels – even negative in some cases (see box 1.3) – with the so-called quantitative easing or unconventional monetary policies with which the central banks injected liquidity in exchange for an ever-broader range of securities.

In 2016, a turning point occurred. As shown in figure 1.6, with data from the US Federal Reserve, income from 10-year securities in the major advanced countries initiated a phase of reversion, commencing an upward path, currently slow. Analyses of how the real interest rates had been falling show a conjunction of factors: increased savings for demographic reasons and changes in the distribution of income; increased uncertainty, which also impacted negatively on investment which reduced volume through technological changes that affected the prices of capital goods; and on the other hand, containment of public spending, which in part respond to structural changes but also more temporary reasons which may result, gradually, in a reversion towards more *normal* levels with various impacts: from the position of savers, debtors and financial entities.

NOMINAL 10-YEAR REFERENCE RATES IN SOME ADVANCED ECONOMIES

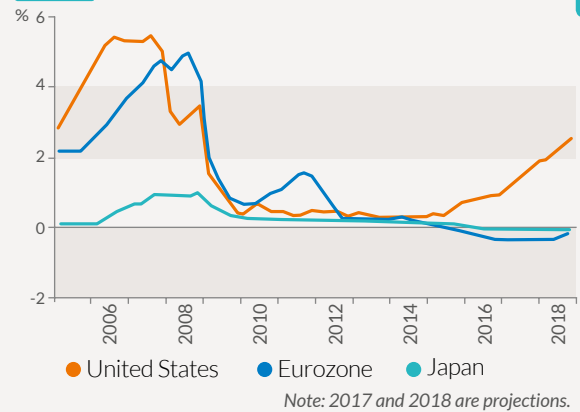
Figure 1.6



Source: Federal Reserve (2017), *Monetary Policy Report*, February 2017.

SHORT-TERM INTEREST RATES IN ADVANCED ECONOMIES

Figure 1.7



Note: 2017 and 2018 are projections.

Source: OECD, *Economic Outlook*, June 2017.

As for the short-term interest rates used to manage monetary policies, in 2016 an asymmetry occurred which indicates that it will continue – and will be accentuated – in 2017. While the United States made a first rise in the rate in 2016, and another additional in February 2017, the Eurozone keeps them at historical lows and, as deduced from their announcements, the intention is for them to continue that way (see figure 1.7).

This announced duality could bring appreciation of the dollar against the euro, which already began in 2016. The competitiveness of products from each side of the Atlantic would be affected, and this would be one of the ingredients of the famous “tailwinds” for the Eurozone economy.

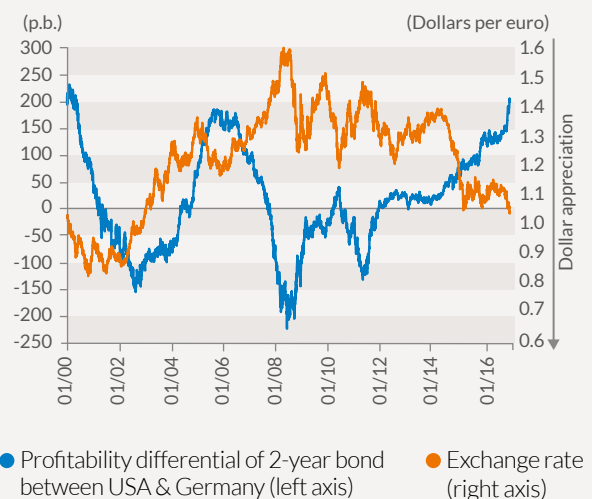
Since, in April 2008, the exchange rate between the euro and the dollar reached the historical high of 1.6 dollars per euro, the single currency has been losing positions in relation to the dollar. That was partly motivated by the growing divergence between the monetary policy of the Federal Reserve (Fed) and that of the ECB: while in the USA the Fed has started to raise reference rates, in Europe, the interest rates have remained relatively stable. More recently, the election of Donald Trump and the possibility that his administration might carry out expansionary fiscal policy in an economy that operates close to full productive capacity have increased inflation expectations in the USA, widening the profitability differential between US and European bonds.

However, apart from the trend for the dollar to appreciate, the volatility of the exchange rate will continue to be relatively high, partly due to the high uncertainty from factors which will guide the monetary policies of the Fed and the ECB, such as the effect of the Trump administration’s policies, the consequences of Brexit or the European electoral battles over the next few months.

Regarding fiscal policy, 2016 also marks a certain turning point in the fiscal consolidation started in 2010, when the initial expansionary response to the crisis greatly increased public

PROFITABILITY DIFFERENTIAL BETWEEN THE USA AND EUROPE AND EXCHANGE RATES

Figure 1.8



Source: CaixaBank Research.

NEGATIVE INTEREST RATES

Traditionally, the impossibility that interest rates would reach negative values was defended, as there was always the alternative of keeping money in cash, which enforced the so-called “zero lower bound” (ZLB). Naturally, reference was made through this to nominal interest rates, as the real interest rates, once inflation was discounted, had already reached negative at different times in the past, both distant and recent. The reduction in nominal interest rates to historical lows, even to modest negative values, associated with the costs of maintenance with effective security, results in the notion of “effective lower bound”, ELB.

The former head economist of the IMF, Olivier Blanchard, has highlighted that one of the lessons of

the crisis for the functioning of the macroeconomy was precisely the need to distinguish between the official or reference interest rates of monetary policy, and interest rates as a cost of obtaining credit for businesses and families, as the duality between the evolution in both types of “interest rate” would have become marked in recent times. The proposals – with measures already started in some countries – of gradually reducing and eventually eliminating cash transactions, usually justified in terms of modernity and the fight against transactions of dubious legality, may also open the door to the technical viability of more persistently negative interest rates, with broad implications on many aspects, from legal security to incentives to save.

PROFITABILITY OF SOVEREIGN BONDS IN EUROS

Country	Rating	1 year	2 years	3 years	5 years	7 years	8 years	10 years	15 years	30 years
Germany	AAA	-0.85	-0.80	-0.79	-0.54	-0.28	-0.14	0.20	0.45	0.94
Netherlands	AAA	-0.86	-0.75	-0.74	-0.37	-0.18	0.10	0.35	0.68	1.03
Austria	AA+	-0.73	-0.70	-0.64	-0.38	-0.12	0.08	0.42	0.90	1.30
Belgium	AA	-0.73	-0.69	-0.62	-0.41	-0.13	0.15	0.53	0.99	1.59
Finland	AA+	-0.77	-0.67	-0.63	-0.47	-0.05	0.01	0.34	0.74	1.01
France	AA	-0.74	-0.69	-0.51	-0.13	0.05	0.26	0.68	1.05	1.61
Ireland	A	-0.70	-0.58	-0.56	-0.30	0.06	0.34	0.74	1.17	1.68
Spain	BBB+	-0.37	-0.31	-0.20	0.26	0.82	1.08	1.38	1.79	2.61
Italy	BBB+	-0.30	-0.19	-0.07	0.60	1.18	1.43	1.81	2.15	2.93

● Negative profitability ● Positive profitability

Source: Own preparation with Bloomberg data on 31/12/2016.

deficits. In 2016, appeals increased to take advantage of the low interest rates – which relax the burden of debt interest – to give a slightly more expansionary tone to fiscal policies. The IMF proposed “wise use of the debt” in its *Fiscal Monitor* in October 2016, considering the argument that monetary policies had reached their limit and that a more active role of fiscal policies was required. On a similar line, the OECD’s *Economic Outlook* in November 2016 recommended “better use of fiscal initiatives to escape the low-growth trap”.

If we observe the evolution in public deficits for the advanced economies as a whole, the reduction after the initial large increase in response to the crisis was sustained, from 7.6% of GDP in 2010 to the 2.7% forecast for 2017. However, as diagram 1.9 shows, fiscal consolidation continues in the Eurozone, while in the United States, where they initially incurred more deficit but also made a more drastic reduction up to 2014, they now find themselves in positions of greater fiscal deficit, while still awaiting materialisation of the figures from the Trump administration’s fiscal measures.

In contrast, emerging economies as a whole, which initially maintained positions close to fiscal equilibrium, have reached higher deficits since 2015 than the advanced economies as a whole, partly through the more expansionary fiscal policies of China, but also, to a large extent, through the reduction in oil prices which led some exporting countries to deficits of unprecedented size (for example, Saudi Arabia went from a public surplus of 12% of its GDP in 2012 to a deficit close to 17% in 2016).

The balance between the role of fiscal policy stimulus and the need to supplement fiscal policies imposes, in a risky manner, the guarantees needed to sustainably redress delicate public finances. To this risk must be added the need for the fiscal tools that are incentivising improvement in productive efficiency not to destabilise the equality structure of the population.

As for the trend in stock markets, since the second half of 2016 this is clearly upward.

As for trends in the stock markets, as shown in figure 1.10, the trend from the second half of 2016 is clearly upward. Initially, this positive dynamic may reflect better performance and better expectations for the economic future, with a greater presence of return on capital, and a greater willingness to assume risks, despite the uncertainties. Another possibility, according to analysts, is that the low interest rates of fixed-income instruments may be making variable income comparatively more attractive.

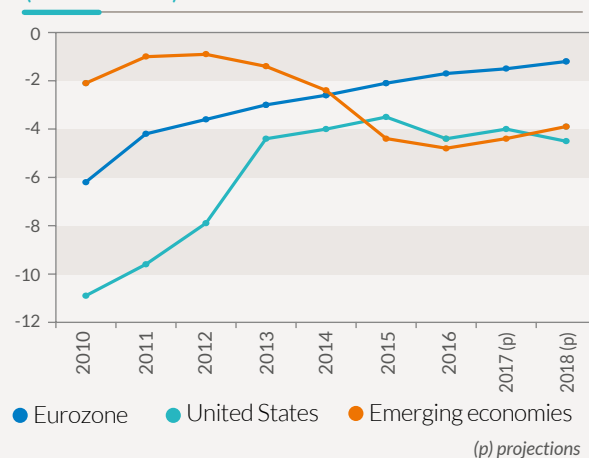
But some caution is indicated. Both the OECD and the Basel Bank for International Settlements (BIS) have analysed the possible existence of overvaluations. So, the BIS' annual report includes a comparison between the recent trend in the cycle-adjusted price-earnings ratio (P/E) – an indicator formulated by the Nobel prize-winner Shiller – and its historical trend. The conclusion is that the United States already exceeded this ratio quite clearly, with the subsequent risk of overvaluation, while the Eurozone is getting close and Japan still stands significantly below the historical references.

6. Financial risks

The turning point in the interest rates has influenced finances in 2016 (and early 2017). The reports by the IMF and OECD have made particular reference to the risks of a reappearance of financial weaknesses which, to a certain extent, already occurred on the path to crisis in 2008.

TRENDS IN THE PUBLIC DEFICITS OF THE UNITED STATES, THE EUROZONE AND EMERGING ECONOMIES 2010-2018
(as % of GDP)

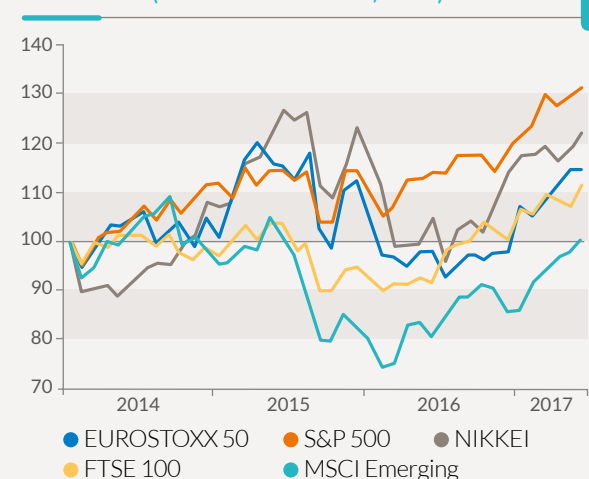
Figure 1.9



Source: IMF, Fiscal Monitor, April 2017.

TRENDS IN THE MAJOR MARKET INDICATORS 2014-2017 (base 100 = January 2014)

Figure 1.10



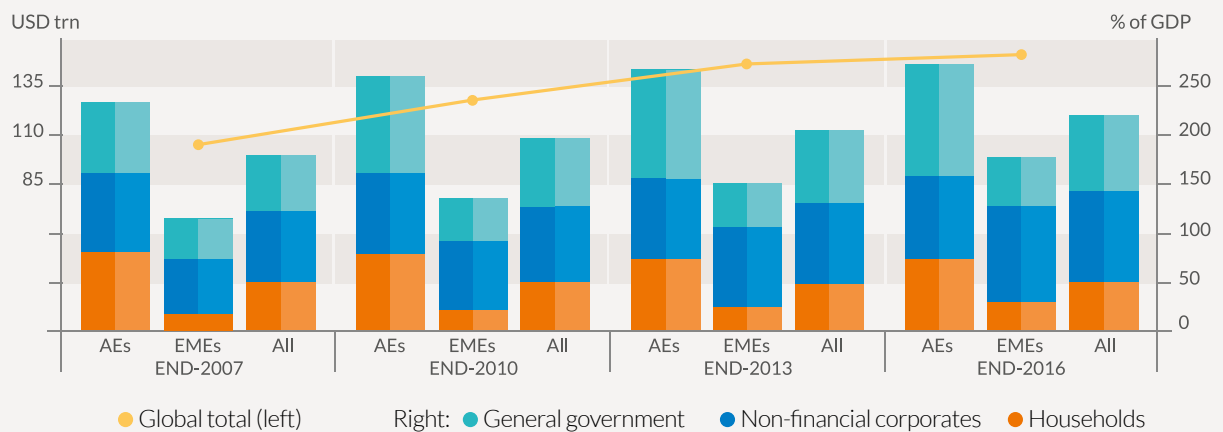
Source: Bank of Spain, Quarterly report, June 2017.

As is well-known, excessive expansion of credit and the correlative increase in debt were the most visible financial factors on the path to crisis (following the patterns of other episodes of financial problems, as already documented in 1933 by Professor Irving Fisher). As has already been much reiterated, an initial effect of the crisis was a major contraction in credit – closing the “credit tap”, in the very explicit terminology which became popular – while a readjustment of debt levels was required to initiate a solid recovery. In fact, some proposals, such as the influential hypothesis formulated by the BIS under the title *financial cycle drag* – debt *supercycle* in some less technical formulations – insisted on the burden represented by the accumulated debt on the recovery in growth and, therefore, the need to reach more sustainable levels to promote more solid and sustainable growth over time. It was considered that these adjustments were sometimes hard but essential.

The annual report of the BIS in June 2017 had as a first reference precisely the continuity of the debt on a global scale, as shown in figure 1.11. This shows the contribution of both the advanced and emerging economies, both on the up from 2007 to 2016, and within each country group that of the major sectors, with a growing percentage of public debt in the advanced economies – in contrast with the private sector, which faces a complicated

Need to reach more sustainable debt levels to encourage stronger, more sustainable growth over time.

TRENDS IN GLOBAL DEBT 2007-2016 (debt as percentage of respective GDPs)

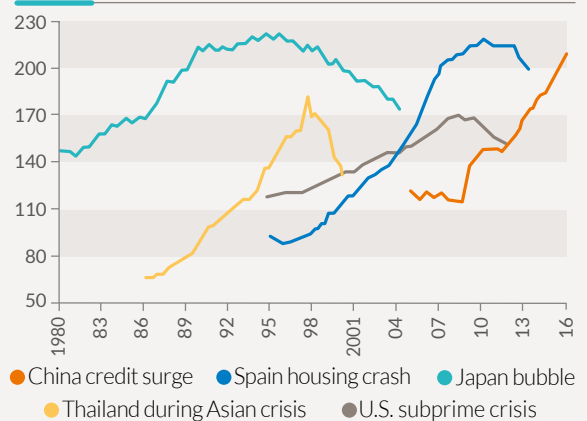


Source: IMF, Global Economic Outlook; OECD, Economic Outlook; national data; BIS calculations.

debt reduction – while in emerging economies the position of the private sector has been progressing towards further debt.

The particular case of China is receiving special attention in recent years. Figure 1.12 depicts how the IMF has shown its concern about the evolution in credit in China in recent years. It established a comparison between three credit expansion precedents which were finally revealed as unsustainable, and which resulted in a more-or-less drastic and delicate reversion. The reference cases are Japan in the 1980s, Thailand at the end of the 1990s (remember that this country was the first to suffer the South-East Asian crisis in 1997, which resulted in the tsunami effect in the region), and Spain

CREDIT GROWTH AS A PERCENTAGE OF NATIONAL GDP: China's recent situation compared with other experienced collapse situations



Source: IMF, Global Financial Stability Report, April 2017.

Figure 1.11

Figure 1.12

in the early years of the 21st century. The repeated pattern is high credit expansion in percentage terms which sooner or later becomes unsustainable and leads to a downturn - "closing the credit tap" in less formal terms - which complicates exit from the *credit bubble*.

The OECD and BIS reports in June 2017 coincide in explaining the debt dynamics of the so-called "financial cycle", and warn of the reappearance of some of the trends which led to the problems in 2008.

In summary, in 2016, a certain tendency to normalisation of some financial variables occurred - such as interest rates or credit volumes - but these dynamics need to progress at a cautious pace, to avoid the swings which could lead to imbalances and risks, and never lose sight of saturation of public deficit utilisation and its repercussion on debt volumes.

7. Prospects

In 2016, interactions between economic and sociopolitical dimensions have been especially evident, above all in view of the results - surprising to many observers - of the June referendum on Brexit in the United Kingdom, and also the presidential elections in the United States. The connections between the implications of the inequalities detected by some indicators and the growing unease - or even angst - over some effects of the global dynamics, are already difficult to avoid. Moreover, we should add, in the case of European countries, the criticisms relating to the manner in which the European Union has managed recent problems. Even the IMF spoke of globalisation "insiders and outsiders" at the end of 2016, and included in the April *World Economic Outlook* a study of the reasons for the loss of importance of the labour factor in the national revenue of many countries, its causes and implications.

Entities as prestigious as the OECD and *World Economic Forum* expressed the concern not only about inequalities - which were leading to the globalisation of anti-globalisation - but also the need to enable growth to be more inclusive, to reach wider segments of the population.

References to *inclusivity* increase: in 2016, the World Trade Organisation started to insist on *inclusive* trade. Even the G20, at the September 2016 summit in China, decided to add the term *inclusive* to the desired form of growth, in addition to the terms used since 2009: strong, sustainable, balanced and now inclusive. The expectations on the results of electoral processes in Europe in 2017 were making themselves felt.

An analysis presented by Branko Milanovic in 2016 has rapidly become a reference. This prestigious specialist on matters of income distribution has documented how, since the start of globalisation (the end of the 1980s, to be specific), the main changes in the dynamic of winners and losers has been:

- a) On the one hand, the appearance in emerging economies of new global middle classes, with growing purchasing power, the new target of the bulk of businesses on a global scale.
- b) And on the other hand, the loss of relative positions (and in some cases, even in absolute terms) of the traditional middle classes in western economies, pressured simultaneously by the ascent of emerging economies and the uncertainties generated by a wave of technological innovations - including automation - forcing a redefinition of potential jobs across broad segments of the population. These concerns of the middle classes were one of the factors which could explain unexpected political results.

A study published shortly after the presidential elections in the United States in November 2016, by top writers such as Autor, Dorn, Hanson and Majlesi (2017) showed, by following trends

Since mid-2016, the economic climate is regarded more optimistically on an international scale.

already noted in previous electoral processes since 2010, a notable correlation between the constituencies that had most swapped the traditional vote for the Democratic Party for a vote in favour of the candidate Trump, and those

which had seen the steepest falls in employment, related to Chinese competition or delocalisation. Economic polarisation was resulting in *political polarisation*, to use the title of the articles by these authors. In general, for centuries, economists have presented all manner of arguments to explain that international relations are at least potentially *positive-sum games*, in which all players could win – directly or with distributive policies – but in the sociopolitical processes these arguments appear to struggle to be recognised.

In summary, in 2016 distributive frictions flourished, complicated by doubts about the sociopolitical impacts of rapid technological changes, from automation to 3D printing in fields where they were, until recently, unimaginable.

This reality requires responses from the political powers, but historical experience tends to show that a swing towards potential deglobalisation is not desirable. Stabilised globalisation at a high level, with adjustments to make it more inclusive, seems to be the most recommendable scenario but, as at other times in history, other kinds of currents cannot be ruled out, which the currently uncertain international cooperation would need to help overcome.

In summary, since mid-2016, the economic climate seems more optimistic on an international scale. According to the IMF's outlook in April 2017, advanced economies will grow 2.0% in 2017 and

OVERVIEW OF PROJECTIONS IN THE GLOBAL ECONOMIC OUTLOOK
(Annual percentage variation)

Table 1.9

	PROJECTIONS			
	2015	2016	2017	2018
Global GDP	3.4	3.2	3.5	3.6
Advanced economies	2.1	1.7	2.0	1.9
USA	2.6	1.6	2.1	2.1
Eurozone	2.0	1.8	1.9	1.7
Germany	1.5	1.8	1.8	1.6
France	1.1	1.2	1.5	1.7
Italy	0.8	0.9	1.3	1.0
Spain	3.2	3.2	3.1	2.4
Japan	1.1	1.0	1.3	0.6
United Kingdom	2.2	1.8	1.7	1.5
Canada	0.9	1.5	2.5	1.9
Emerging and developing market economies	4.3	4.3	4.6	4.8
Russia	-2.8	-0.2	1.4	1.4
China	6.9	6.7	6.7	6.4
India	8.0	7.1	7.2	7.7
Brazil	-3.8	-3.6	0.3	1.3
Mexico	2.6	2.3	1.9	2.0
Saudi Arabia	4.1	1.7	0.1	1.1
Nigeria	2.7	-1.6	0.8	1.9
South Africa	1.3	0.3	1.0	1.2
Oil price (US dollars)	-47.2	-15.7	21.2	0.1
Consumer prices				
Advanced economies	0.3	0.8	1.9	1.8
Emerging and developing market economies	4.7	4.3	4.5	4.6

Source: IMF. *Global Economic Outlook*. July 2017.

2018, but the most notable factor in this report is the upturn in growth expected for emerging and developing market economies (EMED). In effect, the estimate of growth for these economies stood at 4.5% in 2017 and 4.8% in 2018.

One of the main risks in achieving these forecasts is the current erosion of the consensus on the benefits of cross-border economic integration. The possibility that global imbalances will increase and this will combine with strong movements in exchange rates could intensify protectionist pressures. Increasing global trade and migration restrictions would have negative effects on productivity and income and affect the markets' spirits.

Geopolitical risks and a variety of non-economic factors continue to veil prospects in several regions: civil war and internal conflicts in some parts of the Middle East and Africa; the tragic situation of refugees and migratory processes in neighbouring countries and Europe; terrorist attacks throughout the world; the extended effects of the drought in eastern and southern Africa, and the spread of the Zika virus. Intensification of these factors would increase hardship in the countries that are directly affected. The resurfacing of geopolitical tensions and terrorism could also be a hard blow to international markets and economic confidence.

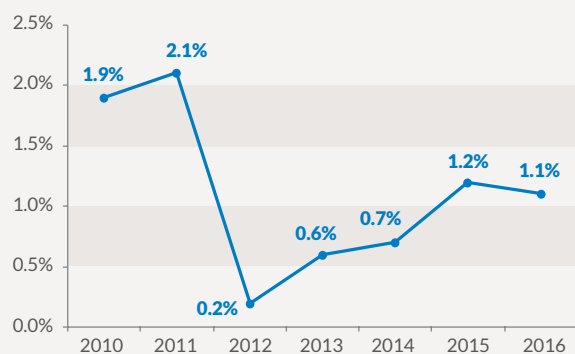
The French economy

1. The main features of economic development in 2016

The macroeconomic projections presented by the Bank of France in June 2017 put figures for economic growth in 2016 at 1.1%, a very similar variation to the 1.2% in 2015, and they predict slight improvements in 2017 and 2018, up to real GDP growth rates of 1.4% and 1.6%, respectively.

In 2016, while domestic demand made a positive contribution to GDP of 2.0 points, the foreign sector affected it negatively by -0.8 points, a gap that has widened since the previous year, although a reversal is expected within the next few years. This situation poses certain questions about the sustainability of domestic demand – mainly in relation to consumption – as a driving force for recovery, and also about the work to be done on the foreign competitiveness of the French economy. The fact that the rate of growth is higher in gross capital formation than in private consumption is a French particularity, which can be partly attributed to regulatory changes that motivated investment. In effect, in 2016, gross capital formation, at a rate of 2.7%, was the most positive component, compared with private consumption which grew 2.1%. The negative contribution from the foreign sector originated in an export rate of only 1.9%, which was surpassed by imports, with growth of 4.2%.

GDP GROWTH IN FRANCE
Interannual variation rates in %



Source: OECD, *Economic Outlook*, June 2017.

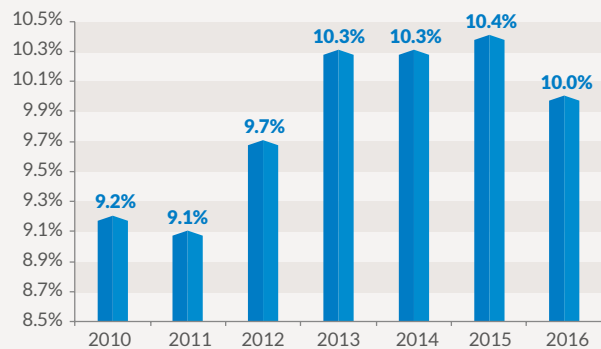
The French economy, with growth of 1.1%, confirms the recovery started in 2015.

According to INSEE, the annual variation rate of the consumer price index (CPI) was 0.6% in 2016 (0.2% in 2015), the annual underlying inflation rate was 0.4% (0.8% in 2015), and the harmonised consumer price index was 0.8% (0.3% in 2015).

As for employment, although in recent years this has been a priority for the French Government, the unemployment rate remains at high levels (10.0%), especially among young people (24%), and job creation is still weak (0.7% annual). One of the actions carried out within the field of employment to mitigate rigidities and also revitalise the economy was a labour market reform with the aim of legally defining dismissal for economic reasons, reinforcing collective bargaining both in businesses and the sector, and improving training for the unemployed.

UNEMPLOYMENT RATE IN FRANCE As % of the active population

Figure 2.2



Source: OECD, *Economic Outlook*, June 2017.

Box 2.1

THE FRENCH ECONOMY INHERITED BY THE NEW PRESIDENT

In terms of economic activity, the new president of France inherits an economy which has recovered from the financial crisis, with 4% higher GDP in 2016 than in 2008. However, growth over the last few years has been gradual and clearly below that of other advanced economies, as can be seen in the diagram below. For 2017-2018, prospects are still not very hopeful: the general consensus of analysts expects growth close to 1.3%.

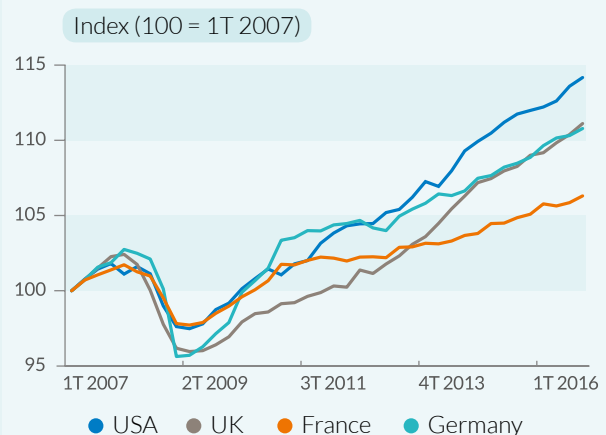
This lack of economic dynamism is the reflection of lower growth in productivity due, to a large extent, to the major structural rigidities which are still present in the French economy. Notably, an inflexible labour market, high tax burden and complex regulation, which act as a barrier to investment and growth of businesses.

In recent years, efforts have been made to relax fiscal pressure and increase competitiveness by reducing social contributions from businesses. So, in 2015, the Macron Law on liberalisation of the markets to promote activity was passed, which included measures such as allowing shops to open on Sundays and liberalising various regulated professions.

However, although these reforms are a step in the right direction, it appears that they have a limited impact, so it is still important to maintain an ambitious reform agenda. One of the priorities is to increase the rate of job creation in the private sector.

Finally, it would be very beneficial to the French economy to improve the trade environment and reduce obstacles to setting up businesses.

GDP IN REAL TERMS

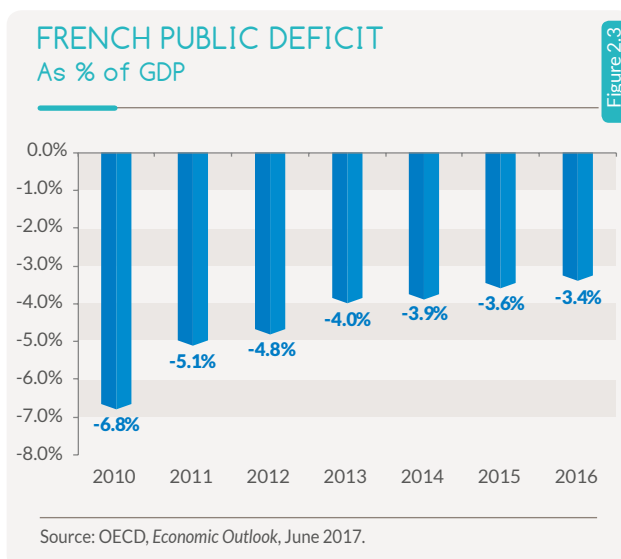


Source: Caixabank Research, based on data from Thomson Reuters Datastream.

Source: Caixabank Research. Monthly report number 412. May 2017.

Another priority of the French economy is public finance adjustment. Although the public deficit fell from 7.2% of GDP in 2009 to 3.4% in 2016, the public debt (96.6% in 2016) is close to 100% of GDP, leaving the French economy vulnerable to changes in investor sentiment and rises in interest rates. Therefore, improvements in public administration efficiency could be a great help, considering the high public spending, which remains well above the average for the Eurozone (57% of GDP, compared with 47%).

According to the 2017 *Doing Business* report, which rates 190 countries worldwide, France holds position no. 29 in terms of “ease of doing business” (no. 15 among EU-member states), after dropping one place since 2016. France confirms its efficiency in cross-border trade matters, and stands at the top of the ranks in this field, for yet another year (along with the other EU-member states). France also stands out for enforcing contracts (18th), resolving insolvencies (24th), getting electricity (25th), and starting a business (27th). In relation to the last item, the waiting period needed to start operating has improved from 4 to 3.5 days. Also of note is France’s significant progress in relation to dealing with construction permits (improving 10 places in this ranking), thanks to a reform that enabled a reduction in the cost of obtaining a permit. However, France stands out negatively in ease of procedures for registering property (100th), getting credit (82nd) and paying taxes (63rd).



2. Prospects

The macroeconomic projections presented by the Bank of France in June 2017 include several forecasts for the French economy in 2017 and 2018. Estimates of GDP growth for 2017 lie between 1.3% and 1.5%; the figure most repeated by international bodies is 1.4%. In general, a certain slowdown is expected in private consumption (1.3% in 2017) and a certain continuity in investment (2.6% in 2017), with a reduction in the contribution from internal demand offset by expectations of an improvement in exports, which exceeds the 2016 figure in any case. Bank of France forecasts for 2018 are slightly more optimistic (exports growth over 5%), even predicting a positive contribution from foreign demand as soon as 2018.

For its part, in March 2017, the European Commission (EC) report on France, within the framework of the in-depth studies on EU countries subject to the macroeconomic imbalance procedure, also accentuates some of the features presented previously by the Bank of France. On the one hand, the EC estimates growth in 2016 at 1.2% - representing a small downturn from 1.3% in 2015 - but equally, its forecasts for 2017 lie slightly above those of the French Central Bank: 1.4% for 2017 and 1.7% for 2018. On the other hand, the EC also concurs in anticipating a rebalance of the contributions from the domestic and foreign sectors in the French economy for 2017-2018.

Forecasts indicate accelerated economic growth for 2017 and 2018.

Probably, therefore, these data show a certain trough reached in the French economy in 2016, with prospects of a moderate correction from 2017 in terms of GDP, a reduction in unemployment and budget balance, among other aspects.

MACROECONOMIC TABLE FOR FRANCE

(Annual variation rates in %, unless otherwise indicated)

Table 2.1

	2016	2017 (p)	2018 (p)	2019 (p)
Real GDP	1.1	1.4	1.6	1.6
Domestic demand (contribution to growth)	2.0	1.6	1.5	1.5
Net exports (contribution to growth)	-0.8	-0.5	0.1	0.1
Stock variation (contribution to growth)	-0.1	0.3	-0.1	0.0
Private consumption	2.1	1.3	1.5	1.5
Public consumption	1.2	1.1	1.0	1.1
Gross capital formation	2.7	2.6	2.1	2.0
Exports	1.9	3.3	5.1	4.2
Imports	4.2	4.8	4.3	3.8
Harmonised Consumer Price Index (HCPI)	0.3	1.2	1.2	1.4
Unemployment rate (% of active population)	10.1	9.7	9.6	9.3
Public account balance (as % of GDP)	-3.4	-3.1	-2.9	-3.1

(p) projections

Source: Bank of France, *Macroeconomic Projections*, June 2017.

In any case, over the French economy hangs the result of implementation of the reform programme deriving from the results of the presidential and parliamentary elections in spring 2017, which are expected to substantially effect the strategic orientations of the economy and also the interactions between the economy and sociopolitical dynamics.

In fact, after the presidential elections, the French appear more optimistic in relation to the future of their economy, and entrepreneurs' levels of confidence in the French and global economies are increasing significantly, according to the latest report from the PME-ETI (SMEs) Observatory of *Opinion Way – Banque Palatine pour Challenges*, of July 2017.

The Spanish economy

1. The main features of economic development in 2016

The Spanish economy grew 3.2% in 2016, repeating the growth seen in 2015, a much higher rate than the Eurozone average. The Spanish economy continues to experience a strong recovery and is moving toward a more balanced growth composition than before the crisis. In its third year of expansion, Spanish real GDP has returned to the crest reached before the crisis, in 2008. The recovery was initially driven by exports, after reversing the losses in cost competitiveness accumulated over the years before the crisis. Then, the recovery gradually extended to the domestic sector.

Since 2015, high job creation, low oil prices and improvement in financial investments have encouraged private consumption. Capital goods investment also increased considerably, while the recovery in investment in the construction sector started. The surplus in the current account balance continues. Therefore, growth has been driven by investment and private consumption, with a positive contribution also from the foreign sector, for the first time since the start of the recovery.

Growth is expected to slow down over the next few years, but will remain solid. The structural reforms carried out in Spain in recent years have strengthened the bases of the strong economic recovery,

to which other favourable conditions have also contributed. An upturn in oil prices, if geopolitical tensions in competing tourist destinations relax, could have a negative effect on the Spanish economy's foreign balance. On the other hand, no new significant improvements in the Spanish economy are expected, considering that the increase in productivity remains moderate and wage increases are recurring. A loss in dynamism in domestic demand is expected, as it will cease to be encouraged by falling prices, by tax cuts applied in the period 2015-2016 and by the improvement in financial conditions. In general terms, real GDP growth is expected to slow, although it will still remain above 2% (2.8% in 2017 and 2.3% in 2018), according to the *Economic Bulletin* of the Bank of Spain.

In any case, the sequels of the crisis have still not been completely overcome and there are still major challenges. Spain has made a substantial economic adjustment, but the persistence of imbalances undermines the economy. The main challenges lie in the field of private debt, public finances, the labour market and the business environment.

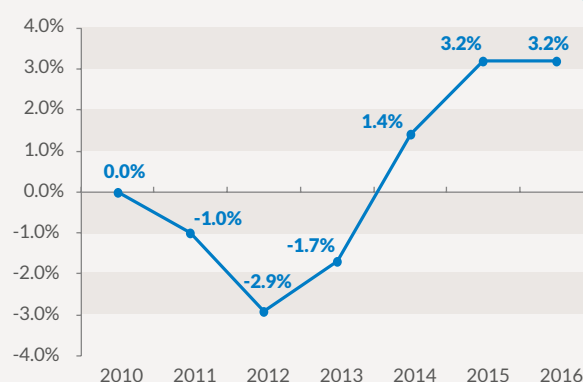
The process of deleveraging in the private sector, started in 2010, is progressing, although the level of debt is still high. The private sector debt was equal to 167.5% of GDP at the end of 2016, representing a fall of 48 points compared with the figure in 2010. A large part of this reduction (approximately 30 points) was the consequence of the major reduction in debt of non-financial companies, although progress in deleveraging households was also notable. Real growth became the main factor for reducing debt ratios, while continuing to expand the concession of new credits to households and to SMEs, favoured by a more rationalised financial sector. Nevertheless, deleveraging requirements are still considerable, especially for households.

As for the public administration debt – 99.3% of GDP in 2016 – Eurostat and the European Commission predict that, in the short-term, this will continue to stabilise at about 100% of GDP, due to strong growth in nominal GDP, which would greatly offset the still high but falling deficit expected until 2018. This decrease in the deficit, combined with economic growth, would bring a slight reduction in the debt ratio in the period 2018-2020 (see box 3.1).

In 2015, the deficit was 5.1% of GDP, falling to 4.5% in 2016, meaning a reduction of 0.6 points. Although public spending increased as expected, much lower than expected revenue from income tax affected public revenue. In the hypothesis that economic policy stays the same, the deficit could continue to fall to 3.3% and 2.7% of GDP in 2017 and 2018, respectively, according to Eurostat and the European Commission.

GDP GROWTH IN SPAIN
INTERANNUAL VARIATION RATES IN %

Figure 3.1

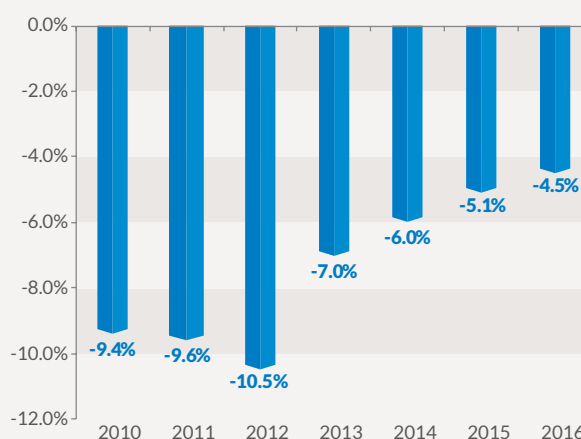


Source: OECD, *Economic Outlook*, June 2017.

Spain has undergone substantial economic adjustment, but persistent imbalances leave the economy vulnerable.

SPANISH PUBLIC DEFICIT
As % of GDP

Figure 3.2



Source: OECD, *Economic Outlook*, June 2017.

Box 3.1

THE SPANISH PUBLIC DEBT

The high levels of debt and public deficits have exacerbated the credit needs of public administrations, to historically high levels in recent years. In this context, adequate management of public debt issuances is key.

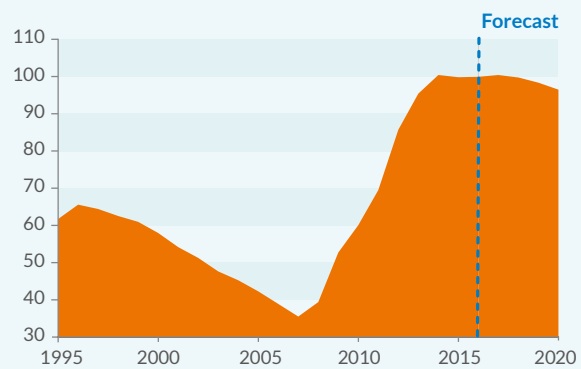
In Spain, in 2017, debt maturity for the value of 185,017 million euros will need to be covered. Moreover, the Treasury is predicting a net issuance of an additional 35,000 million, raising the total gross credit requirement to 220,017 million. Similarly to recent years, the Treasury is planning to finance the new needs through medium to long-term debt issuance, so the average life of the public debt will continue to increase. In 2016, this reached 6.8 years, a similar figure to the one recorded at the start of the crisis. Lengthening the average life helps to reduce the risk of refinancing, an especially relevant risk when the amount of debt needed to renew every year is high.

Lengthening the average life has been compatible with a reduction in its average cost, thanks, to a large extent, to the ECB's accommodative monetary policy. In 2016, the average cost of the debt was around 2.9%, far from the 4.1% recorded in 2011. The lower cost of financing has led to important savings in interest payments, which have even fallen in nominal terms since 2014.

Although, in 2017, the ECB will maintain its asset purchase programmes, the interest rates will no longer be as favourable, as they are expected to rise slowly, especially at the long end of the curve. With this scenario in mind, boosting issuance at the long end of the curve is wise, as it takes advantage of the currently low interest rates and helps to reduce the refinancing risk.

Whatever happens, efforts need to be focussed on continuing the path of fiscal consolidation and gradually decreasing the levels of public debt, to avoid the cost of debt getting out of control when interest rates rise.

PUBLIC DEBT (% of GDP)



Source: CaixaBank Research, based on data from Bank of Spain.

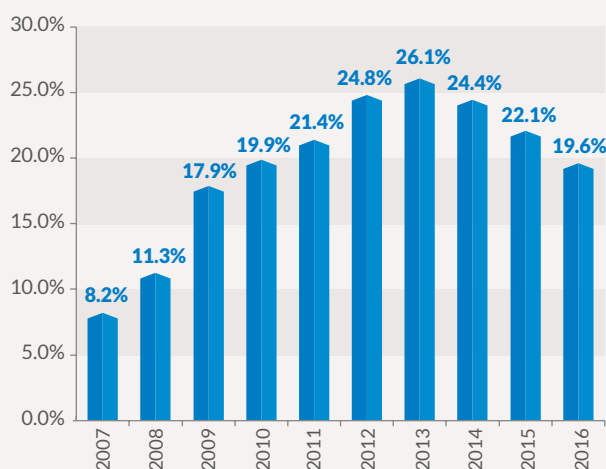
Source: CaixaBank Research. *Monthly Report* number 409. February 2017.

In 2016, strong job creation continued which, despite suffering deceleration, will remain solid until 2018. The employment rate increased again in 2016 due to sustained economic growth, but is still much lower than the level obtained before the crisis (64.5% in the third quarter of 2016, compared with 69.7% in 2007) and the EU average (71.5% in the third quarter of 2016). Current wage moderation and labour market reforms carried out in previous years contributed to the extent of job creation. Full-time equivalent employment is expected to have increased 2.9% in 2016 and continue to rise in 2017 and 2018, by 2% and 1.7%, respectively. Wage moderation was also favoured by very low inflation. However, wage rises are predicted as a result of the gradual upturn in inflation. This, together with a very limited increase in productivity, will probably cause a rise in unit labour costs.

According to the National Institute of Statistics (INE), the annual variation rate of the CPI in 2016 was 1.6% (0.0% in 2015), the annual underlying inflation rate was 1.0% (0.9% in 2015), and the harmonised consumer price index reached a rate of 1.4% (-0.1% in 2015).

UNEMPLOYMENT RATE IN SPAIN As % of active population

Figure 3.3



Source: OECD, *Economic Outlook*, June 2017.

The unemployment rate is still very high (19.6% in 2016), especially among young people and people with low qualifications. Moreover, almost half of the unemployed have been without work for more than a year. This indicates the high risk of long-term unemployment becoming rooted and of devaluation of human resources, which limits potential growth and productivity. Together with this, poverty and income distribution inequality are the highest in the EU.

According to the 2017 *Doing Business* report, which rates 190 countries worldwide, Spain holds position no. 32 in terms of “ease of doing business” (no. 17 among EU states) and has risen one place since the 2016 report. Spain confirms its efficiency in matters of cross-border trade and stands, for yet another year, at the top of the ranks in this field (along with the other EU-member states). It also stands out in other

indicators, such as paying taxes (37th), protecting minority investors (32nd), enforcing contracts (29th) and resolving insolvencies (18th). However, Spain is notably down in the ranks for the indicators of getting electricity (78th), starting a business (85th) and dealing with construction permits (113rd). These fields are especially complicated for recently-incorporated industrial companies, and there are also huge variations between autonomous communities. For example, starting up an SME requires 60 days in the Canary Islands and 250 days in Murcia, and costs range from 6% (Andalusia) and 23% (Catalonia) of income per capita (*Doing Business Subnational*, World Bank, 2015).

Innovation activities by enterprises are still below the levels before the crisis, and the proportion of high-growth innovative enterprises (HGIE) in the economy is still low. The Spanish industrial structure is marked by the high percentage of SMEs that operate in low-technology sectors and, moreover, has reduced the number of actively-innovative enterprises.

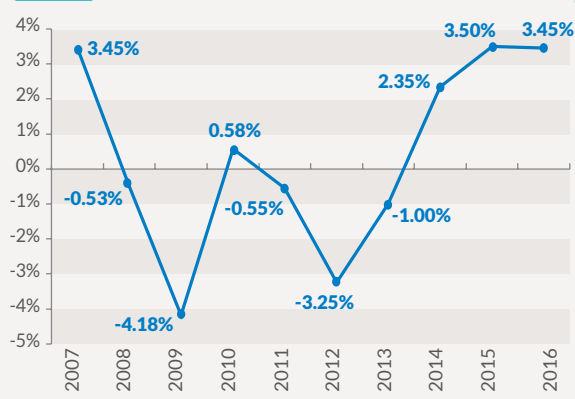
2. The Catalan economy

In the specific case of the Catalan economy, the above-mentioned risks relating to the economic recovery from the international point of view are also applicable. The year finally ended with a growth rate of 3.5%, in keeping with the economic situation in July 2017, as presented by Idescat (Institute of Statistics of Catalonia). So, the high growth rate of 2015 is maintained (also 3.5%), the highest since 2007. This means that the economic recovery that started mid-2013 has been consolidated over the last three years.

In fact, the economic recovery seems to remain sound, being slightly stronger in Catalonia than

GDP GROWTH IN CATALONIA Interannual variation rates as %

Figure 3.4



Source: Idescat.

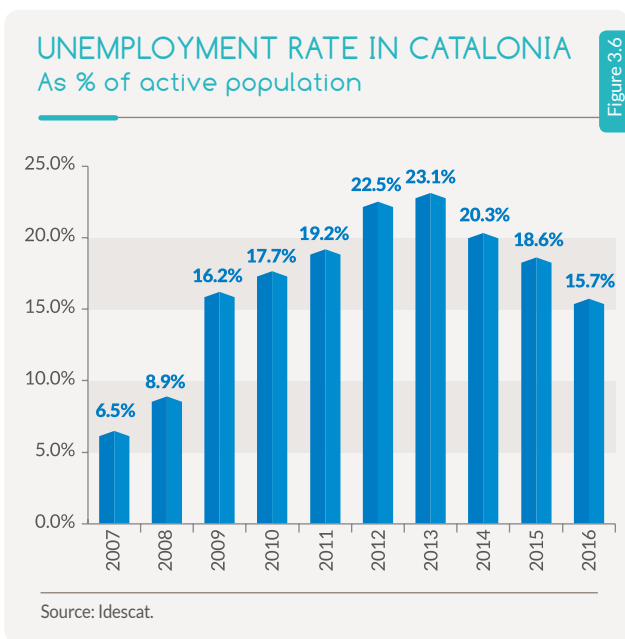
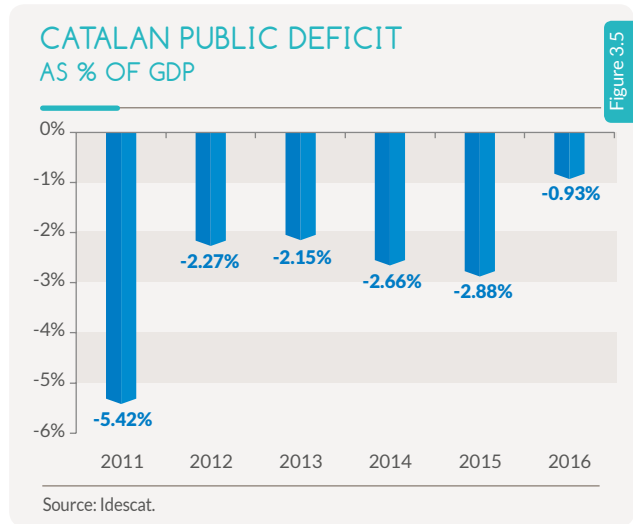
in Spain as a whole, above all in relation to the labour market. All available indicators relating to household consumption still show a strong rate of growth in 2016. This growth is a clear signal that domestic demand in general, and household consumption in particular, is still the driving force behind economic recovery.

Now, lower momentum than 2015 can be seen in the case of investment, which has grown 5.2% throughout 2016. Although this rate is slightly lower than the 5.7% growth in 2015, it is also true that no clear signs of a change in pace can be seen. In any case, investment is probably the field where there is most uncertainty due to the potential impact of certain factors that generate instability on an international scale. Data published in recent months also highlight the strong growth in foreign investment seen in Catalonia, so the potentially negative impact may be lower than initially predicted.

In relation to the foreign sector, the most notable aspect is that exports continued to see a clearly-rising trend until the end of the year. It appears that, at least at the moment, the results of the British referendum are not having a significant impact on the trend in exports. In the case of imports, the trend was more erratic over the year.

As for developments in GDP relating to supply, these were still positive in the industrial sector: in 2016, Catalan industrial production grew 4.0% p.a., higher than the 3.7% recorded in the previous year. This growth rate is still clearly higher than that of Spanish industry as a whole, which was 2.4%.

Other indicators, such as developments in industrial sector employment or industrial vehicle registrations, confirm this vitality in recent months. In the case of electricity bills, although the cumulative variation rate for 2016 was negative, it was notably better than the one observed over recent years. As for the construction sector, this has been going through a process of rapid acceleration, from -0.1% growth in 2015 to 3.2% in 2016. Indicators like cement consumption or the number of workers corroborate this diagnosis. Finally, in the services sector, the growth rate has fallen slightly, going from 3.3% in 2015 to 3.1% in 2016.



Job creation is expected to maintain a good rate, driven by growth in domestic demand. A sign of strong job creation can be seen in the fact that recorded unemployment fell between December 2015 and December 2016 by 11.9%. The results of the active population survey, however, show a huge variation according to sector: from a discreet 0.3% in industry, through 0.9% in construction, to 4.4% in services and 6.2% in the primary sector.

Growth in employment and the (very moderate) downturn in the active population means that unemployment is still decreasing, with an interannual fall of 15.6%. So, the average

The number of unemployed has continued to fall, with an interannual decline of 15.6%.

unemployment rate in 2016 is 15.7%, 2.9 points lower than the rate for 2015 (18.6%). By groups, there was notably a steep reduction in female unemployment, which reached 15.9% at the end of 2016 (it was 3.2 points higher

one year earlier), thanks to the good performance in female employment. For its part, the male unemployment rate also shows a significant fall (2.6 points) and stands at a rate of 13.9% in the fourth quarter of 2016. Idescat predicts that in 2018, the unemployment rate will reach an annual average of 11.6%.

In relation to trends in prices, in 2016, these was completed by an upward trend in inflation that had already begun in May. After some months of negative interannual inflation rates, the annual figure was an increase of 1.9%. This rate is 1.6% higher than for Spain as a whole.

3. Prospects

The data available for Spain until mid-2017 allow us to advance that until now, a growth rate of over 3% is maintained. Forecasts for the end of the year are for this momentum to continue. By components of demand, the upturn in forecasts is based, in general, on trends in the foreign sector and, above all, on expected growth being higher than exports. The forecast is that these exports, which ended 2016 with annual growth of 4.4%, will gain momentum to 6.1% for the whole of 2017. The same occurs with imports, which will keep growing from 3.3% in 2016 to 5.2% in 2017.

As for domestic demand, significant changes are also predicted. Private consumption, with predicted growth of 2.4% in 2017, will probably continue with a similar dynamic to the last two years, making domestic demand a driving force, together with investment (3.3%). In fact, the investment rate in 2017 is expected to be two tenths higher than in 2016 (3.1%). For its part, public consumption will maintain the moderate growth rate of 0.8%, the same as in 2016.

PROJECTIONS OF THE MAJOR MACROECONOMIC MAGNITUDES OF THE SPANISH ECONOMY (annual variation rate over volume and % of GDP)

Table 3.1

	2016	PROJECTIONS		
		2017	2018	2019
Real GDP	3.2	2.8	2.3	2.1
Private consumption	3.2	2.4	1.6	1.5
Public consumption	0.8	0.8	0.8	0.8
Gross fixed capital formation	3.1	3.3	4.4	4.4
Investment in capital goods	5.0	3.1	5.1	5.1
Investment in construction	1.9	3.7	4.4	4.5
Exports of goods and services	4.4	6.1	4.8	4.8
Imports of goods and services	3.3	5.2	4.4	4.4
National demand (contribution to growth)	2.8	2.3	2.0	1.9
Net foreign demand (contribution to growth)	0.5	0.5	0.3	0.2
Nominal GDP	3.6	3.8	3.6	3.7
GDP deflator	0.3	1.0	1.3	1.5
Consumer Price Index (CPI)	-0.2	2.2	1.4	1.6
Unemployment rate (% of active population)	19.6	17.5	16.0	14.5

Source: Bank of Spain, *Economic Bulletin*. January 2017.

As for supply, a very balanced evolution is predicted by sectors. So, it is expected that services and industry will be the most dynamic sectors (3.1%), followed by the construction sector (2.9%). Naturally, given its weighting in

the economy as a whole, the contribution from services to growth will be the most significant. The stability in industrial sector growth stands out. This sectoral evolution is also consistent with the different forecasts for the Spanish economy that have been published in recent months.

Growth is expected to slow over the next few years, but also to remain strong.

Moreover, it is notable that the Harmonised Business Confidence Index (HBCI) for the third quarter of 2017 (136.9) increased by 2.0% in relation to the level of three months ago (134.2), according to the press release in July 2017 from the National Institute of Statistics. In the case of Catalonia, this index increased 0.8%, going from 142.6 to 143.8. These results are consistent with the comments above about the current situation. In fact, if we compare these values with the levels of one year ago, from the third quarter of 2016, we can see that they are clearly higher (131.2 in Spain and 139.1 in Catalonia).



The Andorran economy: general developments

IV. Population, employment and education

1. Population and migratory flows

Since 2009, there are two resources concerning Andorra's population. On the one hand, the historical resource of the commune census, the so-called "registered population", describes a population which is registered but might not be resident in the country. On the other hand, the Department of Statistics of the Government publishes "estimated population" data, which it prepares monthly since 2009, based on communication and crossing-checking of census data between official bodies and the communes.

The registered population at the end of 2016 is 78,264, although the real population is estimated to be 73,105.

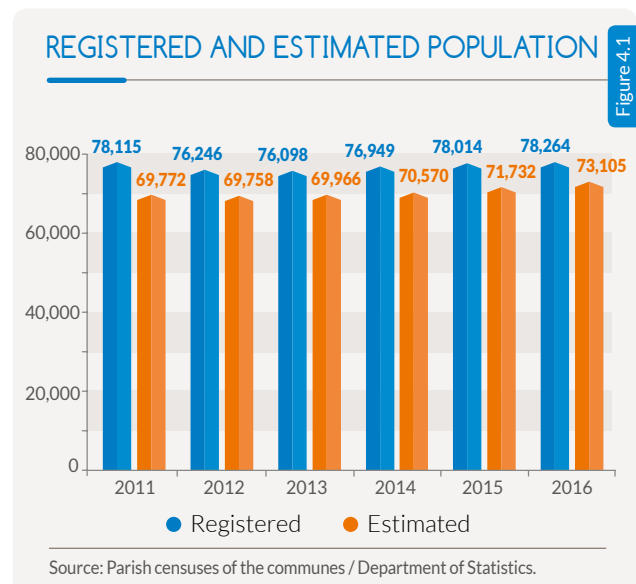
The registered population of Andorra at the end of 2016 was 78,264, 0.3% higher than in 2015 (78,014). This is the highest figure in the last six years, continuing the rising trend which started in 2014, after the contraction seen in previous years as a result of the process of purging the census, and the population adjustment which occurred after the economic crisis.

For their part, the estimated population figures show a population increase of 1.9% compared with 2015 figures (+1,373), putting the Andorran population in 2016 at 73,105. Most probably, the registered population overestimated the real population. In this report, we mostly use the Government data (estimated population) for the purpose of calculating the indicators.

As can be seen in diagram 4.1, the percentage gap between the registered and estimated population is +7.1% (+5,159 people). In 2015, the difference was +8.8%. In any case, these are much lower percentages than in 2010, when the difference was +20.9%, the highest figure it reached, which has not stopped falling.

This gradual shrinking of the gap between estimated and registered population shows that the purging and reviewing of the parish censuses, carried out over the last few years, is on the right track.

So, if we compare the registered population data with the estimated population data by parish, we can see that those that are most overestimated are Canillo, with +18.8% (690 people), La Massana with +13.4% (+1,253 people) and Encamp with +12.5% (+1,375 people). In contrast, Andorra la Vella, with +2.1% (+456 people) and Escaldes-Engordany, with +3.4% (+473 people), are the parishes with the smallest disparities.



REGISTERED AND ESTIMATED POPULATION BY PARISH

Table 4.1

Parishes	REGISTERED POPULATION				ESTIMATED POPULATION			
	2015	2016	Variation 16/15	% total 2016	2015	2016	Variation 16/15	% total 2016
Canillo	4,124	4,360	5.7%	5.6%	3,368	3,670	9.0%	5.0%
Encamp	12,212	12,338	1.0%	15.8%	10,857	10,963	1.0%	15.0%
Ordino	4,687	4,810	2.6%	6.1%	4,429	4,577	3.3%	6.3%
La Massana	10,359	10,571	2.0%	13.5%	9,096	9,318	2.4%	12.7%
Andorra la Vella	22,886	22,128	-3.3%	28.3%	21,428	21,672	1.1%	29.6%
Sant Julià de Lòria	9,379	9,536	1.7%	12.2%	8,681	8,857	2.0%	12.1%
Escaldes-Engordany	14,367	14,521	1.1%	18.6%	13,873	14,048	1.3%	19.2%
Total population	78,014	78,264	0.3%	100%	71,732	73,105	1.9%	100%

Source: Parish censuses of the communes / Department of Statistics.

According to the estimated population data, the increase in population was generalised in all parishes, as occurred in both 2014 and 2015. The highest increases can be seen in the two highest parishes (Canillo +9.0% and Ordino +3.3%). In contrast, Encamp shows the lowest populational increases (1.0%), and both Andorra la Vella and Escaldes-Engordany grew less than the average. Of note is the fall in population of 3.3% in Andorra la Vella, according to the registered population data, a result of the process of purging and reviewing the Comú census, which was carried out in 2016.

Nevertheless, Andorra la Vella remains by far the most populated parish, with 29.6% of the total estimated population of Andorra (21,672 inhabitants). On the other hand, the least-populated parishes are the two highest parishes (Canillo 3,670 inhabitants and Ordino 4,577 inhabitants).

The population increase has been spread across all parishes.

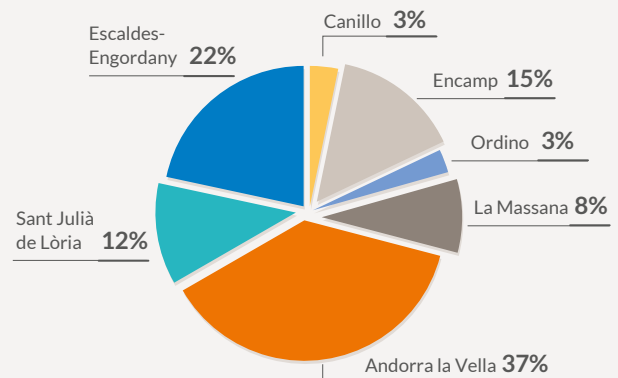
A trend can be seen towards a stabilisation of the distribution of population between the high, less-populated parishes and the low parishes. So, over the last five years (2012-2016), the estimated population of the high parishes has varied between 38.5%-39.0%, less than the 41.0% obtained from the registered population data, but well over the 29.1% which they represented at the start of the nineties. In contrast, the low parishes concentrate 61.0% of the estimated population, a percentage that falls to 59.0% with the registered population data.

The distribution by nationalities reflects the fact that Andorra's rise in estimated population can be explained by the increase in Andorran nationals by 1.2% and the foreign population by

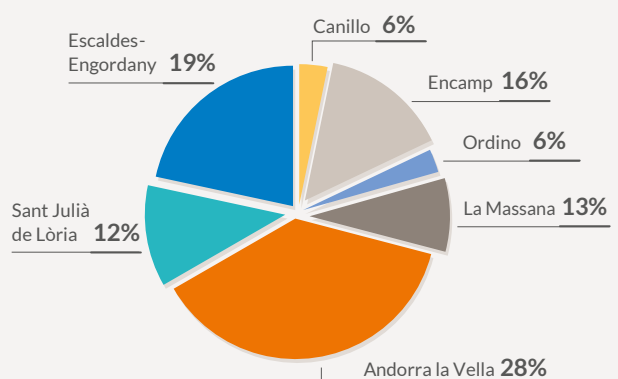
ANDORRA'S REGISTERED POPULATION BY PARISH

Figure 4.2

1991



2016



Source: Parish censuses of the communes / Department of Statistics.

REGISTERED AND ESTIMATED POPULATION BY NATIONALITY

Table 4.2

	REGISTERED POPULATION				ESTIMATED POPULATION			
	2015	2016	Variation	% total	2015	2016	Variation	% total
			16/15	2016			16/15	2016
Andorrans	35,750	36,138	1.1%	46.2%	36,132	36,575	1.2%	50.0%
Foreigners	42,264	42,126	-0.3%	53.8%	35,600	36,530	2.6%	50.0%
Spanish	20,577	20,652	0.4%	26.4%	17,512	18,064	3.2%	24.7%
French	3,890	3,946	1.4%	5.0%	2,834	2,968	4.7%	4.1%
Portuguese	10,697	10,300	-3.7%	13.2%	9,261	9,196	-0.7%	12.6%
Others	7,100	7,228	1.8%	9.2%	5,993	6,302	5.2%	8.6%
Total population	78,014	78,264	0.3%	100%	71,732	73,105	1.9%	100%

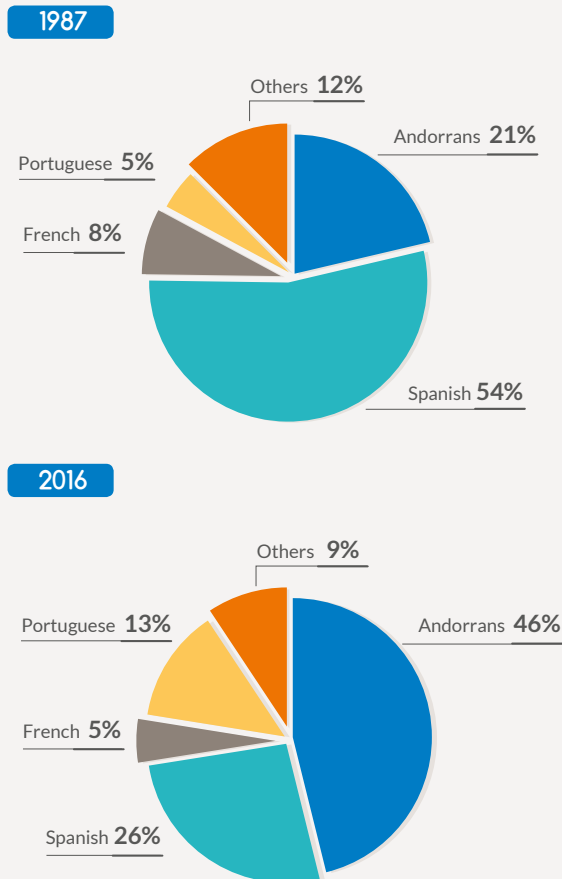
Source: Parish censuses of the communes / Department of Statistics.

2.6%. In 2010 (the start of the historical series), foreigners represented 52.1% of the total population while in 2016 they represented 50.0% (53.8% according to the registered population). Since 2014, both the numbers of Andorrans and foreigners have risen, although the proportion of Andorrans to foreigners has remained quite stable.

The decrease in the number of foreigners according to the registered population was therefore the consequence of the process of purging and reviewing the census and not the real population trend.

ANDORRA'S REGISTERED POPULATION BY NATIONALITY

Figure 4.3



Source: Parish censuses of the communes / Department of Statistics.

By nationalities, the only decrease according to the estimated population data was in the number of Portuguese (-0.7%), continuing the falling trend of recent years. In effect, citizens of Portuguese nationality have gone from representing 15.4% of the estimated population in 2010, to 12.6% in 2016.

For their part, the number of Spanish, which is the largest foreign group, grew 3.2% in 2016. Their share of the total estimated population is 24.7%, similar to the share obtained in 2010 (25.1%).

The increase in French was more significant (4.7%). Despite this increase, for the third consecutive year, like the Spanish, their total share of the population remains stable at around 4%.

The other foreign nationalities (among which are notably British, Argentines, Italians, Morrocans and Philippines) together represent 8.6% of the total estimated population (7.3% in 2010). This means an increase of 1,160 foreigners compared with 2010, resulting in growth of 22.6% in the last 6 years.

In 2016, natural population movement was 633 births: 320 boys and 313 girls. This figure

NATURAL MOVEMENT OF THE ESTIMATED POPULATION

Table 4.3

Demographic indicators	2014	2015	2016
Births	639	659	633
Deaths	276	282	310
Natural growth	363	377	323
Birth rate (per thousand)	9.055	9.187	8.659
Death rate (per thousand)	3.911	3.931	4.240
Natural growth rate (per thousand)	5.144	5.256	4.418
Increase from migration or census regularisation	241	785	1,050
Population increase*	604	1,162	1,373
Marriages	271	285	295

*Natural growth plus migratory increase.

Source: Parish censuses of the communes / Department of Statistics.

represents a fall of 3.9% compared with the previous year's data. The birth rate reached 8.66 per thousand of estimated population. The average age of mothers was 33.35.

In 2016, there were 310 deaths: 174 men and 136 women. This volume represents an increase of 9.9% against registered deaths in 2015. By gender, 56.1% of the deaths were men and 43.9% were women. The average age at the time of death is 75.81 (72.53 for men and 80.01 for women). The death rate has increased since the previous year and stands at 4.24 deaths per thousand inhabitants of Andorra.

This natural movement puts natural growth of the Andorran population at a positive rate of +323 persons, despite the deceleration in the natural growth rate, which went from 5.26% in 2015 to 4.42% in 2016. To these data must be added the positive balance of migratory movement, 1,050 persons, calculated from estimated population (remembering that migratory movement according to the registered population was negative by 73 persons), which saw a total net increase of 1,373 persons.

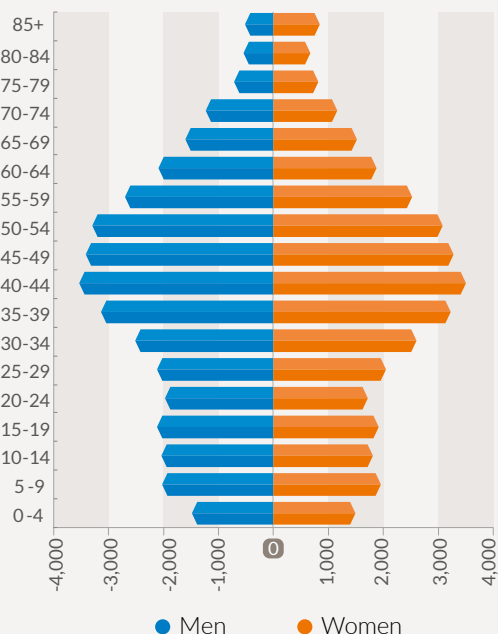
As for the population structure by age and gender, the population pyramid shows that the majority of the population is concentrated between the ages of 30 and 59, in both genders, while the base of the pyramid and up to the age of 29 has a columnar structure. 72.0% of the population is concentrated in the 15-64 bracket; the population under the age of 15 represents 14.8% and the population over 64 represents 13.2%.

The number of men exceeds the number of women in all working age brackets, except in the 30-39 age bracket and especially in the over-75 age bracket. In fact, 56.8% of the population over the age of 75 are women. This gap is accentuated in the higher age brackets: from the age of 85, only 37.8% are men.

The dominance of the male population in the working age brackets tends to become less

STRUCTURE OF THE ESTIMATED POPULATION BY AGE AND GENDER. 2016

Figure 4.4



Source: Parish censuses of the communes / Department of Statistics.

marked. In fact, the difference between the percentages of male and female populations is about one point. Note that the greater presence of men can be explained by the importance of the foreign workforce which has traditionally been male.

The number of foreigners easily exceeds Andorrans in all age brackets from the age of 30.

On analysis of the relation between Andorrans and foreigners by age brackets, we can see that the presence of foreigners is clearly higher than Andorrans in all age brackets from the age of 30. In contrast, the proportion of Andorrans is much higher in the 0-29 age bracket (making up almost 73% of the total population). In contrast, the population of Andorrans is no higher than 35% of the total population in any age bracket after the age of 65.

In 2016, the increase in the population of Andorra occurred in the 45-74 age bracket (3.3%). In contrast, among the population in the 0-44 age bracket, it fell by -1.5%. In fact, a new historical high has been reached in terms of the average age of the population, at the age of 40.96. This population structure shows an aging population. In any case, it is important to highlight the differences between parishes, which vary from 41.67 in Andorra la Vella to 37.82 in Ordino, the parish with the youngest average age.

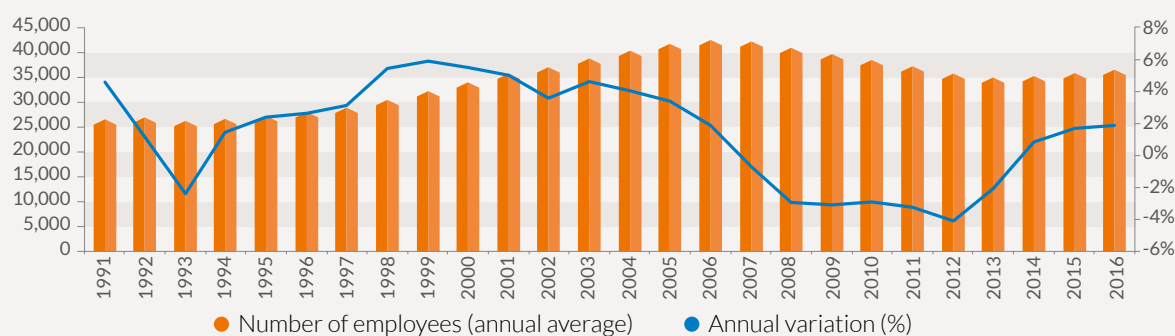
The aging population (given the increase in the average age of the population and the falling birth rate) presents a major risk to financing public pensions and also financing the expected increase in health spending. These factors are analysed in the section about the Andorran Social Security System (CASS – see chapter VIII. *Public sector*).

2. Employment and unemployment

The situation of the Andorran labour market in 2016 has developed favourably. In 2016, the annual average number of employees, according to data from the Andorran Social Security System (CASS) and the Department of Statistics, was 36,604, with an increase of 1.9% from the previous year. This is the third consecutive year of increases in employment, which started in 2014, breaking the negative trend that started in 2007, when the number of employees exceeded 42,000. This may indicate a consolidation of the recovery in the labour market. In 2016, therefore, the number of employees stands at a similar level to 2002.

With these data, the employment rate – measured as the number of employees in relation to the registered population aged 15-64 – reaches a value of 65.32%, almost one point more than in 2015

TRENDS IN THE NUMBER OF EMPLOYEES (1991-2016)



Source: CASS / Department of Statistics.

NUMBER OF EMPLOYEES (annual average)

Table 4.4

Number of employees	2015	2016	Var. 16/15 (%)	% total 2016
Agriculture, livestock, hunting & forestry	164	171	4.5	0.5
Industry	1,591	1,615	1.5	4.4
Extraction industries	2	3	13.8	0.0
Manufacturing industries	1,432	1,452	1.4	4.0
Production & distribution of electricity, gas & water	157	160	2.1	0.4
Construction	2,758	2,816	2.1	7.7
Services	31,415	32,002	1.9	87.4
Commerce & motor vehicle repairs (etc.)	8,667	8,754	1.0	23.9
Hotels & catering	4,553	4,702	3.3	12.8
Financial system	1,960	1,947	-0.7	5.3
Real estate activities & business services	4,358	4,571	4.9	12.5
Public administration, defence & mandatory social security	4,405	4,317	-2.0	11.8
Others	7,472	7,711	3.2	21.1
Total	35,928	36,604	1.9	100

Source: CASS / Department of Statistics.

(64.38%) and the highest level in the last seven years, except 2011, when the employment rate reached a value over 66%.

The services sector generates almost 88% of total employment in Andorra.

If we make a sector analysis, we can see that rising employment is generalised, with three exceptions: households employing domestic staff, which fell 2.1%; the financial system, where employment fell 0.7%, and public administration, where average employment fell 2.0%.

The services sector generates almost 88% of total employment in the Principality. Specifically, “health and veterinary activities, social services” (with an increase of 6.6%), “education” (6.0%), “real estate activities and business services” (4.9%), “transport, storage and communications” (4.3%), and “hotel activities” (3.3%), are the activities where employment increased most.

For its part, the construction sector, which generates 7.7% of total employment, also shows an increase against the previous year, of 2.1%. The industrial sector, which holds 4.4% of total employees, grew 1.5% against 2015.

Many of these figures are the result of the improvement in Andorra's economic situation with the inertia of improvement in neighbouring economies, and the impetus from programmes to promote employment that are being pushed by the Andorran public sector, with the following objective: to progressively introduce a personalised, integrated itinerary system of job orientation, aimed at all those registered with the Job Service; to bolster access to work for those struggling to enter the labour market, and to increase the efficiency in the use of public resources assigned to the programmes of active employment policies and allocate them according to needs and the socioeconomic context at any one time.

The active programmes to promote employment in 2016 were:

Programme promoting permanent contracts in the private sector, giving grants of 250 euros per month, for fifteen months, to businesses that employ workers who can prove at least 150 hours of training related to the job and/or at least one year's professional experience in the five years preceding the intervention.

Programme to promote employment and training in the private sector giving, in the first stage, a grant of 550 euros per month, for up to six months (plus a maximum single payment of 300 euros if there is theoretical training) and, at a second stage, in the case of a permanent contract, a grant of 250 euros per month, for up to six months. This is for workers with less than 150 hours of training related to the job and/or at least one year's professional experience in the last five years.

Programme to promote employment in distant geographical areas. In this case, a grant of 200 euros per month is given, for a maximum of twelve months, to businesses that employ a worker on a permanent contract (through an initial permanent contract or else a temporary six-month contract followed by a permanent contract), and also an individual economic allowance for the worker related to the cost of transport between home and work.

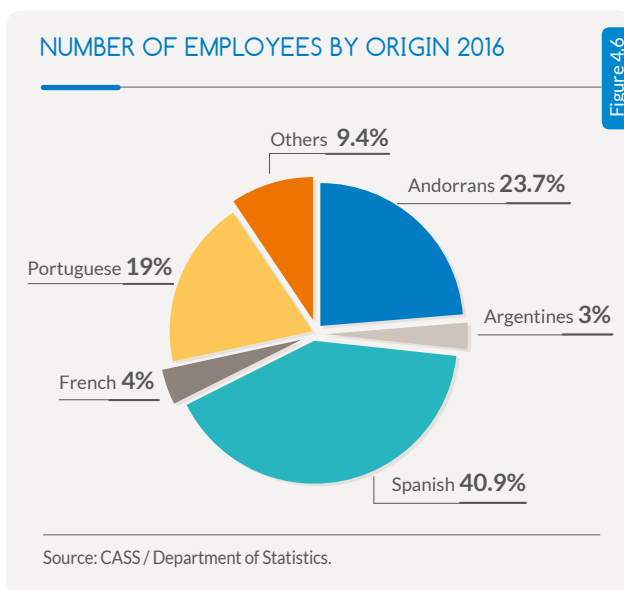
Programme to improve employment through the public sector, aimed at promoting employment from groups of people with difficulties entering work: over 45s, 18-25s looking for their first job; emancipated minors, long-term unemployed and disabled persons.

Programme to promote employment and practical training within the company for active youths aged 16-20, the beneficiaries being the communes, semi-public bodies, public companies, non-profit making entities or businesses that employ youths aged 16-20 who have successfully carried out a training course to improve their employability. In this programme, a grant of 550 euros per month is given at the first stage, for up to six months (plus a maximum single payment of 300 euros if there is theoretical training) and, at a second stage, a grant of 400 euros per month, for up to six months.

By gender, the increase in employment in 2016 was very balanced, with female employment rising (1.9%), one tenth more than male (1.8%), and a division between workers of 49.4% and 50.6%, respectively. But this distribution no longer appears equitable if the data are broken down by sector. So, the sectors with most male workers are construction (89.6%), energy (77%) and transport and agriculture (66%). In contrast, the sectors most held by women are households employing domestic staff (93%), health and veterinary activities, social services (80%), domestic work for communities (79%) and education (72%).

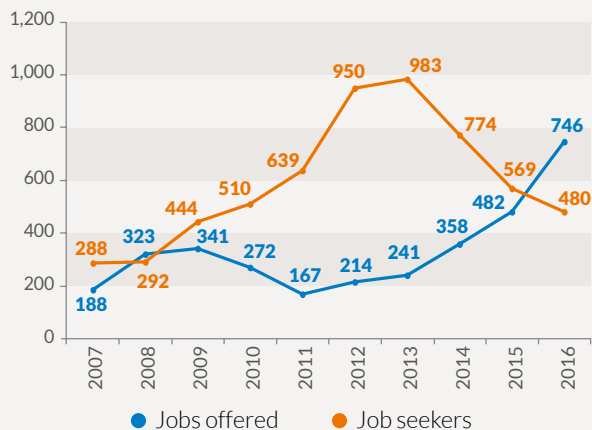
If we analyse the data on employees based on nationality, almost one fourth of those in employment are Andorrans, although the bulk of employees are Spanish (41%). As for the trend in both of these groups, the percentage of Andorrans has increased 8 percentage points since 2004, while the number of Spanish employees has decreased, by precisely 8 percentage points over the same period 2004-2016. The Portuguese stand out as the third group, representing 19% of total employment.

In 2016, there were 607 job seekers, the lowest figure in the last eight years. By components, the number of job seekers looking for work stands at 480 (a drop of 15.7% compared with the last year). For their part, the number of job seekers looking for a better job fell to 128 (19.3% less than in 2015).



JOBS OFFERED AND JOB SEEKERS REGISTERED WITH JOB SERVICE. 2016

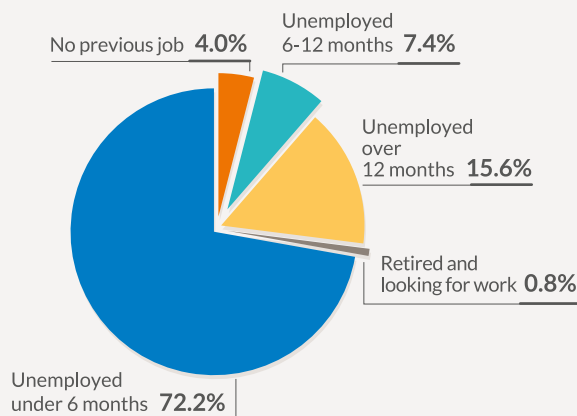
Figure 4.7



Source: Department of Labour / Department of Statistics.

JOB SEEKERS BY EMPLOYMENT SITUATION. 2016 (% of total)

Figure 4.8



Source: Department of Labour / Department of Statistics.

In parallel, the number of jobs offered at the Job Service continue to rise steeply, with an increase of 55% to 746, the highest figure in the historical series (available since 2007). This trend seems to indicate an improvement in the employment provisions of businesses, in keeping with a more favourable economic context. So, the number of jobs offered exceed the number of job seekers for the first time since 2007.

The number of jobs on offer exceeds the number of job seekers for the first time since 2007.

The improvement in the trend in the labour market was reflected in a drop in the number of receivers of unemployment benefit, an accumulation of six years of decreases. Specifically, the number of people receiving financial benefits for involuntary unemployment went from 57 to 51 in the last year, representing a fall in the indicator of 10.7%. As a result, the coverage rate for job seekers went from 10.1% to 10.7% in the last year.

If we focus on the employment situation of job seekers we can see how, for yet another year, the bulk of job seekers have been unemployed for less than 6 months (72.2%), a figure that has fallen 3 points against the previous year. In contrast, those who have been unemployed for more than one year have increased 1.3 percentage points, to become 15.6% of total job seekers. The same increase (1.3 points) occurred in the group of job seekers who have been looking for work for between 6 and 12 months, who represent 7.4% of the total.

3. Education

During the 2015-2016 academic year, the student population in Andorra, including the school, university and non-university population abroad, was 12,606, 0.2% less than the figure for the previous year. This downturn can be explained by both the decline in the non-university population abroad (-5.3%) and the university population (-2.5%) – which includes students in higher vocational education, falling for the third consecutive year. For its part, the school population increases for the third consecutive year but by only 0.2%. These data are consistent with the population structure for these age brackets.

In any case, the population at school level represents 87.4% of the total, while the university population represents 10.4% and is still losing importance for the fourth consecutive year. For its part,

STUDENT POPULATION BY EDUCATIONAL LEVELS

Table 4.5

	2014-15	2015-16	% total year 2015-16	% variation 15-16/14-15
School	10,986	11,013	87.4%	0.2%
University	1,342	1,308	10.4%	-2.5%
Non-university abroad	301	285	2.3%	-5.3%
Total	12,629	12,606	100%	-0.2%

Source: Ministry of Education and Higher Education.

STUDENT POPULATION BY COUNTRY OF STUDY

Table 4.6

	2014-15	2015-16	% total year 2015-16	% variation 15-16/14-15
Andorra	11,418	11,474	91.0%	0.5%
Spain	902	851	6.8%	-5.7%
France	268	247	2.0%	-7.8%
Others	41	34	0.3%	-17.1%
Total	12,629	12,606	100%	-0.2%

Source: Ministry of Education and Higher Education.

the non-university population abroad, which has been moving consistently at about 2% for the last eight years, was 2.3% this year.

By country of study, it can be seen that the number of students studying in Andorra increased for the third consecutive year (0.5% in 2016) to reach 11,474, the highest figure in the twenty-five-year study. In 2016, these students represented 91% of the student population.

Andorrans who study in other countries do so mostly in Spain (6.8% of the total), with a drop in the number of students, for the fourth consecutive year, this time by 5.7%. The percentage of Andorran students in France also fell compared with the previous year and stands at 2.0%, with a drop in students of 7.8%. The distribution by countries of study is completed by 34 students spread among other countries, 17.1% less than in the previous year.

3.1. School population

During the 2015-2016 academic year, there were 11,013 students at school level, a figure that represents a small increase of 0.2% compared with the previous year. This trend raised the total student population to 87.4%.

The Andorran educational system still has the highest number of students, with 39% of the total.

86.6% of school students are concentrated in kindergarten, primary and secondary education, almost one percentage point less than in the previous year, which is the lowest level in the last nineteen years. By sub-groups, the drop in students at kindergarten (-3.6%) and students in secondary education (-2.4%) stands out. In contrast, the number of students in primary education rose 2.0%.

For their part, baccalaureate and vocational students show major increases (7.6% and 7.2%, respectively), the highest figures in the whole series in the case of vocational education, and the highest for almost twenty years in the case of baccalaureate. This means that the percentage of baccalaureate students in the total student population has risen seven tenths to 9.6%; in the case of vocational students, their percentage of the total student population stands at 3.8%.

Analysis of the trend in the school population by type of education shows that since the 2006-2007 academic year, the Andorran educational system is progressively consolidating the largest number of students, followed by the French and lastly, the Spanish system.

In the 2015-2016 academic year, the Andorran educational system still had the largest number of students, with 39% of the whole student population, although, compared with the previous

STUDENT POPULATION BY LEVELS

Table 4.7

	2014-15	2015-16	% total year 2015-16	% variation 15-16/14-15
Kindergarten	2,427	2,340	21.2%	-3.6%
Primary education	4,164	4,248	38.6%	2.0%
Secondary education	3,022	2,949	26.8%	-2.4%
Baccalaureate	982	1,057	9.6%	7.6%
Vocational education	391	419	3.8%	7.2%
Total	10,986	11,013	100%	0.2%

Source: Ministry of Education and Higher Education.

year, the number of students who chose this option fell 0.7%. It is notable that the behaviour of the two areas within this system has diverged greatly: while the number of students in vocational training is still growing (9.2% compared with the previous year), the number of students registered at the Andorran School has fallen 1.1% compared with the previous year.

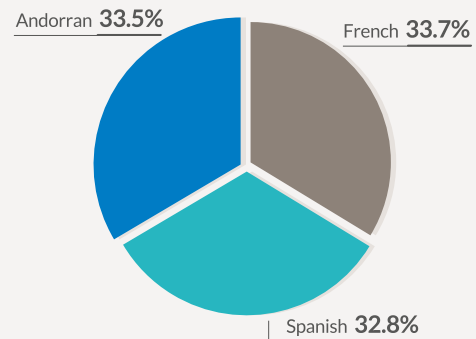
In the case of the Spanish educational system, after nine consecutive years of falls, the number of students in this year increased 0.4%. In this way, its percentage of the total school population stayed at 28%. If we look more closely at the Spanish educational system we can see that the number of students in Spanish schools continues to fall (-2.1% in this year), while the number of students in congregational schools increases (0.8%), as do students in private schools (4.0%).

For its part, the number of students in the French educational system increased 1.3%, putting its share of the total school population at 32.6%, three tenths more than the previous year and the highest level in the last eight years.

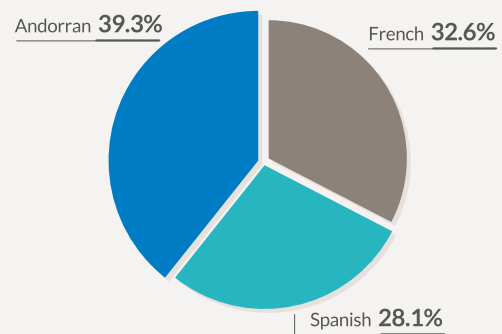
ANDORRA'S SCHOOL POPULATION BY EDUCATIONAL SYSTEM

Figure 4.9

2005-2006



2015-2016



Source: Ministry of Education and Higher Education.

3.2. University population

The Andorran university population in the 2015-2016 academic year was 1,308, 2.5% less than in the previous year. This is the third consecutive year of falling numbers of university students. By gender, women are still the majority, as they represent 54.2% of the total.

The distribution by countries of study shows that the drop in student numbers has affected all destinations abroad. The most significant downturn was recorded in France, with a fall of 12.8%: from 203 university students from Andorra who studied in France in the previous year to 177 in the 2015-2016 year, a figure that represents 13.5% of the total. In Spain, they fell 5.2% and this

Spain is still the main destination for Andorran university students.

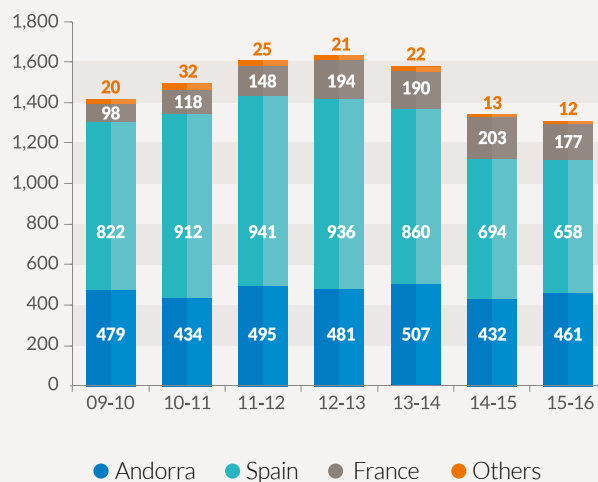
is the fourth consecutive fall. However, it is still the main destination for Andorran university students, receiving 658 students (representing 50.3% of the total). In second place are students who study at the University of Andorra, with a concentration of 35.2%, an increase of 6.7% compared with the previous year.

To complete the analysis, the 0.9% of other students – i.e. 12 individuals – are spread among other countries (Argentina, USA, Portugal, United Kingdom and Switzerland).

The distribution by field of studies reflects the fact that the field with most university students from Andorra is still that of social sciences, business studies and law, concentrating 43.4% of total university students, with 568 students. Next are health sciences and social services (16.2%), engineering, industry and construction (12.9%) and arts & humanities (8.6%). With a lower percentage are education (7.3%), science (6.1%) and services (5.0%), and agriculture comes last with just 7 students (0.5% of the total).

UNIVERSITY POPULATION BY COUNTRY OF STUDY

Figure 4.10



Source: Institute of Andorran Studies.

V. Activity and demand

1. Developments in economic activities in 2016

In 2016, Andorra continued along the path to economic recovery that began in 2013, with a slight acceleration in the rate of activity, although still far from the levels of the previous expansionary phase. This moderately positive trend was evident in an improvement in the main available indicators of activity, although levels were still modest.

The recovery in the Andorran economy that has been seen in recent years was favoured, to a large extent, by the progressive improvement in the international context, above all in the Eurozone, and more specifically in Spain. This impetus was partly offset by problems of a domestic nature, suffered by the financial sector in the last two years, concerning the administration of Banca Privada d'Andorra (the so-called BPA affair) in March 2015, and the subsequent process of ordered resolution of the entity, which ended mid-2016.

From the perspective of demand, in 2016 there was a moderately positive trend in the most relevant indicators related to consumption and investment, with an especially notable contribution from foreign demand. From the perspective of supply, Andorran economic growth was still led by services, especially activities linked to commerce and tourism which, in turn, depend fundamentally on a good performance in foreign demand. The contribution from construction should also be noted, finally showing a positive if moderate trend, after nine years of very deep crisis in the sector. The performance of agriculture also discretely improved, while industrial activity continued to appear weak.

SUMMARY OF INDICATORS OF ACTIVITY AND DEMAND (Interannual variation rates, %)

Table 5.1

Activity	2015	2016
Businesses ⁽¹⁾	6.2	5.0
Establishments ⁽²⁾	5.4	5.6
Employees	1.7	1.9
Industry	2.0	1.5
Construction	0.9	2.1
Services	1.7	1.9
Job seekers	-26.5	-15.7
Number of visitors	0.7	2.6
Electricity consumption ⁽³⁾	0.7	2.8
Imports	-0.6	4.9
Demand		
Average wage	-3.0	4.3
Car registrations	10.8	10.5
Industrial vehicle registrations	9.9	30.0
Imports of capital goods ⁽⁴⁾	4.7	1.9
Imports of building materials ⁽⁵⁾	7.2	-1.6
Credit from banking entities ⁽⁶⁾	-1.3	-0.4
Operating costs of the Administration ⁽⁷⁾	2.6	2.0
Real investment of the Administration ⁽⁷⁾	27.3	-17.0

(1) Excluding "Households employing domestic staff" and "Voluntary declarants (no activity)".

(2) Establishments registered on the Trade and Industry Register that carry out a commercial, industrial or services activity.

(3) Except domestic use, public lighting and other distributors.

(4) Includes chapters 84 and 85, according to the Andorran Customs classification.

(5) Includes chapters 25, 68, 72 and 73, according to the Andorran Customs classification.

(6) Net lending to customers.

(7) Settled figures. Includes Government and communes.

Source: own preparation.

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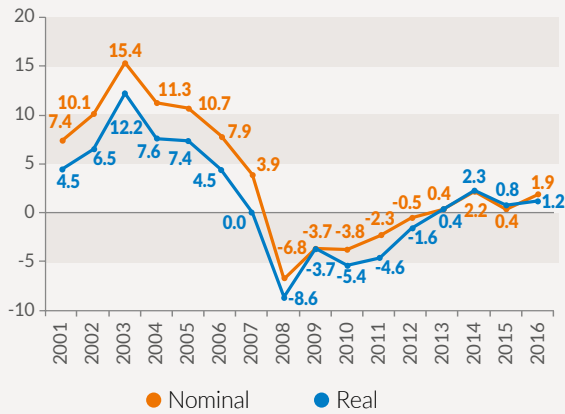
The pace of the Andorran recovery can be seen in the upward trend in most indicators of activity and demand. Among the most relevant are notably the increases in imports without fuels (7.5%), the number of visitors (2.6%) and employment (1.9%), all higher than in 2015. Also significant was the dynamic in car registrations (10.5%) and industrial vehicles (30%), the number of businesses (5%) and establishments (5.6%) and electricity consumption (2.8%). The few indicators where the upward trend slowed, such as administrations' operating costs (2%) and imports of capital goods (1.9%), are still positive.

Other signs of the progressive strengthening of the Andorran economy come from the dynamics of the labour market, being a delayed indicator of activity. So, as well as job creation, wage growth stands out (4.3%), clearly above inflation (0.4%) – after several years of adjustment – and there is a notable fall, for the third consecutive year, in the number of job seekers (-15.7%). All this demonstrates, moreover, more favourable conditions for residents' consumption. The negative tone of 2016 can still be seen in the trend in bank lending, although the rate of fall slowed to -0.4% interannual, after the adjustments caused by the BPA affair in the banking sector in 2015. In conclusion, the recovery of the Andorran economy continued to progress slowly in 2016 and is gradually extending to all economic activities.

This trend is reflected in the first estimate of GDP published by the Government, which shows growth of 1.2% in real terms, higher than the increase of 0.8% recorded in 2015. In nominal terms,

TRENDS IN ANDORRAN GDP Interannual variation rate (%)

Figure 5.1



Source: Department of Statistics.

Official GDP figures for 2016 show real-term growth of 1.2%, higher than the 0.8% increase seen in 2015.

the rise in GDP for the whole of the financial year was 1.9%, a percentage that includes the positive trend in prices in 2016, unlike the previous two years. This increase represents acceleration compared with 2015 (0.4%) and puts the total nominal GDP figure at 2,584.1 million euros, the highest value since 2009.

Specifically, this year, official GDP figures include two notable innovations. On the one hand, an estimate of the trend per quarter is published

for the first time, to be updated periodically, and on the other hand, sectoral disaggregation is limited to the four major sectors (agriculture, industry, construction and services) and three services subsectors, according to the European economic activities classification (NACE Rev. 2), which are: Commerce, transport, hotels & catering, information and communications; Financial, real estate, professional and technical activities, and Public administrations, education, health, social and personal services. Towards the end of each year, it is intended to publish a semi-definitive estimate of GDP figures, which are likely to include greater sectoral disaggregation.

Analysing GDP by quarter throughout the financial year, it can be seen that the economy started the year strongly (at an interannual growth rate of 1.8% in the first three months), but lost impetus in the second and third quarters (at a rate of 1%), to end the year rising a little (1.2% in the fourth quarter).

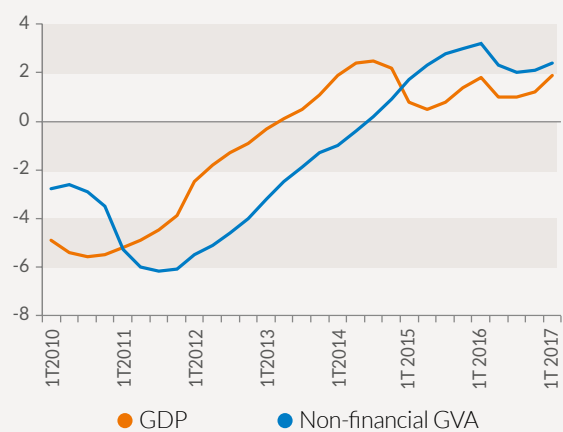
So, the economy saw four consecutive years of growth after seven years of crisis and economic losses that still put the value of current real GDP (1,924.8 million euros) at about the level it was in 2003, and 18% lower than the maximum it reached in 2007. To be specific, the trend in the Andorran economy over the last two years was affected by a domestic financial crisis, deriving from the BPA affair, so if we exclude the financial sector from the global trend, the rate of growth of the real economy (non-financial GVA) was double (2.4%).

Official Andorran GDP growth in 2016 was the same as for France (1.2%), but remained well below Spanish GDP (3.2%) and, to a lesser extent, the whole of the EU (1.9%), while population growth in Andorra was significantly higher than in Europe (1.9% and 0.4%, respectively).

Consequently, we can state that Andorra continued to lose relative positions compared with neighbouring economies in relation to the level of per capita wealth. According to official

QUARTERLY TREND IN GDP AND NON-FINANCIAL GVA IN ANDORRA Interannual variation rate (%)

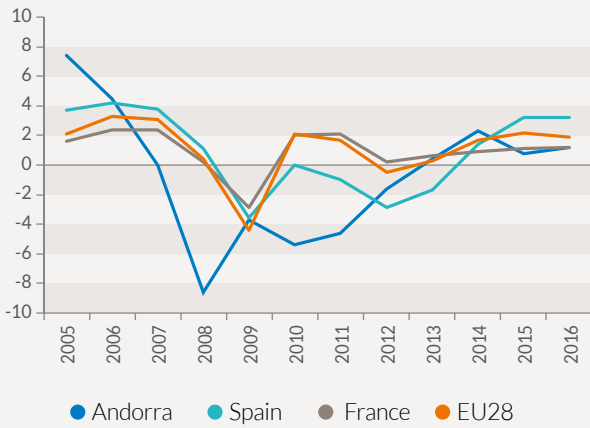
Figure 5.2



Source: Department of Statistics.

TRENDS IN ANDORRAN GDP COMPARED WITH NEIGHBOURING ECONOMIES
Interannual variation rate (%)

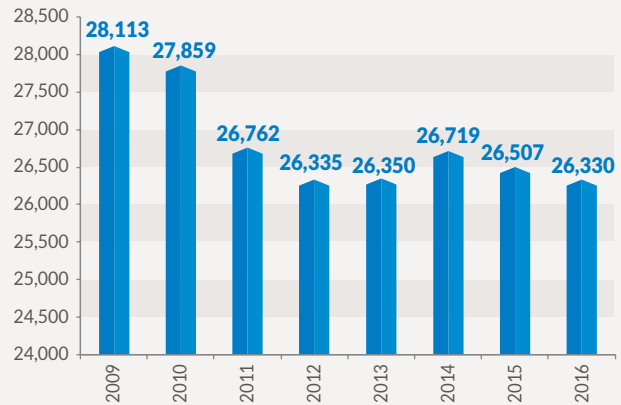
Figure 5.3



Source: Eurostat and Department of Statistics of the Government of Andorra.

ANDORRAN REAL GDP PER CAPITA
In euros (Base year 2000)

Figure 5.4



Source: Department of Statistics.

figures, Andorran per capita GDP stood at 35,348 euros in nominal terms, a similar level to 2015 and its levels in 2012-2013. In contrast, in real terms, per capita GDP fell (-0.7%) for the second consecutive year, to 26,330 euros (base year 2000), a similar figure to those seen in 2012 and 2013.

2. Developments in activities by sector

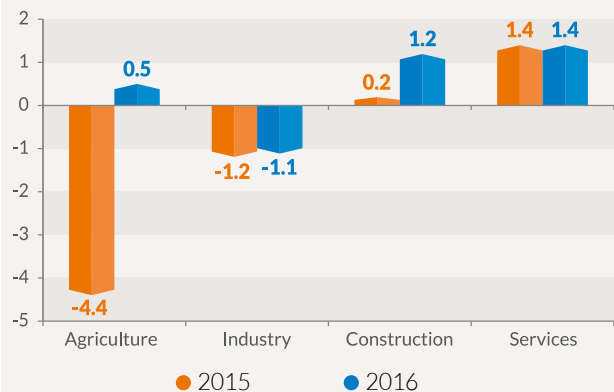
The disaggregation by major sectors shows that Andorran real GDP growth in 2016 was led by services (1.4%), which represent 88.8% of GVA, so their performance is usually determined by the trend in the Andorran economy. In second place, the positive contribution of construction also stands out, for the first time in a decade. In contrast, industry held back economic growth and agriculture made a minimal contribution, due to its low percentage of GVA and a very weak increase in activity.

Up close, the construction sector recorded real GVA growth of 1.2%, compared with the near-stagnation that marked 2015 (0.2%). This upturn, although modest, is significant because it comes after nine years of deep crisis, with major falls in GVA, which fell 60% below the 2006 maximum in 2015. As a result, construction currently represents 5.8% of total GVA, compared with 12.6% before the crisis.

The signs of improvement in construction can also be seen in the trends in most available indicators of activity for the sector. So, in 2016, an acceleration was seen in the rate of job creation (2.1%) and the number of establishments (2.7%), accompanied by an increase in the number of businesses (1.9%) and the average wage for the sector (1.5%). Moreover, the total number of authorised square

TREND IN ANDORRAN GDP BY SECTOR
Interannual variation rate (%)

Figure 5.5



Source: Department of Statistics.

Construction saw real GVA growth of 1.2%, after nine years of deep crisis.

metres saw growth of 50.8%, reaching close to 155,000 m², after many years of steep decline. In parallel, the number of building permits for new works increased 20.7%, although there

were only 35 permits, a figure that contrasts with over 200 permits granted in 2004. So, the rate of progress in activity is still modest and based on very low levels, reflected, for example, in the lack of dynamism in imports of building materials and energy consumption (-1.6% in both cases). Moreover, public investment saw a major downturn in 2016 (-17%), after two years of growth, a factor which limited the chances of improvement in the sector. In contrast, measures such as the Renova Plan, consisting of aid to promote remodelling of properties, improvements in buildings' energy efficiency and the use of renewable energies, are a stimulus to activity in the sector.

Along the same line, the results of the Chamber's surveys show that construction reached a turning point, leaving behind the strong contractionary dynamic, with new signs of reactivation. So, business activity turned upward, with three consecutive weeks on positive ground, while businesses' replies about developments in contracted and executed works have started to show signs of improvement, if at still very low levels. Altogether, this resulted in a slight increase in sales figures (1.3%), for the first time since 2005, and in investment (1.8%), after ten years of major downturns.

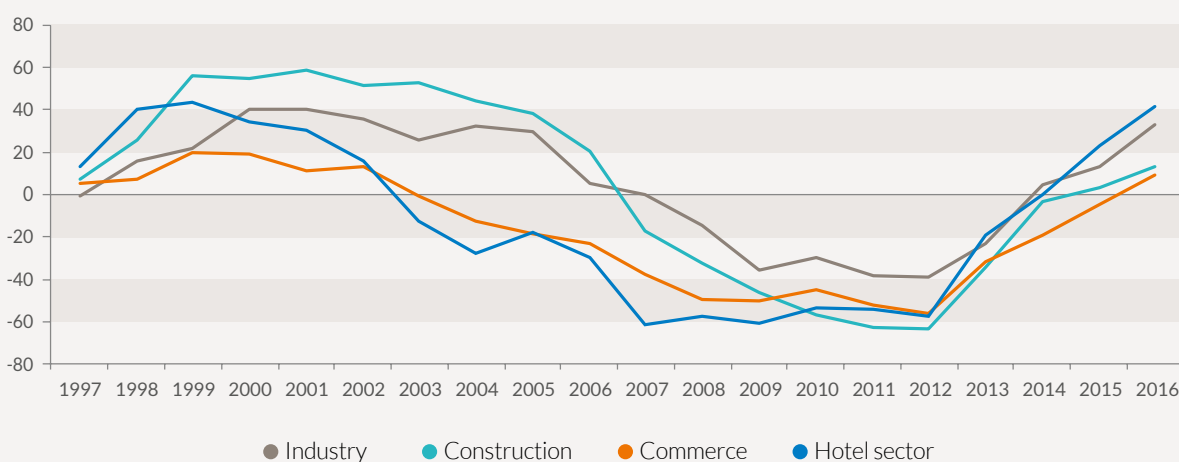
As for the industry and manufacturing sector, the trend in 2016 was still negative, although the rate of fall in activity slowed in comparison with the previous year. So, real GVA fell 1.1%, one tenth less than in 2015, reducing its percentage of total GVA to 4.9%. Remember that this sector consists, on the one hand, of basic industry, based mostly on energy production and distribution, and on the other hand, manufacturing, which is the most significant activity - in 2015, it concentrated 71% of GVA from secondary activities (2016 data are not available).

The rate of decline in activity slowed in industry.

The weakness of industrial and manufacturing activity as a whole that was seen in 2016 resulted in a reduction in the number of businesses in the sector (-0.7%) and a slower rate of job creation (1.5%) and energy consumption (1.2%). However, a trend has also been seen towards a gentle improvement in the climate of confidence in the sector, reflected in businesses' replies to the

TREND IN BUSINESS ACTIVITY BY SECTOR
Balance between the percentage of positive and negative replies

Figure 5.6



Source: Chamber of Commerce, Industry and Services of Andorra.

Chamber's surveys. Specifically, the confidence indicator recovered a positive balance in the second half of the year, after almost 12 consecutive years on very negative ground. Moreover, businesses' opinions about business activity show the most favourable climate of the last 13 years, while levels of production and the level of productive capacity utilisation improved gently. So, the latter reached about 67%, about 11 points more than the low reached in 2011, but still far from the levels prior to the crisis. In this context, industrial businesses showed an average increase in turnover of 3.6%, higher than in 2015, and a rise in investment (5.1%) that contrasts with the falls of previous years.

As for services, in 2016, these were still the most dynamic sector of the economy, at still modest levels, led once again by the improvement in activities linked to commerce and, above all, tourism. This positive trend was again driven by the increase in numbers of tourists (6.3%) and a slight recovery in same-day visitors (0.7%) which in turn favoured growth in commercial sales. So, the impetus from foreign visitors' demand resulted in progress in goods imports of 4.9%, compared with the slight drop seen in 2015. The upward trend in tourist activity was also evident in the increase in the number of ski days sold (4.4% in the 2015-2016 season and 1.3% in the 2016-2017 season) and the total number of overnight stays (2.6%), although the average length of stay fell slightly (from 2.3 to 2.1 days) – according to the Chamber's surveys. Moreover, the level of hotel occupancy is still rising. Altogether, this resulted in an increase in numbers of employees of 3.3% in hotels & catering and 1% in commerce, which occurs in the latter after ten consecutive years of decline. In parallel, the number of establishments increased at a rate of 3.8% in hotels & catering and 2.9% in commerce.

The most dynamic sector is still services, led by the improvement in activities related to commerce and especially tourism.

The progressive recovery in tourism and commercial activity was also reflected in the Chamber's surveys, with better assessments of business activity than in 2015. The surveys also indicate acceleration in growth of sales figures in hotels (6.1%) and a small increase in commerce (0.9%), which had not happened since 2001.

BUSINESSES' OPINIONS OF ECONOMIC DEVELOPMENTS IN 2016

Table 5.2

Results of the situation survey in industry

2016 COMPARED WITH 2015 (as % of businesses)

Turnover	Higher	49
	Same	34
	Lower	16
	Average variation (%)	3.6
Investment volume	Higher	31
	Same	60
	Lower	9
	Average variation (%)	5.1
Number of employees	More	18
	Same	72
	Less	10

PROSPECTS FOR 2017 (as % of businesses)

Trend in turnover	Upward	43
	Stable	49
	Downward	8
Trend in investment volume	Upward	22
	Stable	62
	Downward	16

Results of the situation survey in construction

2016 COMPARED WITH 2015 (as % of businesses)

Turnover	Higher	34
	Same	42
	Lower	24
	Average variation (%)	1.3
Investment volume	Higher	25
	Same	63
	Lower	13
	Average variation (%)	1.8
Number of employees	More	15
	Same	68
	Less	17

PROSPECTS FOR 2017 (as % of businesses)

Trend in turnover	Upward	21
	Stable	53
	Downward	26
Trend in investment volume	Upward	19
	Stable	45
	Downward	36

Source: Chamber of Commerce, Industry and Services of Andorra.

Results of the situation survey in retail commerce

2016 COMPARED WITH 2015 (as % of businesses)		Total retail commerce	Food	Clothing & Footwear	Household equipment	Health & hygiene	Electronics	Vehicles & accessories	Other commerce	Superm. & dept. stores
Sales figures	Higher	40	33	44	46	43	43	32	41	36
	Same	32	47	25	24	29	21	40	33	36
	Lower	28	20	31	30	29	36	28	27	27
	Average variation (%)	0.9	0.7	-1.3	1.8	3.7	2.9	-0.7	0.9	0.5
Investment volume	Higher	29	30	15	36	33	23	24	29	46
	Same	61	60	73	55	67	69	60	62	36
	Lower	10	10	12	9	0	8	16	9	18
	Average variation (%)	3.3	2.0	0.7	3.9	11.1	3.8	3.6	2.7	2.5
Number of employees	More	11	3	6	21	10	0	0	15	27
	Same	82	94	85	71	67	93	88	83	64
	Less	8	3	9	9	24	7	12	2	9
PROSPECTS FOR 2017 (as % of businesses)										
Trend in sales figures	Upward	34	38	35	28	55	14	30	32	40
	Stable	55	53	56	66	35	71	61	53	40
	Downward	11	9	9	6	10	14	9	15	20
Trend in investment volume	Upward	22	21	14	15	48	8	24	24	18
	Stable	65	62	71	70	52	77	60	63	82
	Downward	13	18	14	15	0	15	16	13	0

Source: Chamber of Commerce, Industry and Services of Andorra.

In the same way, businesses indicated an upward trend in investment in both sectors (9.3% and 3.3%, respectively), stronger than in 2015. In any case, we must remember that these increases come after many years of decreases, which left activity at historically low levels, so they are still far from the levels of the previous expansionary phase.

As a result, real GVA in the subsector Commerce, hotels & catering, transport, information and communications saw two consecutive years of fairly high growth, progressing 4.4%, two tenths more than in 2015, finally leaving behind a phase of seven consecutive years of falls (2008-2014). Consequently, the percentage of this subsector of the economy increased to 31% of total Andorran GVA, having seen historical lows in 2014.

The financial subsector was the only services branch that saw a negative trend, as occurred in 2015. Official GDP figures show a drop in GVA in the subsector Financial, real estate, professional and technical activities, of 0.7% in 2016, which is added to the drop of 0.5% seen in 2015, contrasting with the strong growth of about 10% p.a. in the financial and insurance branch in the period 2012-2014. However, this subsector (which encompasses financial, real estate, professional and technical activities) is still by far the most important in the economy, with a percentage of 38% of total GVA.

The weakness of activity was seen in a reduction in net lending to customers (-0.4%) and deposits (-2%), which resulted in a drop in profits in the banking sector, for the third consecutive year, of 7.5%, and a cut in employment in the financial and insurance sector as a whole (-0.7%). In any case, these figures need to be viewed within the special context that marked the sector over the last two years, regarding Banca Privada d'Andorra (BPA) being put into administration by the Andorran National Institute of Finance (INAF), after 10 March 2015, when the US administrative authority,

BUSINESSES' OPINIONS OF ECONOMIC DEVELOPMENTS IN 2016

Table 5.4

Results of the situation survey in hotel sector

2016 COMPARED WITH 2015 (as % of businesses)

Turnover	Higher	67
	Same	33
	Lower	0
	Average variation %	6.1

Investment volume	Higher	62
	Same	33
	Lower	4
	Average variation %	9.3

Number of employees	More	21
	Same	67
	Less	12

Source of clients per sales channel (as %)	Direct client / own web	22.9
	Internet / booking sites	57
	TO & travel agencies	17.3
	Others	2.8

Average stay of clients (nights)	2.1
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PROSPECTS FOR 2017 (as % of businesses)

Trend in turnover	Upward	55
	Stable	41
	Downward	5

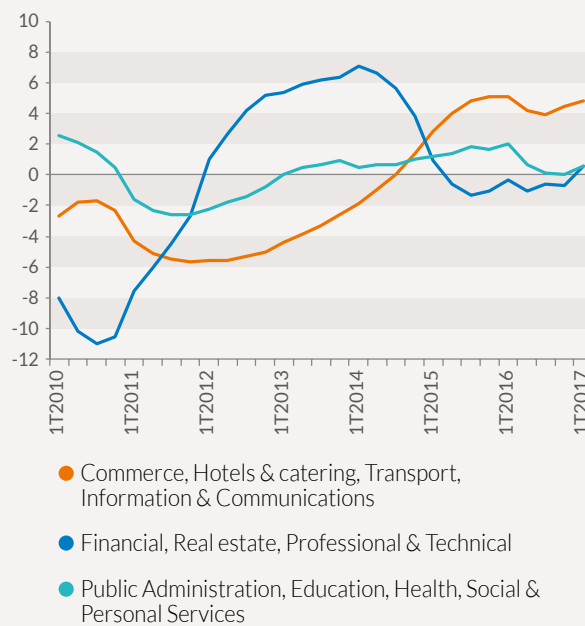
Trend in investment volume	Upward	27
	Stable	61
	Downward	11

Source: Chamber of Commerce, Industry and Services of Andorra.

THREE-QUARTERLY TRENDS IN GVA IN THE SERVICES SECTOR BY BRANCHES OF ACTIVITY

Figure 5.7

Interannual variation rate (%)



Source: Department of Statistics.

The financial subsector was the only services branch that saw a negative trend, as occurred in 2015.

the Financial Crimes Enforcement Network (FinCEN) classified Banca Privada d'Andorra, SA (BPA) as a "financial institution of primary money laundering concern". This started the process of ordered resolution of the entity, which ended in May 2016 with its liquidation and the transfer of clean assets to Vall Banc, which was sold to an American fund.

Analysis of sectoral developments is completed by the primary sector which, in 2016, saw modest growth in real GVA by 0.5%, after three years of quite major falls in activity (-4.4% in 2015). This change in trend was accompanied by an increase in the number of employees by 4.5%, in a context where the agricultural usable surface area and the tobacco harvest both grew (0.9% and 0.6%, respectively). In contrast, the number of livestock fell for the second consecutive year (-5%), but this is in line with the historical average observed since 1995 (about 5,200 heads). In any case, it should be noted that the importance of the primary sector in the economy is very small (0.5%), so its impact on total GDP is very limited.

3. Developments in demand by components

By components of demand, available indicators show, in general, that domestic demand saw an upward trend, from levels that are still low. The increase in population and employment, together with wage growth in real terms (after discounting inflation), generated favourable conditions for

growth in residents' private consumption. This situation was reflected, for example, in an increase in car registrations (10.5%), which was also partly favoured by implementation of the Engega Plan, offering incentives to purchase eco-friendly vehicles.

As for investment, available indicators show that in the field of transport material, there was acceleration in registrations of lorries and vans (30%), while investment in capital goods still appears weak, as deduced from slowing growth in imports of these goods (1.9%). However, the Chamber's surveys reflect a growing trend in investment in all the major sectors of the economy, led by the hotel sector, although progress is slower in commerce, industry and construction. So, it appears that the gradual improvement in the economic context and in business confidence is slowly reactivating investment.

The progressive improvement in the economic context and business confidence is reactivating investment.

In contrast, the contribution from the public sector to activity in 2016 was marked by more restrictive central government fiscal policy, unlike in 2015. Specifically, a moderation in growth in operating costs occurred, of nine tenths, to 2.8%, to which was added a reduction in real investment (-3.2%). Consequently, the increase in non-financial expenditure was limited to 3% in 2016, compared with 7.2% in the previous year. This factor, together with accelerated income growth, partly stimulated by the improvement in the economic situation, resulted in a change in direction in the settled budget balance, which went from deficit (-0.5% of GDP) to surplus (0.9% of GDP). In parallel, the tax burden increased almost two points, to 25.3%, a figure that sets a new historical high and is the result of the culmination of the process of implementing all forms of direct tax brought out since 2011.

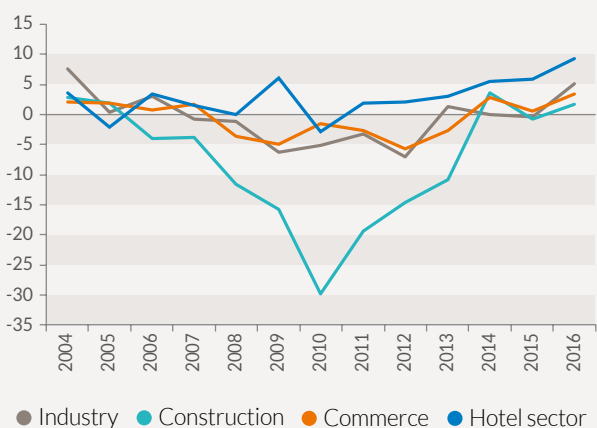
Equally, the communes adopted a clearly contractionary policy, with the reduction in non-financial expenditure of 11.8%, among which is notably the cut in real investment (-51.5%). As a result, the aggregate non-financial surplus of the communes almost doubled, to represent 1.7% of GDP. In this way, the aggregate real investment of the public sector (central government plus communes) fell 17% and the growth in aggregate operating costs slowed six tenths, to 2%. Therefore, overall, the performance of the public sector was clearly restrictive, contrasting with the expansionism it followed in 2015. According to the Government's own estimates, this change in direction in fiscal policy resulted in slower growth in GVA in the subsector

Public administration, education, health, social and personal services, to 0.7% in 2016, contrasting with the increase of 1.5% it saw one year before.

As for the foreign sector, in 2016 there was an increase in imports (4.9%), which contrasted with the slight decline in the previous year. Moreover, it should be noted that this figure is pushed downward by the reduction in oil prices seen in 2016, so if this chapter is excluded, growth in imports was higher (7.5%). In parallel, exports increased, for the second consecutive year, at a rate of 12.6%, so the trade deficit increased 4.4%. So, in 2016, the traditionally negative contribution from the trade balance to national GDP increased, correlating with the improvement

TRENDS IN INVESTMENT BY SECTORS
Interannual variation rate (%)

Figure 5.8



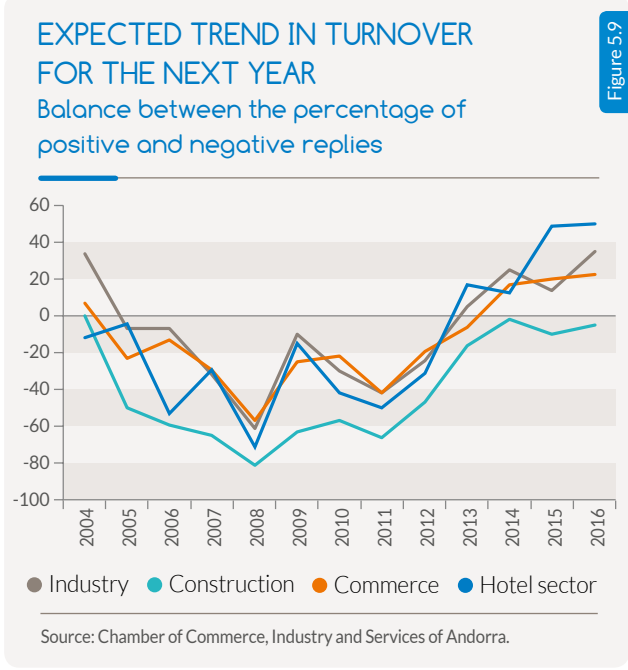
Source: Chamber of Commerce, Industry and Services of Andorra.

in the economic situation. In any case, the most significant contribution from the foreign sector to the Andorran economy is obtained from income from tourism services – the country’s most important source of revenue – which continued the upward trend, as commented in the analysis of the hotel sector made in previous paragraphs. It should be said that this rising trend was driven by the good performance of the neighbouring economies of Spain and France, from where most visitors to Andorra come (51% and 41%, respectively). So, the number of tourists increased 6.3% and same-day visitors 0.7%, and aggregate growth in visitors was 2.6%, higher than in 2015.

To end the analysis of the foreign sector, it should be noted that the new Foreign Investment Law which entered into force in 2012, is having a growing impact in attracting foreign capital to Andorra. So, in 2016, 810 investment applications were received, 8.6% more than in 2015 and the highest figure since the Law came into force.

4. Prospects

As for the prospects for the Andorran economy in 2017, the results of the Chamber’s surveys suggest a new, if moderate, improvement in trends, allowing faith in the gradual consolidation of the economic recovery. By sectors, it is expected that the improvement trend will reach all branches of activity, but with differing intensity. The hotel sector will continue to lead the recovery, while the activity rate will gain momentum more slowly in commerce and industry. So, in all three sectors, positive replies about the trend in turnover and investment for 2017 exceed negatives, more noticeably favourable in the case of hotel activity. For its part, construction is the sector that still poses most doubts about the future, although growing dynamism in the rest of the economy should pull up this sector too in the end.



In 2017, it can also be expected that the impetus from the foreign sector will continue to favour Andorran economic activity, taking into account the high dynamism forecast for the Spanish economy and, to a lesser extent, other European countries. In this context, it is expected that Andorra’s economy will see a new increase in GDP in 2017, which will probably overtake the growth rate observed in 2016.

The GDP data for the first quarter are consistent with this forecast, as they show acceleration in the growth rate to 1.9% interannual, seven tenths more than the previous quarter. The improvement was generalised over sectors, except for agriculture, and is still led in growth by the subsector Commerce, hotels & catering, transport, information and communications (4.8% interannual). Also, notably positive is the start of the upturn in Financial, real estate, professional and technical activities (0.6%), after seven consecutive negative quarters.

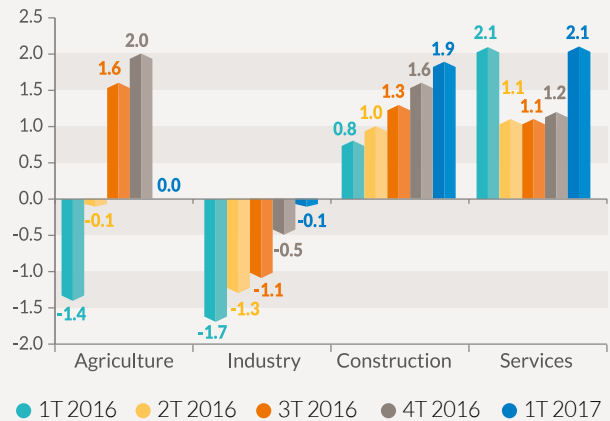
The trend in the main available indicators of activity for the first few months of 2017 also support a forecast of higher economic growth, with a quite generalised upward trend, if within levels that are still moderate. More specifically, employment grew close to 3% in the first four months of the year,

The recovery in the Andorran economy will continue to gain strength throughout 2017.

higher than the increase of 1.6% seen in the same period in 2016, and with a particularly notable contribution from the hotel sector. Along the same line, the rate of total imports, imports of building materials and car registrations accelerated until June. Moreover, the growth in the number of visitors, another key indicator for evaluating Andorran economic activity, remained positive in the first half of the year, although the rate weakened a little in relation to 2016. Only energy consumption stands out with a slightly negative trend, which might be influenced by other factors not directly linked to the economic cycle.

THREE-QUARTERLY TREND IN ANDORRAN GVA BY SECTORS
Interannual variation rate (%)

Figure 5.10



Source: Department of Statistics.

So, the overall view allows us to conclude that the recovery in the Andorran economy will continue to strengthen throughout 2017, led by the tourism sector, and favoured by the good performance of the European economy and, above all, Spain.

VI. Prices and costs

65

1. Consumer prices

After 24 consecutive months of negative values (in interannual terms), inflation, measured by the Consumer Price Index (CPI), reached an annual +0.4% in December 2016, a positive value that represents a clear upturn in comparison with falling prices in December 2015 (-0.9%). From August 2016, the inflation rate started to recover, resulting in a return to positive inflation rates from December, due to rising prices associated with energy and the progressive improvement in economic activities. So, the inflation rate continued to rise during the first few months of 2017 and the Andorran CPI reached 3% in March 2017.

The period of price stagnation in 2013 and 2014, and deflation in 2015 and for much of 2016, was significantly reversed. There was a marked change in trend from the end of 2016. This resembles the international dynamic, especially in the countries closest to Andorra, supporting the approach that global factors have a greater influence on national inflation rates¹ - such as the trend in petrol prices and other raw materials, together with the role of global value chains. Naturally, specific national factors still play an important role, as highlighted by the European Central Bank.²

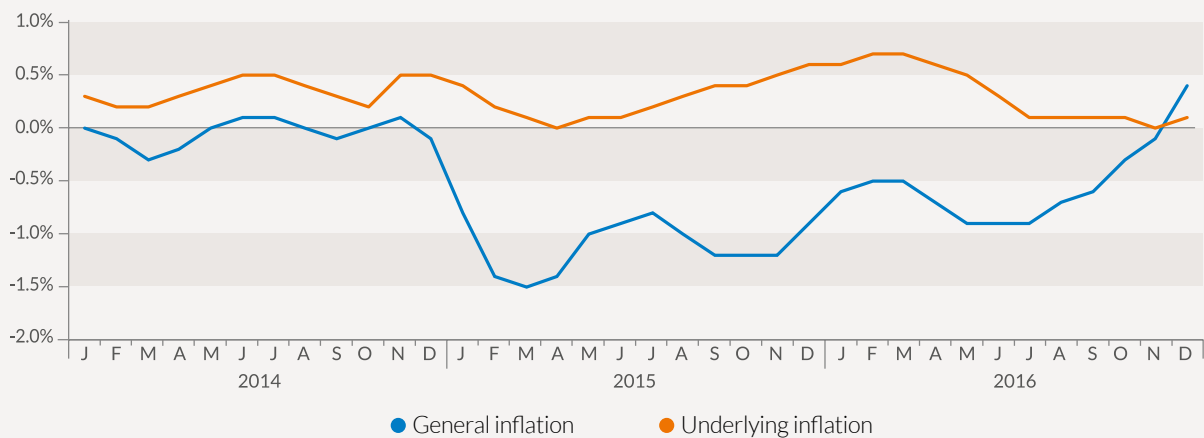
The role of imported inflation/deflation, linked to the trend in oil prices and other commodities, is reflected in the comparison between inflation measured by the CPI and underlying inflation. The latter indicator, as we know, excludes the most exogenous and volatile components, such as imported energy prices and unprocessed food.

¹ For example, Auer, Borio i Filardo, "The globalisation of inflation: the growing importance of global value chains", BIS working paper, n. 602, 2017.

² Vid. "Domestic and global drivers of inflation in the euro area", in ECB Economic Bulletin, Issue 4/2017, June 2017.

ANDORRAN CONSUMER PRICE INDEX (2014-2016) Interannual variation rate (%)

Figure 6.1



Source: Department of Statistics.

The expected result is, of course, that underlying inflation will show a more stable trend than general inflation, with subtleties. In 2016, underlying inflation fell five tenths against the previous year, to reach +0.1%, the lowest value in the last five years. This fall in underlying inflation to low levels demonstrates that, despite the scenario of gradual economic recovery, a good number of businesses have tended to contain or lower prices in order to promote sales, in a context where consumer demand remains weak. In 2016, underlying inflation pursued a U-shaped trend, with interannual rates between 0.6% and 0.7% up to April, reaching almost zero levels between July and December (with a technically zero low in November 2016), and started to rise again a little at the beginning of 2017. This dynamic of underlying inflation is the result of more specifically national changes.

The change in relative positions of the two indicators since 2016 is notable: the significant downtrend in petrol prices in previous years brought general inflation down below underlying inflation, while recently, a certain (unconsolidated) recovery in some commodities may lead to a reversal. Both indicators therefore provide supplementary information about price behaviour.

By components, the upturn in inflation throughout 2016 is, to a large extent, the result of the trend in prices in the energy group, which have seen an increase of 1.7% as a whole, a rate that contrasts with the steep declines noted in the previous two years (-13.9% in 2015 and -6.2% in 2014).

This trend was motivated by the behaviour of prices of fuel and combustibles, which reflected the rise in prices of oil producers and ended the year with a clearly upward trend. Specifically, oil and lubricant prices increased 2.6%, compared with the fall of 15.4% in 2015; those of liquid combustibles and others rose 1.3%, while in 2015 they fell 20.8%. Another, if smaller, contributing factor was the more gradual decline in gas prices (-1.3%) and the stability in electricity prices (0.0%).

The effects of this increase in energy prices was felt particularly in the transport chapter – which saw a rise of 0.9%, contrasting with the fall of 3.1% in 2015 – and also the housing component which, influenced above all by the increase in domestic fuel prices, went from falling 2.4% in 2015 to rising 0.1% in 2016.

The upturn in inflation in 2016 is, to a large extent, the result of rising prices in the energy group.

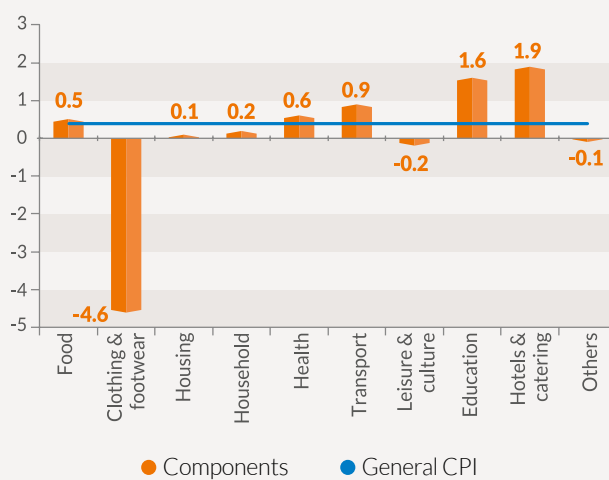
On the other hand, the chapters that saw a more marked increase in prices than in the previous year and which have therefore had a notable influence on the upturn in the CPI, were hotels,

cafes and restaurants (1.9%), education (1.6%), health (0.6%) and, to a lesser extent, furniture, domestic appliances and household services (0.2%). In contrast, the increase in the component of food, beverages and tobacco, despite maintaining an upward trend, slowed nine tenths to +0.5%.

The only chapter which has contributed decisively to containing the inflationary change was clothing and footwear, which ended the year with a more marked fall in prices than in the previous year (-4.6% against -0.4% in 2015).

Finally, the group of miscellaneous goods and services (-0.1%) continued to see a fall in prices, if slower than one year ago (-0.3%), and leisure, shows and culture ended 2016 with a negative variation in the interannual inflation rate of -0.2%, contrasting with the 1% increase in 2015.

CONSUMER PRICE INDEX.
December 2016
Interannual variation rate (%)



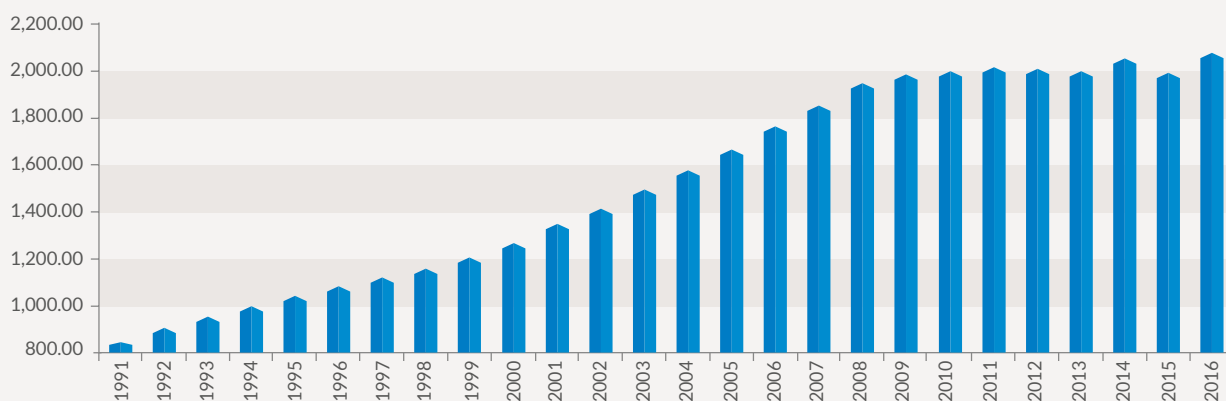
Source: Department of Statistics.

2. Wages

In 2016, the average wage reached a historic high at 2,076.70 euros, 4.3% higher than in 2015. It can be said that since 2009, average monthly wages in Andorra have remained quite stable at around 2,000 euros (in 2009 they were 1,984.30 euros), in keeping with the low – and sometimes absent – inflationary pressure. In fact, in 2016, the purchasing power of employees increased by 3.9 points, offsetting the 2.1-point drop in 2015. So, it can be seen that the improvement in the economy and the labour market detected in 2015 is starting to cross over to wages.

In cumulative terms, the average wage has increased 4.7% since 2009, while the cumulative increase in consumer prices in the same period was 4.4%, representing an increase in purchasing power of only 0.3 points in the last seven years.

ANNUAL TREND IN AVERAGE WAGES (1991-2016) In euros



Source: CASS / Department of Statistics.

Average wages by sector vary notably.

If we extend our view to a longer period, to before the 2007 crisis, growth in the Andorran average wage is positive throughout the whole available series since 1990, with very high

interannual increases until the arrival of the crisis in 2008. From that point on, the tendency towards ever smaller increases began, reaching the first historical negative rates in 2012-2013.

It should be noted that since 2015 the source of data on average wages used for the analysis are data prepared by the Department of Statistics, based on employees' contributions supplied by the CASS.

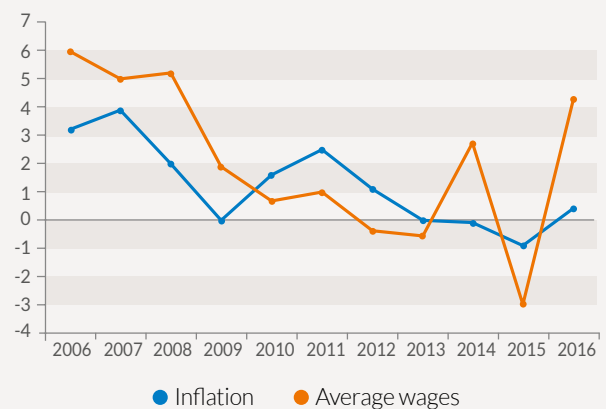
To interpret the trend in global average wages in Andorra and, in particular, those of the financial system, we must bear in mind that statistical data for the years 2014 and 2015 are not identical to those of previous years or 2016. This is because, with the implementation of the IRPF (personal income tax) in 2015, the frequency of payments of an unfixed part of the wages which some businesses made to their employees was disrupted. From 2016 on, it is likely that they will become regular each year. If a comparative calculation is desired, to include 2014 and 2015, it is advised to use an average of these two years to obtain a more realistic estimate.

The minimum interprofessional wage in 2016 was fixed at 5.63 euros/hour (for workers over the age of 18), equal to 975.87 euros/month, for a 40-hour working week. This amount represents the first upward review since 2013, in which wages were set at 5.55 euros/hour or 962 euros/month. At the beginning of 2017, it was raised again, to 5.72 euros/hour or 991.47 euros/month. These values are higher than those of Spain but lower than those of France.

The recent upward reviews are coherent with the perceived revitalisation of the socio-economic situation and the desire to maintain a coherent level of "inclusivity", to use the term which has already been used by bodies such as the OECD or the G20 to refer to the need for the economic recovery to reach a critical mass of the whole of society.³ Insofar as the minimum wage is applied to lower-qualified jobs but also guarantees a minimum spending threshold to those sectors of the labour market, its moderate but perceptible upward trend has socio-economic dimensions which should be seen as positive, beyond their direct impact on wage costs which, as we know, must always be measured against the trend in productivity.

Average wages by sector show a notable regularity. So, the average figure for 2016 of 2,076.70 euros derives from sectoral data which ranges from 5,163.16 euros in the financial sector (maximum) to 1,325.26 euros for domestic household staff (minimum). This means that the highest wage is 3.9 times higher than the lowest wage. This gap between sectors has widened since the previous year, when it was 3.3 (but 4.4 in 2014). The second sector in the wage ranks is production and distribution of electricity, gas and water, with wages 55.7% higher than the average, followed by the extraction industries – paying 51.2% more – and extraterritorial bodies with 51.1% higher wages

AVERAGE WAGES AND INFLATION (2006-2016) Interannual variation rate (%)



Source: CASS / Department of Statistics.

Figure 6.4

³ Vid., Vid., among other references: <http://www.oecd.org/inclusive-growth/> or the final declaration of the G20 in China (September 2016): <http://www.consilium.europa.eu/en/press/press-releases/2016/09/05-g20-leaders-communiqué/>, which included the term "inclusive" to describe desired post-crisis growth, added to other already-adopted properties, such as "strong", "balanced" and "sustainable".

than the average. After these come public administration, transport, storage and communications; health and veterinary activities and social services, and education, with wages from 21.8% to 4.8% higher than the average.

The other branches lie below the average wage level, with percentages varying by between 0.8% lower in the manufacturing industries, and 36.2% lower for household domestic staff. Within this group of sectors are notably those of commerce and hotels and catering, which employ a large part of the Andorran population (36.8% of total employees), with wages 16.4% and 27.0% lower than the average, respectively. The construction sector lies below the average for the seventh consecutive year, when traditionally it had been above.

All sectors saw wage increases in 2016. The extraction industries and extraterritorial bodies need to be separated from the general analysis, as they are sectors in which very few people work so the variation in one wage can greatly influence the total. The financial sector has seen the largest wage increase (22.5%). The average wage in the financial sector for the year 2016 was unaffected by the calculation disruption that occurred in 2014 (with an increase of 19.5%) and 2015 (with a decrease of 23.9%) linked to the introduction of the IRPF. Average interannual growth from 2014 to 2016 was 6.0%, a more realistic figure than the nominally-produced increases and decreases of the last three years.

Other notable wage increases occurred in the activities of domestic work for the community (7.3%), the primary sector (3.5%) and real estate activities and business services (3.4%). Among the sectors where the average wage rose - and more rapidly than in 2015 - are public administration (2.9%), households employing domestic staff (2.5%), hotels and catering (2.1%), commerce (1.6%) and transport, storage and communications (0.9%).

On the other hand, the average wage also rose, if more slowly, in health and veterinary activities, social services (1.8%), the construction sector (1.5%) and energy production and distribution (1.2%), after falls of between 0.1% and 1.9% in 2015.

AVERAGE WAGES BY SECTORS OF ACTIVITY IN EUROS

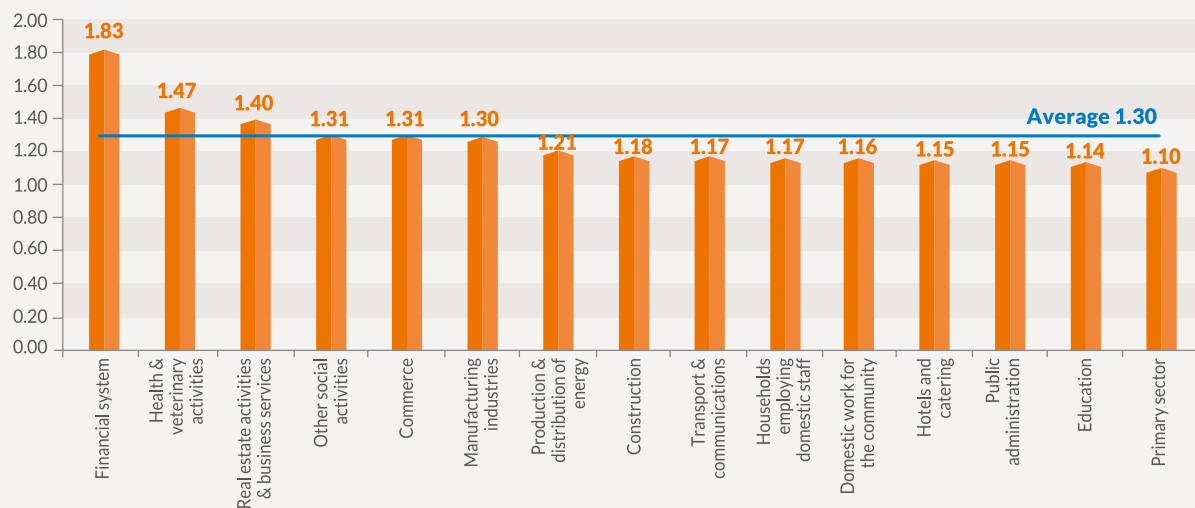
	2015	2016	Var. 2016/15	Average index in Andorra=100
Agriculture, livestock, hunting and forestry	1,405.55	1,454.53	3.5%	70.0
Extraction industries	2,293.02	3,139.52	36.9%	151.2
Manufacturing industries	2,045.48	2,060.66	0.7%	99.2
Production and distribution of electricity, gas and water	3,196.83	3,233.59	1.2%	155.7
Construction	1,880.77	1,908.19	1.5%	91.9
Commerce and motor vehicle repairs (etc.)	1,709.00	1,736.55	1.6%	83.6
Hotels and catering	1,484.24	1,515.93	2.1%	73.0
Transport, storage and communications	2,240.88	2,260.45	0.9%	108.8
Financial system	4,214.29	5,163.16	22.5%	248.6
Real estate & rental activities; business services	1,842.13	1,905.58	3.4%	91.8
Public administration, defence & compulsory social security	2,458.92	2,530.02	2.9%	121.8
Education	2,176.87	2,175.92	0.0%	104.8
Health & veterinary activities, social services	2,239.57	2,279.54	1.8%	109.8
Other social activities & community services, personal services	1,724.35	1,777.40	3.1%	85.6
Households employing domestic staff	1,293.47	1,325.26	2.5%	63.8
Extraterritorial bodies	2,577.13	3,138.18	21.8%	151.1
Domestic work for the community	1,269.39	1,362.26	7.3%	65.6
Average	1,992.00	2,076.69	4.3%	100.0

Source: CASS / Department of Statistics.

Table 6.1

WAGE QUOTIENT MEN/WOMEN BY SECTORS (2016)

Figure 6.5



Source: CASS / Department of Statistics.

In 2015, most sectors saw very slight wage cuts or growth, so the 2016 data are a sign that the economic situation is tending to improve, if slowly.

As for wage levels by gender, the average monthly wages for men were 2,346.54 euros compared with an average wage for women of 1,800.52 euros, i.e. men's wages are 30.3% higher than women's, a difference that has increased slightly since the previous year when it was 28.9%. In 2014, this difference was 34%. The wage differences between men and women appear in all sectors.

Men's wages are 30.3% higher than women's. The greatest differences are found in the financial sector.

Leaving to one side the extraction industries and extraterritorial bodies, for statistical reasons, the greatest differences are found in the financial sector, where the average wage for men is 83% higher than for women; in health and veterinary activities, social services (in which it is 47% higher) and in real estate activities and business services (in which it is 40% higher). These data demonstrate that, on the whole, men occupy the highest-level jobs in these sectors. In contrast, the smallest differences are found in the primary sector, education, public administration and hotels and catering (with men's average wages 10-15% higher than women's).

VII. Foreign sector

1. Foreign trade flows

The foreign trade figures for 2016 show the value of imports of goods at 1,226.1 million euros, the highest figure since 2008, with a positive variation rate of 4.9%, especially notable after the downturn of 0.6% in 2015.

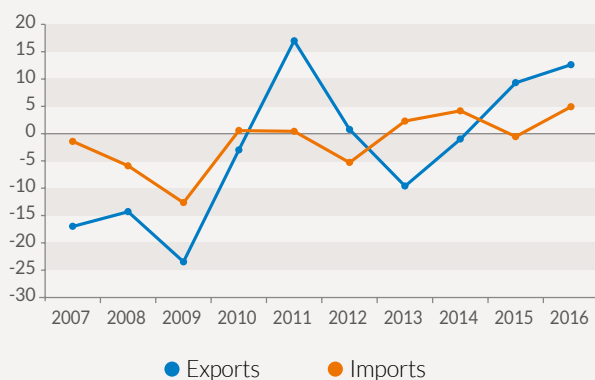
By chapters, the most positive contributions to the increase in imports was in pearls, precious stones and metals (1.9 points); motor vehicles (1.5 points), and perfumery or toiletries (1 point), while in

Imports of goods reached 1,226.1 million euros, the highest figure since 2008.

FOREIGN TRADE

Interannual variation rate (%)

Figure 7.1



Source: Department of Tax and Frontiers.

the previous year – 2015 – on the positive side were notably motor vehicles (1.1 points) and electrical machinery and apparatus (0.6 points).

In 2016, on the negative side, the most important contribution was from fuel (-1.9 points) and, to a lesser extent, knitted articles of apparel (-0.3 points), while in 2015 it had been fuels (-2 points) and pearls, precious stones and metals (-1 point). So, if we exclude the fall in imports of fuels from the total, the increase in imports without the chapter of fuels would become 7.5%.

The most significant chapter is still motor vehicles, which represents 11.0% of total imports (10.0% in 2015). It is followed by perfumery or toiletries with 7.9% of the total (7.3% in 2015); electrical machinery and apparatus with 6.8% of the total (7.3% in 2015), and fuels with 6.6% of the total (8.9% in 2015). In fact, an increase can be seen in the sectoral

concentration of Andorran imports, as the top four sectoral groups (food, products of the chemical industries, electrical machinery and equipment and transport material) represent more than half of the total (51.3%), 0.7 points more than the top four groups represented in 2015, which were the same in this case.

As in the case of imports, Andorran exports have risen in 2016, but with growth 2.6 times higher. In fact, exports grew 12.6% in the last year, whereas in 2015 they grew 9.3%. This growth represents the most positive level in the last five years. In absolute terms, the volume of exports was 90.8 million euros.

The 12.6% growth in exports is the most positive level in the last five years.

The most important chapter is still that of electrical machinery and equipment, with 24.2% of total exports (22.1% in 2015). It is followed by motor vehicles, with 19.3% of the total (19.0% in 2015) and optical, photographic, cinematic and measuring apparatus, with 10.2% of the total (11.4% in 2015). In fact, the top three sectoral groups (machinery and electrical equipment; transport material and optical, photographic and precision material) already easily exceed half of total exports, as they represent 63.6% of the total. These percentages represent 2.6 points more than the top three groups in 2015, which were also the same in this case. It can be said that the concentration of sectoral groups is quite high and, in any case, higher than seen in the case of imports.

It is notable that part of the Andorran imports involves later re-export. In fact, if we classify the ten top imports and exports chapters by percentage, there are five matches: “motor vehicles”, “electrical machinery and equipment”, “articles of apparel, not knitted”, “mechanical apparatus” and “pearls, precious stones and metals”. In the economic literature, this is understood to indicate the so-called intra-industry trade and/or so-called bidirectional trade (one country is both exporter and importer of one type of product). In the cases of sectors where one country is clearly just an importer or exporter, the traditional international trade explanations are relevant (comparative advantages, available resources, residents’ demands unsatisfied by national products), while in

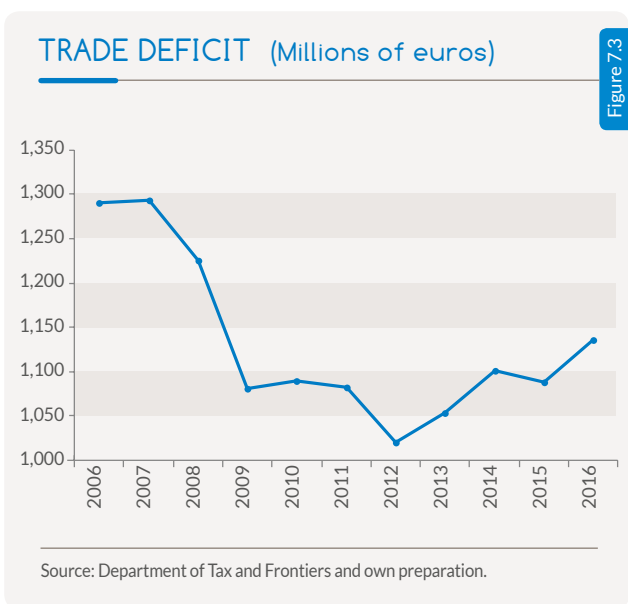
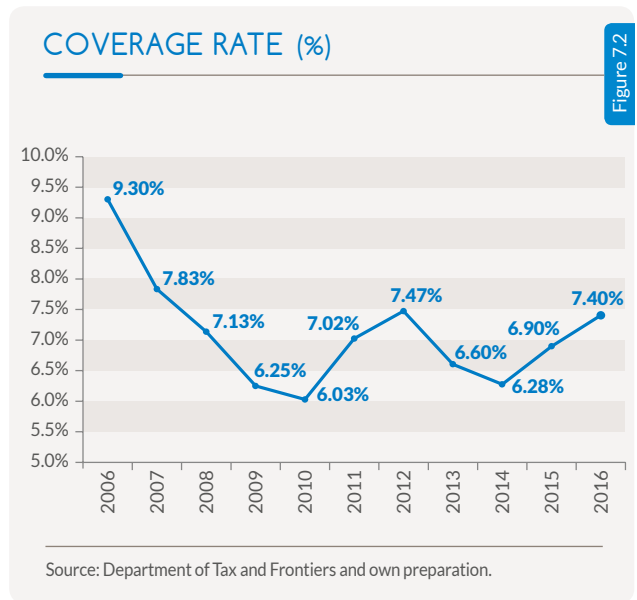
the chapters with bidirectional trade the added value generated in the national economy or the timing in commercial trading operations become essential factors and assets.

In the case of Andorra, this re-export activity has no defined trend. It concerns products that allow commercial trading operations on an international scale, with significant value differences between countries which an intermediary can take advantage of, or the creation of activities linked to coupling with creation of an added value within Andorra, taking advantage of a market niche.

Both trends in exchange rates and legislative amendments in international trade are important factors that influence re-exports of products. Andorra is in the process of negotiating an association agreement with the EU which, among other aspects, will allow for the free circulation of goods from chapters 1 to 23 in the harmonised system and, equally, continue to exclude tobacco from the customs union for a transition period long enough to allow for reconversion of the sector. This may open up new opportunities for trade between Andorra and the European Union.

The trends in Andorran exports align with the general trends in international commerce on a global scale. In effect, after growing significantly over the years prior to the crisis, it saw a major downturn, especially in 2009 – known in economic analysis as the *great trade collapse* – with an upturn in 2010-2011 (more pronounced in Andorra in 2011), and then, when some expected a quick normalisation with a return to figures before the crisis, it dropped off – known as a *trade slowdown* – from which it only seemed to be breaking away at the end of 2016 and beginning of 2017, although the change in trend is awaiting consolidation.

The disparity between exports and imports can be seen in the coverage rate, which is the percentage of the value of imports covered by exports. As the following diagram shows, the coverage rate rose 5 tenths to 7.4%, the highest level in the last four years. A positive figure for 2016 would be the upturn in this coverage rate, with an improvement in exports proportionally greater than in imports. The follow-up to this trend would be significant, if it consolidates, as a sign of a still modest but valuable contribution from exports to covering the import requirements of the Andorran economy.

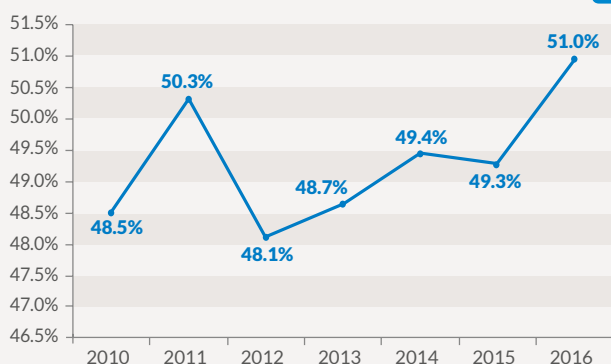


be the upturn in this coverage rate, with an improvement in exports proportionally greater than in imports. The follow-up to this trend would be significant, if it consolidates, as a sign of a still modest but valuable contribution from exports to covering the import requirements of the Andorran economy.

Andorra is traditionally characterised by a major trade deficit. In the years prior to the crisis the deficit lay at values close to 1,300 million euros. Contraction in foreign trade activity reduced the deficit to a band between 1,000 and 1,100 million euros. In 2016, this band was surpassed (to reach 1,135 million euros) within the framework of imports growth. In Andorra, a country specialised in tourism

OPENNESS RATE (Trade as % of GDP)

Figure 7.4



Source: Department of Tax and Frontiers and own preparation.

and commerce, the increase in imports should be associated with a certain improvement in overall economic activity, greater demand for imported consumer products (both domestic and for tourism) and investment.

The traditional preparation of the “openness rate” is expressed by the value of foreign goods trade (exports + imports) as a percentage of GDP. Before the crisis, levels of 55% were reached – still a little lower than those of Catalonia and Spain – which fell to a low of nearly 46% in 2009. The openness rate did not exceed the level of 50% again until 2016, when it reached about 51%.

2. Geographical distribution of foreign trade

2.1. Imports

In 2016, imports from Europe, the main geographical source of Andorran imports, concentrated 92.1% of the total, one tenth more than in the previous year. This equals the 2014 level, the highest in the historical series. Purchases from Europe grew 5.0% compared with the previous year. This trend was the combined result of a moderate increase in imports from France and Spain, the main suppliers of Andorra and, at the same time, a major increase in imports from other EU-28 countries, basically Portugal, Italy, the UK and the Netherlands.

FOREIGN TRADE BY GEOGRAPHICAL AREA

Table 7.1

	IMPORTS			EXPORTS		
	Thousand euros 2016	% var. 2016/15	% total 2016	Thousand euros 2016	% var. 2016/15	% total 2016
Spain	785,732.3	5.8	64.1	46,029.4	8.6	50.7
France	190,932.8	3.3	15.6	13,431.8	-10.7	14.8
Germany	35,580.4	-3.3	2.9	3,769.2	590.6	4.2
Italy	27,531.7	11.7	2.2	1,335.1	-42.2	1.5
United Kingdom	17,478.3	9.8	1.4	273.5	-67.0	0.3
Netherlands	11,158.4	24.2	0.9	1,273.9	66.9	1.4
Portugal	10,749.7	27.7	0.9	225.7	175.0	0.2
EU-28	1,104,573.7	5.2	90.1	67,689.5	6.2	74.6
Switzerland	18,617.8	-4.5	1.5	679.0	28.2	0.7
Norway	25.3	-85.8	0.0	4,656.0	57.6	5.1
Europe	1,128,929.1	5.0	92.1	73,375.8	8.6	80.8
USA	7,993.1	10.9	0.7	1,031.1	81.1	1.1
America	13,255.6	14.3	1.1	4,147.7	59.1	4.6
China	42,392.9	-4.9	3.5	1,782.5	15.5	2.0
Vietnam	6,531.7	1.8	0.5	2.3	744.7	0.0
Asia	73,865.6	3.4	6.0	6,262.6	42.1	6.9
Global total	1,226,103.9	4.9	100.0	90,774.5	12.6	100.0

Source: Department of Tax and Frontiers.

Asia is the second largest supplier of Andorra, with a 6.0% share of the total (6.1% in 2015). Although imports from Asia grew 3.4%, they did so at a slower rate than the average. America (mainly North America) consolidates third position, with 1.1% of total imports (1.0% in 2015) and notable growth of 14.3% in 2016. In contrast, the African continent only represents 0.2% of total imports, due to steep falls in imports in recent years (-32.7% this year). In fact, in 2013, it came to represent 1.0% of total imports.

Within the EU-28, Spain is by far the largest supplier of Andorra, with a share of 64.1%. Purchases from Spain increased 5.8%. Despite lower growth than many other countries in the European Union, this easily represents the largest contribution (3.7 points) to the increase in imports. Both in 2015 and 2014, Spain was also the country that contributed most to growth.

France remains the second largest supplier to Andorra with a share of 15.6%, at a distance from the third, although its share is far smaller than it had in the nineties, when it was higher than 30%. In fact, in 2015, imports broke eleven consecutive years of falls. This year, imports from France grew at a moderate rate (3.3%), so contributing 0.5 points to total imports.

As for the other EU-28 countries, Germany remains in third place in the ranks, followed by Italy, the UK, the Netherlands and Portugal, in this order, with shares that vary between 2.9% and 0.9%. Imports from Germany fell 3.3%, contrasting with the steep fall in 2015 (-18.6%) and the sharp increase in 2014, of 29%. Its percentage of the total went from 3.8% in 2014 to 2.9% in 2016. On the other hand, both the Netherlands and Portugal saw very high growth, over 20%, which raised their shares against the previous year by 1 and 2 tenths, respectively. Leaving Germany to one side, these four countries together have a share of 5.5% and contributed 0.8 points to import growth, significantly more than France, which alone has a share almost three times that of these countries.

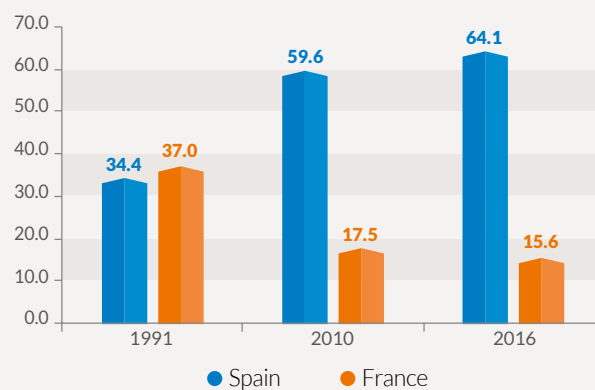
The other EU-28 countries have very small shares (around 2%), so their contribution to total growth is not very significant. Outside the European Union, the reduction in imports from Switzerland stands out (-4.5%), after the intense contraction of the previous year (-43.3%). As a result, Switzerland's share of the total went from 2.9% in 2014 to 1.5% in 2016.

As for imports from countries in the rest of the world, in general, only imports from the USA and some Asian countries have any significance. In fact, eight out of ten of Andorra's main suppliers are European countries. China is Andorra's third largest supplier and the USA is tenth. Next are Vietnam and India in eleventh and twelfth place, respectively. While China continues to lose ground for the second consecutive year, going from 4.1% in 2014 to 3.5% in 2016, the USA has gained against previous years, although it still represents less than 1% of total imports (0.7% in 2016).

In summary, Spain's share of imports increased between 2006 and 2016, while France's decreased. China has risen to third place and overtaken European countries such as Germany and Italy. The appearance of Vietnam in 11th place (with India and Turkey not far behind) becomes a sign of the new age in the global economy.

IMPORTS FROM NEIGHBOURING COUNTRIES Percentage of total (%)

Figure 7.5



Source: Department of Tax and Frontiers.

Eight of the ten main suppliers to Andorra are European countries.

2.2. Exports

Compared with other countries, Andorran exports are much more volatile than imports, so steep rises and falls in volume can be seen from one year to the next, as occurred in 2016. The increase in Andorran exports seen in 2016 was 12.6%.

80.8% of sales are made in Europe. In 2016, the increase of 8.6% in European sales contributed 7.2 points to growth in Andorran exports. Nevertheless, the percentage of exports to Europe decreases year after year. In 1991, exports to European countries represented practically all Andorran exports (98.8%). In 2015, they represented 83.9%, 3.1 points more than in 2016.

The falling percentage of exports to Europe contrasts with the growing contribution from Asia and America. In this respect, the contribution from the Asian continent stands out, with a share of 6.9%. Growth in exports to Asia in recent years has been very notable (42.1% in 2016 and 39.9% in 2015), considering that in 2010 they only represented 0.6% of total exports.

The third continent in the ranking is the American continent, with a share of 4.6% in 2016 and higher growth (59.1%) than for Asia. The strong growth in sales to America in recent years (notably the increase of 144.1% in 2014) has enabled its share to rise 3.6 points since 2011.

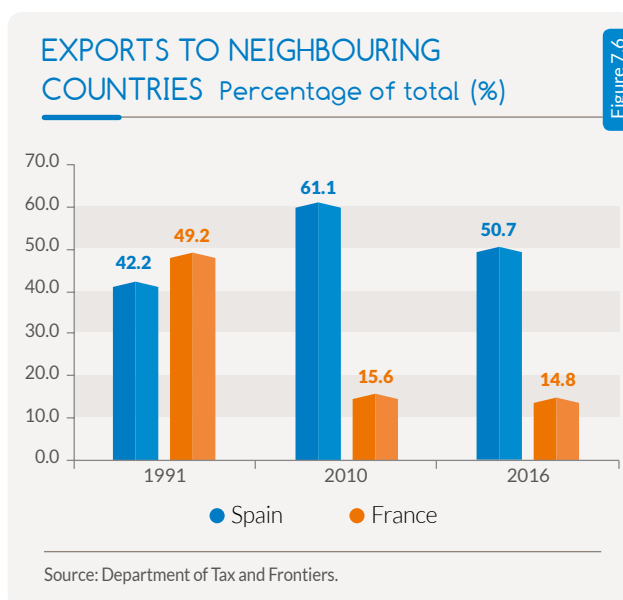
For its part, the African continent only represents 1.1% of total exports, although this share increased 0.9 points against 2010. Growth in 2015 was 188.2% and in 2016, 32.3%.

By countries, in 2016, Spain is still the main consumer of products from Andorra, with an increase in exports of 8.6% and a share of 50.7%. Despite being the country that contributed most to growth (4.5 points), its share is falling every year in relation to exports. In fact, in 2010, 61% of products coming from Andorra were exported to Spain. Now, only half.

The behaviour of sales to the second largest Andorran market, France, was negative in 2016, considering that exports fell 10.7%. This decrease meant a fall in its share of total sales of 3.9 points against the previous year, going from 18.7% to 14.8%. As France still has a considerable share and is still easily the third largest consumer, the negative contribution to Andorran exports was 2 points.

As for the other EU-28 countries, Germany stands out in fourth place in the ranking, followed by Italy (ninth) and the Netherlands (tenth). Exports to Germany went from a value of 545.8 thousand euros in 2015 to 3,769.2 thousand euros in 2016; i.e. in the last year, exports to Germany multiplied almost sevenfold. The weighting of sales to Germany has been very volatile over the years, varying between 0.5% and 13.2% in the last 10 years. Despite representing a relatively low share compared with Spain, in 2016 its contribution to growth in total exports was 4 points, only 0.5 points below Spain. The notable increase in exports to Germany occurs mainly in the chapters

The falling importance of exports to Europe is offset by the contribution from the Asian and American continents.



of pearls, precious stones and metals and motor vehicles. In fact, these two chapters are those that contributed most to the increase in imports (1.9 and 1.5, respectively).

Sales to the Netherlands also increased significantly in 2016 (66.9%), although they had decreased 28.3% in the previous year. Netherlands' share is 1.4%, equal to that of 2014 (the highest in the last 10 years). In contrast, exports to Italy fell 42.2% over 2016, despite growing 74.2% in 2015. Italy is the second country to lose growth (-1.2 points), only below France (-2.0 points). In 2007, its share was 3% of total exports, falling to 0.5% in 2011 and ending up at 1.5% in 2016.

The country outside the EU-28 that stands out is undoubtedly Norway which has, since 2014, become the third consumer of products from Andorra. In 2016, its share of total exports stands above 5% (5.1%), 3.4 points more than 10 years before. In contrast with 2015, in which exports to Norway fell 30.5%, they grew 57.6% in 2016. In fact, Norway was the country which deducted most growth from Andorran exports in 2015 (-1.8 points), but in 2016 made the third most positive contribution (2.1 points). These ups and downs are partly influenced by euro appreciation or depreciation against the Norwegian crown.

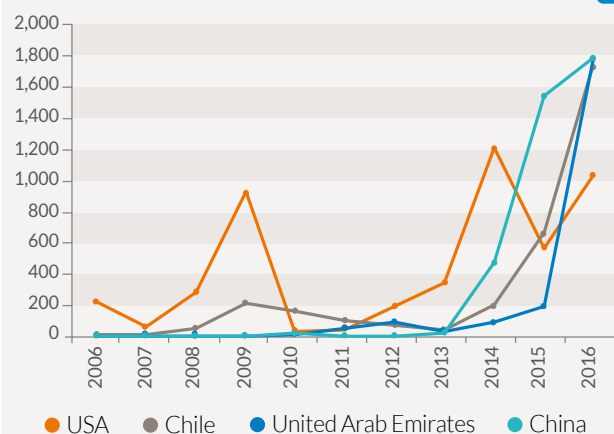
Since 2014, Norway has become the third largest consumer of products from Andorra.

As for Asian countries, Hong Kong, China and the United Arab Emirates stand out, as fifth, sixth and seventh consumers of products from Andorra. Together, they represent 6.3% of the total share, while in 2010 they only represented 0.1%. Of these three countries, the most notable growth in 2016 was to the United Arab Emirates as, in one year, sales went from 198.47 thousand euros in 2015 to 1,770.56 thousand euros in 2016 (almost nine times more).

Finally, growth in exports to the American continent in recent years was driven not only by the USA but also a series of Central and South American countries, notably Chile which, in 2016, was eighth in the ranking of Andorran exports, compared with the USA, which is eleventh. On the one hand, growth in exports to Chile was 3 digits in the last three years (159.2% in 2016) and this contributed 1.3 points to growth in total exports. So, its quota went from 0.1% in 2013 to 1.9% in 2016. On the other hand, in 2016, growth in exports to the USA was also notable (81.1%), but trends have been volatile in recent years. In fact, in 2015, exports to the USA fell to half.

In summary, there is the tendency for Andorran exports to diversify, within the framework of reorientation towards more dynamic areas of the global economy. In demonstrating the potential of emerging export destinations, the following diagram shows the trend in Andorran exports to various countries, such as China, for which growth is accelerating since 2014, already the 6th destination in 2016. To be sure, creating more and better connections with destinations that possess greater current and future purchasing capacity is becoming an interesting strategy in the internationalisation of Andorran trade.

VARIOUS EMERGING EXPORT DESTINATIONS Thousands of euros



Source: Department of Tax and Frontiers.

Figure 77

3. Sectoral composition of foreign trade

3.1. Imports

The increase in Andorran imports seen in 2016 (4.9%) was basically the result of growth in most groups. The first group in the ranking is food products, beverages and tobacco, with the largest percentage of total imports (15.9%) for the seventh consecutive year. In 2016, imports in this group grew 4.3%, after the fall of 1.1% in the previous year. This meant a positive contribution to growth of 0.7 points. The most important chapter in this group is beverages, alcoholic liquids and vinegars, with 6.3% of total Andorran imports, after seeing growth of 6.2% in 2016. The second most important chapter is tobacco, with 2.2% of the total and more modest growth (0.7%).

The group of food, beverages and tobacco still tops the import ranks, for the seventh consecutive year.

The second group in the import ranking – for the third consecutive year – is products of the chemical industries, with a 12.6% share of Andorran imports. Its contribution was 0.8 points to growth in total imports, as it grew 6.3%. The trend in this group has continuously risen over the last three years. The chapters that most explain this trend are perfumery – the second most important chapter in Andorran imports, with 7.9% of the total – which grew 13.1%, and pharmaceutical products – the second most important chapter in this group, with 2.4% – which, on the other hand, fell 5.1%.

FOREIGN TRADE BY SECTORS

	IMPORTS			EXPORTS		
	Thousand euros 2016	% var. 2016/15	% total 2016	Thousand euros 2016	% var. 2016/15	% total 2016
Live animals and animal products	62,558.85	2.7	5.1	83.33	-22.4	0.1
Vegetable products	26,529.05	10.3	2.2	7.57	349.0	0.0
Fats & oils	5,837.47	19.4	0.5	118.32	20.5	0.1
Food products, beverages & tobacco	194,370.85	4.3	15.9	453.97	-21.2	0.5
Mineral products	86,491.46	-21.3	7.1	179.02	-25.7	0.2
Products of the chemical industries	154,198.27	6.3	12.6	975.71	1.6	1.1
Plastics, rubber & articles thereof	26,128.61	-3.2	2.1	1,737.44	8.9	1.9
Fur, leather & articles thereof	14,864.52	-3.5	1.2	799.20	13.0	0.9
Wood, cork & articles thereof	9,563.51	22.7	0.8	1,025.08	36.5	1.1
Paper & graphic arts	28,537.00	8.3	2.3	4,523.47	22.3	5.0
Textiles	104,867.39	0.1	8.6	6,421.46	-9.0	7.1
Footwear, headgear, umbrellas, etc	36,342.05	4.4	3.0	1,698.66	-9.4	1.9
Articles of stone, cement, ceramic products	13,650.54	2.6	1.1	233.94	20.5	0.3
Pearls, precious stones and metals	38,774.59	129.7	3.2	7,581.65	57.7	8.4
Base metals and articles thereof	33,230.00	8.6	2.7	3,839.25	-25.3	4.2
Machinery & electrical equipment	143,717.55	1.9	11.7	26,395.35	30.0	29.1
Transport material	136,755.67	15.3	11.2	18,108.91	17.0	19.9
Optical, photographic, precision app.	52,169.35	5.3	4.3	13,232.08	-1.5	14.6
Arms & ammunition	963.43	13.9	0.1	60.44	-20.3	0.1
Miscellaneous manufactured articles	53,732.18	12.3	4.4	2,584.66	78.0	2.8
Works of art, antiques	2,821.59	4.9	0.2	714.96	-65.3	0.8
Total	1,226,103.93	4.9	100.0	90,774.47	12.6	100.0

Source: Department of Tax and Frontiers.

Table 7.2

77

Machinery and electrical equipment is positioned, for the fifth consecutive year, as the third group in the import ranking, with a share of 11.7% of the total and a contribution to import growth of 0.2 points. Although growth in imports in this group was positive (1.9%), this was more moderate than in the previous year (4.7%), so the share of total imports fell 0.4 points against 2015. The fall in purchases of electrical machinery and apparatus by 2.2% was partially offset by the increase in purchases of mechanical apparatus (8.1%). In fact, the chapter of electrical machinery and apparatus is the third largest in the total, and contributed negatively to the trend in Andorran imports by 0.2 points.

As for the groups that contributed more positively to import growth, the most notable are pearls, precious stones and metals (1.9 points) and transport material (1.6 points). On the other hand, imports of pearls, precious stones and metals went from 16,879 thousand euros to 38,775 thousand euros, representing growth of 130% against the previous year. In fact, this group's share of total imports went from 0.8% in 2012 to 3.2% in 2016. On the other hand, the transport material group is the fourth in total imports (11.2%). In 2016, 15.3% growth continues the strongly rising trend that started in 2013. The explanation for this progress can be found in the strong growth in imports in the chapter of motor vehicles (14.4%) – the most important group, with an 11.0% share of total imports – which is in keeping with the increase in vehicle registrations in the Andorran market and also the increase in vehicle re-exports.

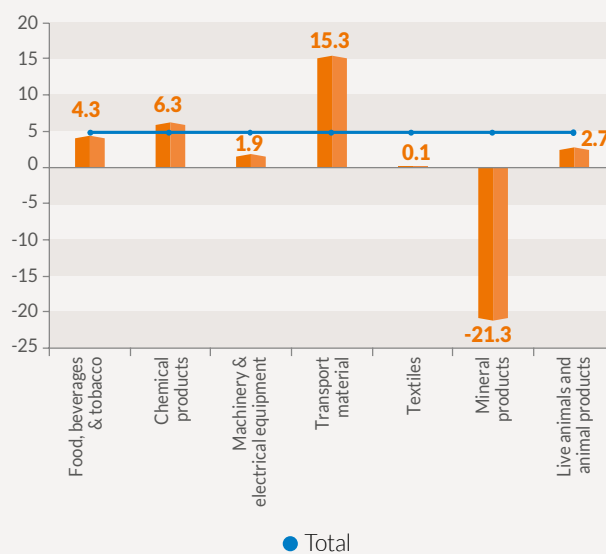
In contrast, the only group which significantly reduced growth in Andorran imports (-2.0 points) was the group of mineral products, with a share of 7.1% of the total. In fact, purchases of mineral products made the most negative contribution to the variation in imports, for the fourth consecutive year. As a result of these decreases, its share of the total fell to half that of 2012 (-7.5 points). The chapter of fuels, fourth in total purchases, fell 21.6% in 2016.

3.2. Exports

The rising trend in Andorran exports in 2016 can be analysed by groups. The first group in the ranking of exports in 2016 is still that of machinery and electrical equipment, as it has been since 2007. In 2016, it saw a strong increase of 30.0%, after the moderate increase of 3.6% in 2015. This group made a positive contribution of 7.6 points to growth in Andorran exports in 2016, more than the other groups altogether. Its share is very important (29.1%), 3.9 points higher than in the previous year. By chapters, growth in this group can be explained by the increase in electrical machinery and apparatus (23.1%), the most important chapter in all exports – with 24.2% of total foreign sales. Moreover, the chapter of mechanical apparatus, with 4.9%, grew 79.4%, helping to explain the strong increase in exports of machinery and electrical equipment.

ANDORRA'S MAIN IMPORT GROUPS.
2016 Interannual variation rate (%)

Figure 7.8



Source: Department of Tax and Frontiers.

The top export group in 2016 is still, as it has been since 2007, machinery and electrical equipment.

In second place in the exports ranking is still – since 2010 – transport material, with 19.9% of the total, 0.7 points more than in the previous year. With growth of 17.0% in 2016, it contributed 3.3 points to total growth in foreign sales. The chapter that determines this behaviour is motor vehicles, the second most important in all exports – with 19.3% of total foreign sales. This chapter saw an increase for the fourth consecutive year, of 14.5%.

Behind transport material comes the group optical, photographic and precision apparatus, for the seventh consecutive year. This group represents 14.6% of total exports and made a negative contribution to the variation in exports (-0.2 points), as sales in 2016 saw a downturn of 1.5%. In 2015, sales in this group had shrunk more strongly (-7.3%), losing 5.1 points in total sales compared with 2014. By chapters, optical and photographic products – the third largest chapter in all exports, with 10.2% of total foreign sales – grew a modest 1.3% in 2016. In contrast, the chapter of clocks and watches, which is less significant, saw a downturn of 9.4%, causing a drop in exports in the group of optical, photographic and precision apparatus.

On the other hand, the three groups that made the most negative contribution to the trend in total exports was, in this order, works of art and antiques (-1.7 points); base metals (-1.6 points) and textiles (-0.8 points). The group of works of art and antiques, despite representing only 0.8% of total exports in 2016 (2.6% in 2015), had a significant influence on the trend in total exports, as it saw a fall of 65.3% in sales, after three consecutive years of steep increases. For its part, the group of base metals and articles thereof represents 4.2% of total exports (6.4% in 2015), and saw a downturn of 25.3% in sales, after the strong increase in 2015 (31.5%). This fall was basically motivated by the chapter of aluminium and articles thereof, which alone made a negative contribution of 1.5 points to the trend in total exports. Finally, the textiles group represents 7.1% of total exports. The fall in sales in this group (-9.0%) is due, basically, to the chapter articles of apparel, not knitted, which made a 1.1% negative contribution to total exports.

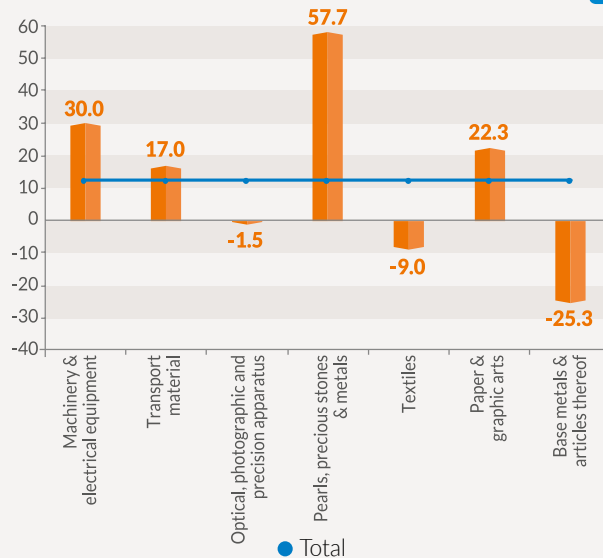
Other groups saw different variations in direction and intensity, but with a very limited impact on total growth.

4. Foreign investment flows

To complete the analysis of the foreign sector, remember that the new foreign investment law came into force in the Principality of Andorra in 2012, a step forward to opening up and liberalising the economy with respect to the 2008 regulatory framework, making a significant impact and increasingly attracting foreign capital to Andorra, with the consequent contribution to activity and job creation. So, in 2016, 810 investment applications were received, 8.6% more than in 2015 and the highest figure since the law came into force. Of these applications,

ANDORRA'S MAIN EXPORT GROUPS.
2016 Interannual variation rate (%)

Figure 7.9

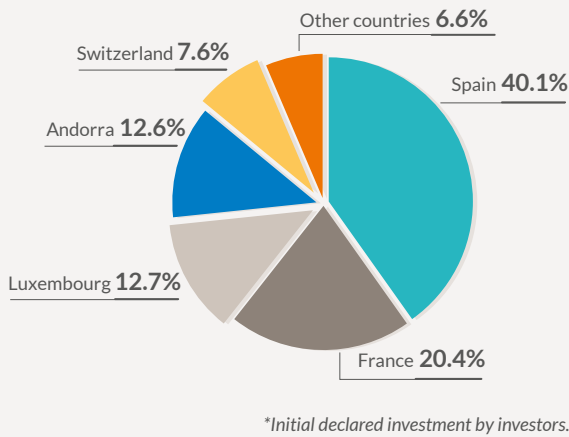


Source: Department of Tax and Frontiers.

810 investment applications were received, 8.6% more than in 2015 and the highest figure since the Law came into force.

VOLUME OF FOREIGN INVESTMENT BY COUNTRIES. * 2016 (%)

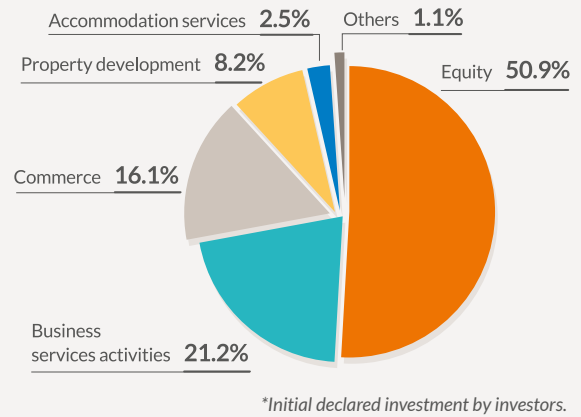
Figure 7.10



Source: Ministry of Economy, Competitiveness and Innovation.

VOLUME OF FORMALISED FOREIGN INVESTMENT BY SECTOR OF ACTIVITY. * 2016 (%)

Figure 7.11



Source: Ministry of Economy, Competitiveness and Innovation.

781 were granted and 630 have been formalised, for a total amount of initial declared investment by investors of 98.2 million euros, representing 3.8% of Andorran GDP and 1.3% more than in the previous year (97.4% more than two years ago).

Moreover, it is calculated that in 2016, this investment had an impact on the Andorran labour market of 562 jobs, 13% more than in 2015, both including jobs created in new businesses and those resulting from the acquisition of already-existing businesses.

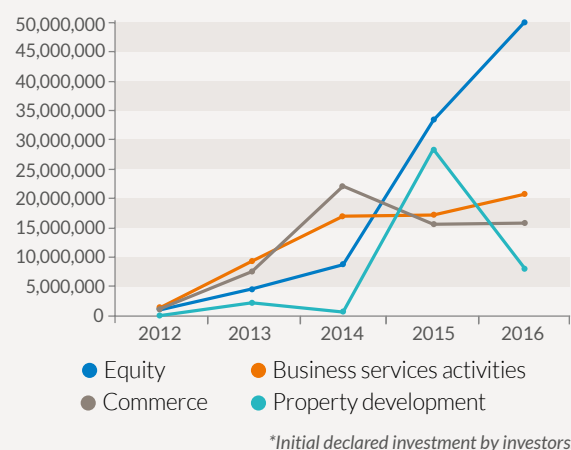
The geographical distribution of formalised investment shows that Spain is still easily the largest investor country (40.1%), followed at a distance by France (20.4%), Luxembourg (12.7%) and Switzerland (7.6%). Among the other countries are notably Germany (1.5%), Portugal (1.1%), Italy (0.5%) and Russia (0.4%), but with very low percentages. The percentage attributed to Andorra as a foreign investor (12.6%) is the result of investments made by Andorran companies which have a foreign majority shareholding.

By sector of activity, equity investments represent half of formalised investments (50.9%), followed by investment in business services activities (21.2%) and commerce (16.1%).

If we analyse the trend in formalised foreign investment by sector of activity in the period 2012-2016, continuous growth can be seen in investments linked to the business services activities; in contrast, the volume of investments linked to commerce slowed from 2014. On the other hand, the volume of foreign investment linked to equity activities has become more significant from 2015, with very significant volumes of investment. Also notable was the volume of investment in property development in 2015, which exceeded 28 million euros.

TREND IN FORMALISED FOREIGN INVESTMENT IN MAIN SECTORS OF ACTIVITY. * 2016 (in euros)

Figure 7.12



Source: Ministry of Economy, Competitiveness and Innovation.

VIII. The public sector

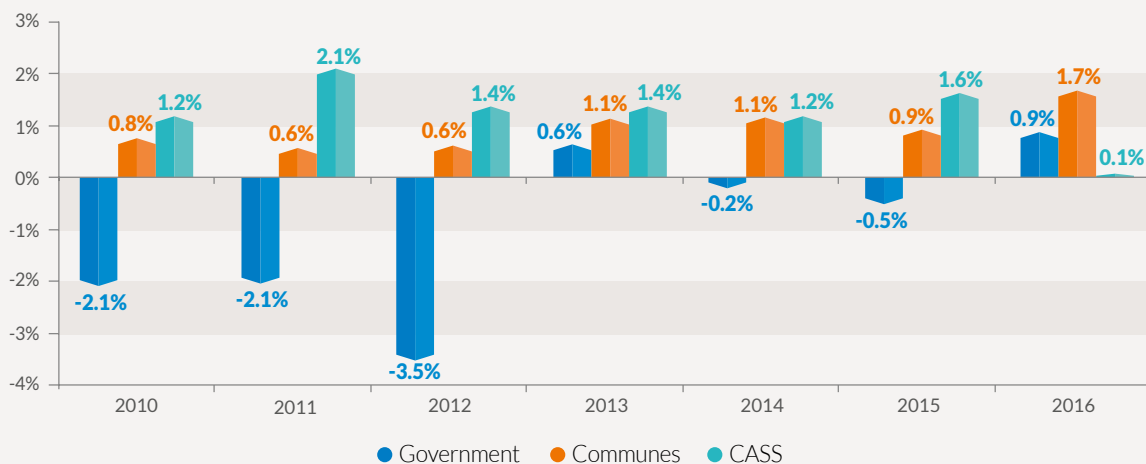
The most notable event in public sector performance in 2016 was the presence of budget surpluses in the three public bodies under this analysis: Government, communes and the CASS (Andorran Social Security System). This had not happened since 2013, although as explained below, in 2013 this was due to a specific situation.

Budget surpluses in the three public bodies under analysis: Government, Communes and CASS.

At the root of the good budget performance in the public sector is the major increase in Government revenue, a sign of consolidation of the tax system that has been introduced over the last few years, and contained spending by the communes. Interpretation of the CASS surplus is more complex, as it combines flows from two very different activities, as analysed in each relevant chapter.

This surplus situation affects the stability of debt levels, which have shown improvement even in per capita and GDP percentage values.

NON-FINANCIAL CASH SURPLUS OR DEFICIT OF THE PUBLIC ADMINISTRATION (% GDP)



Source: Ministry of Finance, commune administrations, CASS, Department of Statistics of the Government and own preparation.

The surplus in the Government's accounts represents 0.9% of GDP, something that has only happened once before in the last seventeen years. In effect, it also occurred in 2013, but in that case the Government surplus benefited from a special payment from the distribution of accumulated reserves by Andorra Telecom and not just from the distribution of the yearly profits, as is usual.

For their part, the communes, in aggregate figures, have again ended the financial year with a surplus (1.7% of GDP), as has happened every year since 2010, but this time better, almost doubling the 2015 surplus (which was 0.9% of GDP).

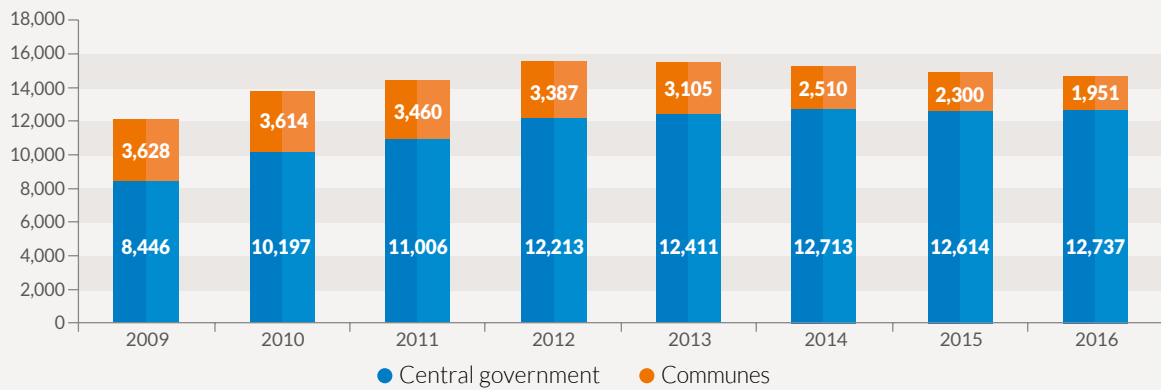
In contrast, CASS' surplus, although usual, was only 0.1% of GDP this year, contrasting with the 1.6% in the previous year.

In this context of improvement, Andorra's total debt (central Government plus communes) was 1,073 million euros, equal to 41.6% of GDP, a percentage that is under the 50% limit stipulated

Figure 8.1

PER CAPITA DEBT (€/person)

Figura 8.2



Note: data for 2016 published by the communes and data for the other years reviewed by the Court of Accounts. Calculation made taking the estimated population as the base.

Source: Ministry of Finance, commune administrations, Court of Accounts and own preparation.

by the Law on the sustainability of public finances and budgetary and fiscal stability. So, per capita debt (calculated using estimated population) reached 14,688 euros, 1.5% less than in 2015, when it reached 14,914 euros, and continuing the downward trend that started in 2013.

As explained in detail in the relevant chapter, the tax burden has reached 25.3%, with an increase of 1.9 points against 2015 (23.4%), a level that positions Andorra as a tax-friendly country.

The economic and financial development of the public sector in 2016 is described and analysed below, with details of each authority.

1. Central Government

According to the provisional data on settlement of the budget in 2016, the Government's accounts closed with a non-financial cash surplus of 22.61 million euros, a figure that is far from the deficit in 2015 (13.26 million euros). This surplus represents 0.9% of GDP and, as mentioned, breaks a dynamic of continuous deficits that occurred in fifteen of the last seventeen financial years.

The Government's accounts closed with a non-financial cash surplus of 22.61 million euros.

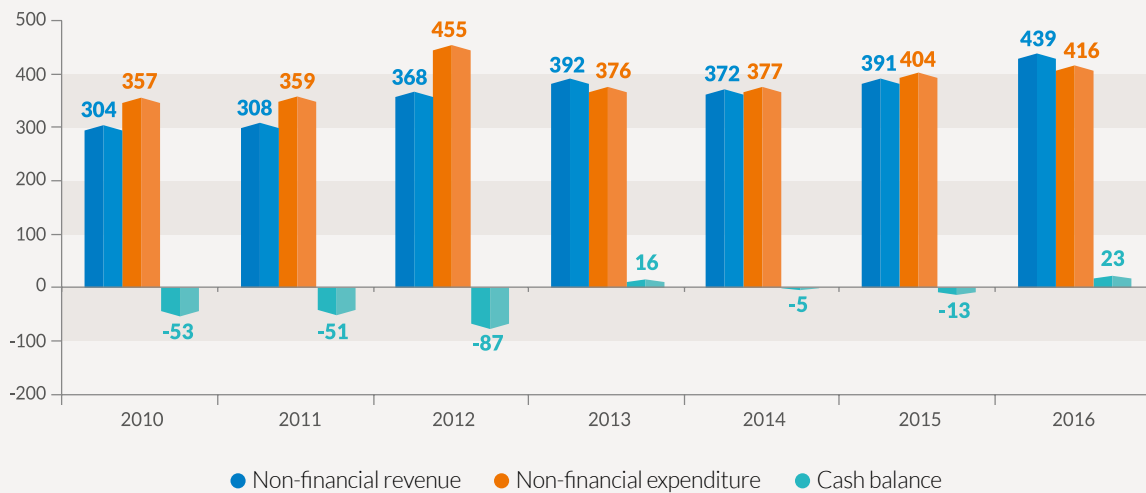
If this non-financial surplus is added to the financial operations which have been carried out over the year, we find a budget result for 2016 of 39.44 million euros (337.2% higher than the result in 2015), the highest figure achieved in the last twenty-five years.

In relation to the details of these financial operations, in revenue, the settled amount for the 2016 financial year for financial assets was 3,900 thousand euros, a figure which, compared with 2015, represents a positive variation of +1,964 thousand euros (in relative terms, an increase of 101.5%). Of this amount, the figure settled as loans to semi-public bodies stands out, the result of a loan granted by the Government to the National Agency for the Resolution of Banking Entities (AREB) to cover the costs related to the process of resolving the entity Banca Privada d'Andorra, SA. This body already began to amortise the financial operation in 2016, with an amount of 3,294 thousand euros.

On the other hand, in 2016, revenue from financial liabilities shows a settled value of 726,255 thousand euros which, if compared with 2015, represents an increase of 341,884 thousand euros

IMPLEMENTATION OF THE GOVERNMENT BUDGET (Millions of euros)

Figure 8.3



Source: Ministry of Finance.

(88.9%). The main variation in this chapter comes from an increase in the subscription to debt operations against the previous financial year with the object of renewing matured issuances.

As for expenditure, the most significant variation in budget settlement in the entry Variation in financial assets and liabilities, can be seen in financial liabilities (+314,305 thousand euros), as in 2016, the Government refinanced public debt for a total nominal value of 680,000 thousand euros, relating to four bond issuances and a syndicated bridging loan which matured during the 2016 financial year. During this refinancing process, an increase of an additional 30,000 thousand euros of bond issuance was generated. In 2015, the Government refinanced public debt for a nominal value of 360,000 thousand euros.

For its part, in 2016, the Government's volume of debt stands at about 931 million euros, an increase of 2.9% compared with the previous year. This volume represents 36% of GDP, three times more than in 2015, and is ever closer to the 40% limit set by the Law on sustainability of public finances for the central Government.

The volume of Government debt represents 36% of GDP.

The most important change in this figure occurred on the maturity timescale. So, in 2016, long-term debt represents 43.12% of the total (in 2015, it represented 23.55%). This change improves the Government's manoeuvrability in short-term financing.

The developments in the Government's non-financial activity from the point of view of revenue and expenditure resulted in the surplus mentioned at the start of this chapter. The reason is the combination of major growth in revenue of 12.3% and a slight increase of 3.0% in expenditure.

The increase in revenue is motivated by a strong increase in the entries of taxes, both direct and indirect, and also the increase in investment income.

As for expenditure, a reduction occurs in most entries, except personnel costs and current transfers, which increase 45.9%, to a large extent due to legislative change which, from 2016, means that transfers to communes are no longer considered as capital transfers and are incorporated into current transfers. This also means that capital transfers expenditure has fallen 90.1%.

1.1. Revenue

Settled non-financial revenue in 2016 increased 12.3%, reaching 438.8 million euros, with an execution rate of 111%, which therefore exceeds the budget provisions. This increase is the result of the increase in collection of direct tax (increasing 21.5%), and indirect tax (increasing 8.1%). Direct taxes continue to grow for the sixth consecutive year, while indirect taxes break with the negative trend of the previous three years through the increase that occurred in 2016. Collection of other taxes and revenue fell 14.4%, following the trend of the last two financial years.

Direct taxes have continued to grow for the sixth consecutive year and already represent 18.9% of total revenue.

Diagram 8.4 shows how the main revenue entries develop and allow us to see both the important percentage of indirect tax (66.3% of the collected total), which reached 290.7 million euros, and the growing importance of direct taxes, which already represent 18.9% of the collected total, with a total of 82.9 million euros. In 2016, investment income brought in 40.4 million euros and represents 9.2% of the collected total, continuing the growth trend of the last two years. The downturn seen in 2014 is the result of the special distribution of reserves by Andorra Telecom in 2013.

Collection of direct taxes represents 22.2% of total direct and indirect taxes, despite being below the 40% limit fixed by the Law on sustainability of public finances.

The same diagram shows that tax collection continues to lose importance in the total non-financial revenue (5.6% of the total).

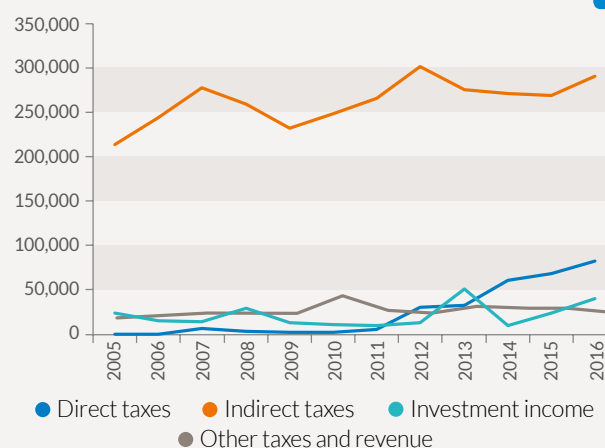
As can be seen in table 8.1, revenue from direct taxes increased 21.5%, with an execution percentage of 135.7%, meaning that it generated revenue that was 36% higher than the budget. This was the result of the major increase in personal income tax (IRPF), which brought in 28.5 million euros (63.1% more than the previous year). This tax was implemented on 1 January 2015, and in that year only monthly and quarterly retentions were made for employment income and income from capital, respectively. In 2016, however, not only were retentions on 2016 income reflected but also the effects of settlements and self-assessments of IRPF relating to income obtained in 2015.

The other major increase in direct tax was corporate tax, which brought in 40.7 million euros, 33% more than in 2015. This tax form is directly related to business results. So, its figures demonstrate an improvement in economic activity within Andorra's business network and confirms the improving climate of confidence which entrepreneurs express in these opinion surveys.

In contrast, non-residents' income tax (IRNR) brought in 11.6 million euros, representing a drop in revenue of 26.5%. It has to be said that this tax has been affected by the signing of various double taxation agreements, especially those with Spain and France.

Finally, in the section on direct tax, revenue from tax on economic activities shows ever smaller figures, with a major drop compared

GOVERNMENT NON-FINANCIAL REVENUE (Thousands of euros)



Source: Ministry of Finance.

with the previous year. This behaviour can be explained by the fact that income generated by these activities has been integrated into the current IRPF.

The IGI tax consolidates its position as Andorra's main source of tax revenue.

Revenue from indirect tax, on the other hand, still has the most important impact on the total. 2016 generated 290.7 million for the public coffers, with an increase of 8.1% against the previous year, thanks to the increase of 9.8% in the IGI consumption tax, which collected 127.8 million euros. This is the result of the improvement in economic activity in the service sector, which is analysed in a later section, and positions this tax (IGI) as the main revenue form for Andorra.

In the same vein is the increase of 5.6% in revenue from taxes on foreign trade, which brought in 107.6 million euros, with an execution rate of 104.5%. Within these taxes are notably consumption tax, a customs duty applicable to agricultural products imported into Andorra, which provides almost 100% of foreign trade tax revenue. This revenue is directly linked to imports of raw materials needed to manufacture Andorran tobacco.

IMPLEMENTATION OF THE GOVERNMENT BUDGET1⁽¹⁾ (Millions of euros)

Table 8.1

	Settlement 2016	Variation % Settlement 16/15	% execution 2016 ⁽²⁾
Direct taxes	82.9	21.5	135.7
On capital gains on property	1.9	49.8	115.6
On personal income tax (IRPF)	28.5	63.1	151.5
On companies /economic activities	40.8	21.4	116.1
On non-residents' income	11.6	-26.5	213.0
Indirect taxes	290.7	8.1	104.3
On property transfers	2.4	1.8	125.7
On consumption (IGI)	127.8	9.8	102.8
On services (ISI)	6.6	140.3	207.7
Special taxes	45.0	1.7	100.4
On foreign trade	107.6	5.6	104.5
On gambling	1.3	-7.7	83.4
Other taxes and revenues	24.7	-14.4	97.4
Current transfers	0.1	22.5	-
Investment income	40.4	71.6	135.3
Real investment sales	0.0	215.4	-
Capital transfers	0.0	-	-
Non-financial revenue	438.8	12.3	111
Current expenditure	365.9	21.9	96.0
Personnel costs	105.6	5.5	97.6
Consumption of goods and services	44.0	-3.0	87.9
Financial expenditure	16.2	-7.3	89.0
Current transfers	200.1	45.9	97.8
Capital expenditure	50.3	-51.6	65.9
Real investments	44.5	-3.2	65.4
Capital transfers	5.7	-90.1	69.6
Non-financial expenditure	416.2	3.0	91.0

(1) Settlement of the 2016 budget is provisional.

(2) In the case of expenditure, this is calculated from the final budget, which is the result of incorporating into the budget passed by the General Council the credit obligations undertaken during the previous financial year relating to expenses proposed for the following financial year, and the modifications and increases in budget credit. In 2016 these modifications represented an increase of 8.1% on the initial non-financial spending budget.

Source: Ministry of Finance.

Special taxes, which are the third largest tax form in volume of revenue, generated 45 million euros, with an increase of 1.7% against 2015. These taxes are applicable to imports and manufactures of specific products such as alcohol, tobacco and fuels. The fact that they behaved almost identically to the previous year implies a certain stability in the import figures for these products and is also a clear indication of the maturity of the market in the three taxed products, especially in the case of fuels.

The only decline in indirect revenue occurred in the tax on gambling which consists of the tax on bingo and the tax on gambling activities since the end of 2015, falling 7.7% against the previous year, and providing revenue of 1.3 million euros to the Government.

Other taxes and revenue saw a drop of 14.4%.

For their part, other taxes and revenue saw a decrease of 14.4%, with collected revenue of 24.7 million euros. This was basically motivated by two circumstances: on the one hand, the decline in revenue from sanctions, which fell 50.9%, with 4.3 million less than in the previous year, and on the other hand, the reduction in withholding tax on savings income, which fell 34.6%, with revenue for this concept of 1.6 million euros. This decline is basically attributable to the exceptionally low interest rates on the euro and major currencies. It should be remembered that this source of revenue will end in 2017 with the withholding tax obtained in 2016, due to the tax transparency agreement between Andorra and EU countries.

As for taxes, in 2016, the rate of vehicle ownership tax did not increase nor the tax on the registry of owners of economic activities, applying the same rates as in 2015. This is the eighth consecutive year in which the rates for both taxes have remained stable.

Through investment income, the Government increased revenue by 71.6%, to 40.4 million euros. This trend can be explained by the increase in dividends distributed by the public entities Andorra Telecom and FEDA. Except for the distribution of Andorra Telecom's reserves in 2013, as mentioned, in other years the routine of distributing dividends consists of 30% of FEDA 's profits and 100% of Andorra Telecom's profits.

1.2. Expenditure

Non-financial expenditure settled in 2016 was 416.2 million euros, an increase of 3.0% compared with the previous year. This trend is the result of an increase of 5.5% in personnel costs, combined with a decrease of 3.0% in consumption of goods and services, a decrease of 7.3% in financial expenditure and a decrease of 3.2% in real investments.

A case apart is the increase in current transfers of 45.9% which, as already mentioned, can be explained mostly by the variation in the reclassification of the subconcept of Transfers to communes from chapter 7 to chapter 4,

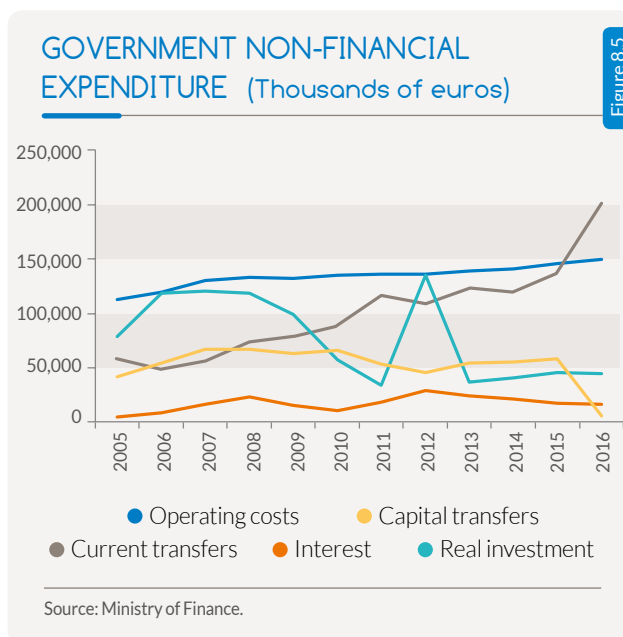
according to the amendment approved by the General Council during the debate on the Budget Bill for 2016. This caused the fall of 90.1% in capital transfers. For 2017, it should be noted that the General Council decided not to continue the freeze on the global amount of transfers to communes, in force since 2014. This will involve a notable increase in this transfer entry.

Current transfers represent almost half of total non-financial expenditure, and personnel costs one quarter.

A consequence of this reclassification was the change in weighting between current expenditure and capital expenditure. So, 2016 ends with current expenditure representing 87.9% of total

non-financial expenditure, while capital expenditure represents the remaining 12.1%.

Analysing the different entries, current transfers represent 48.1% (200.1 million euros) of total non-financial expenditure. In second place are personnel costs (25.4% of total non-financial expenditure), of 105.6 million euros, with an increase against the previous year of 5.5%. This increase can basically be explained by the increase in the social benefits entry, which encompasses various concepts related to pensions, basically retirement pensions and supplements to mandatory retirement benefits, and also by the repeal of the wage freeze measures that affected seniority payments and high wages.



The chapter of consumption of basic goods and services fell 3%, with an expenditure figure of 44 million euros, in line with the levels these chapters reached in 2013 and 2014, offsetting the increase of 3.3% that was generated in 2015. This entry's share of total non-financial expenditure stands at 10.6%.

Finally, the trend in the chapter of financial expenditure continues to fall in the last four financial years, and on this occasion shrinks 7.3%, leaving the expenditure figure at 16.2 million euros. This situation, which can still be explained by contained lending interest rates existing on the monetary market, leaves this type of expenditure at 3.9% of total non-financial expenditure.

Regarding capital expenditure, real investment broke with the growth trend of the last two years and fell to 44.5 million euros, 3.2% less than in the previous year, at 10.7% of total non-financial expenditure.

2. Communes

According to the settlement of the 2016 commune administration budgets, if we include financial assets and liabilities, the total volume of commune revenue reached the figure of 139.5 million euros and settled expenditure stands at 123.5 million euros. This means that the balance for the commune administrations as a whole is positive for the ninth consecutive year, at 15.9 million euros, which generated a positive variation of 46% regarding the previous financial year, in which the commune surplus reached 10.9 million euros. This increase in the surplus is the result of an increase in revenue of 2.9 million (2.1%) and a reduction in expenditure of 2.1 million (-1.7%).

The budget balance for all the commune administrations together is positive for the ninth consecutive year.

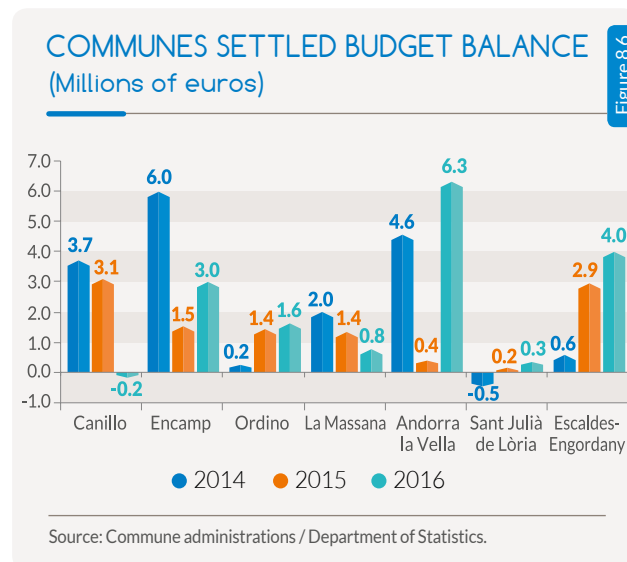
The decrease in expenditure was mainly motivated by the steep fall in capital expenditure, which went from 21.4 million in 2015 to 9.4 million in 2016 and, to a lesser extent, by the reduction in current expenditure from 88.2 million in 2015 to 87.3 million in 2016. The increase in commune revenue, on the other hand, can mainly be explained by the increase of 11.5% in current income.

This situation of surplus in the commune accounts extends to all the communes, except Canillo, the only commune with a deficit on closure of the 2016 financial year. It should be noted, however,

that this deficit was the result of Canillo reducing the bank debt in 2016 and makes it the commune with the least debt both in absolute figures and as a percentage of total revenue. Of the other six communes with a positive result in their accounts, there are five who increased their surplus; only La Massana saw their surplus shrink.

Specifically, Andorra la Vella became the commune with the largest surplus (6.3 million euros), compared with 0.4 million euros in 2015; then comes Escaldes-Engordany (4.0 million euros); Encamp (3.0 million euros), doubling its surplus; Ordino (1.6 million euros); La Massana (0.8 million euros), reducing the level it reached in 2015 by 42.6%, and Sant Julià de Lòria (0.3 million euros), doubling the previous surplus. As has been said, Canillo is the only commune that ended the year with a deficit, of 0.2 million euros.

For the third consecutive year, all the communes are clearly under the legally-established debt limit.



As for the communes' debt, they ended 2016 with a consolidated debt of 142.6 million euros, according to the data published by the communes, a figure that represents a drop of 13.5% against the 2015 data already reviewed

by the Court of Accounts, and which represents the seventh consecutive year of debt reduction. The debt reduction in 2016, in absolute terms, was 22.3 million euros. With this level of debt for the third consecutive year, the communes are clearly under the legal debt limit (200% of average settled revenue in the last three years).

With these figures, the communes represent 13.3% of the total public debt (seen as the total debt of the central government and communes), a percentage that was 15.4% in 2015. This share represents 5.5% of Andorran GDP.

The analysis by parishes shows that in the 2016 financial year, the communes reduced the debt, in line with the surplus situations that occurred. In absolute terms, the most indebted commune is still Andorra la Vella, with a figure of 38.2 million euros, a reduction of 10.3% from the previous year. On the other hand, the commune with the lowest level of public debt is Canillo (5.7 million euros), dropping from 50.5% in 2015.

In summary, there have already been seven consecutive years of collective effort to reduce levels of commune debt and the reward for their efforts is evident.

2.1. Revenue

The settled commune revenue increased for the fourth consecutive year, by 2.1% on this occasion, to reach the figure of 139.5 million euros, 5 million more than budgeted. With this level of revenue, the share of total public sector revenue (total revenue of central government and the communes) stands at 10.66%, the lowest in the last 15 years. As has already been mentioned in the reports of previous years, to a large extent this very low level was a distortion due to the central government's volume of financial liabilities, as a result of its borrowing requirements, especially from 2009, which artificially reduced the communes' share of the total. So, if just non-financial revenue is considered,

the commune share rises to 24.1%, a higher percentage than they represent in total non-financial revenue (18.9%).

The communes have increased their settled revenue for the fourth consecutive year, at a rate of 2.1% in 2016, to reach a figure of 139.5 million euros.

Observing trends by chapters, the increase in revenue can be explained by the increase in current revenue, which increased from 90.5 million in 2015 to 100.9 million in 2016, representing an increase of 11.5%. Within this revenue is notably the increase of 37.9% in indirect taxes. The most important entries in revenue are obtained from other taxes and revenue, bringing in 37.7 million euros and increasing 10.5%, and from direct taxes, bringing in 25 million euros, with an increase of 6.7% against the previous year.

For its part, capital revenue fell 8.2%, due to receiving less revenue through transfers of real investments, which fell 3.0%, and also the 8.3% fall in capital transfers, which reached 38.1 million euros.

By parish, Encamp, Ordino and Escaldes-Engordany saw falls in total settled income (-7.5%, -4.5% and -2.2%, respectively). If only non-financial revenue is considered, the negative trend only occurred in Encamp and Ordino (-0.2% and -4.5%, respectively). On the other hand, the commune that most increased non-financial revenue is Andorra la Vella (12.4%), due to the major increase in current income (17.1%), basically due to strong growth in the collection of other taxes and revenue. In contrast, La Massana saw a more moderate increase of 3.1% and the other communes show increases in non-financial revenue of about 6%. Specifically, in Canillo growth was 5.6%; in Sant Julià de Lòria, 6.2%, and in Escaldes-Engordany, 6.4%.

2.2. Expenditure

The communes' settled expenditure in 2016 reached the figure of 123.5 million euros, 1.7% less than in the previous year, a trend that contrasts with the increase of 7.8% that occurred in 2015. With this decline, the communes' share of total public sector expenditure (central government plus communes) fell 3.8 points to 9.9%, which remains below their share of revenue.

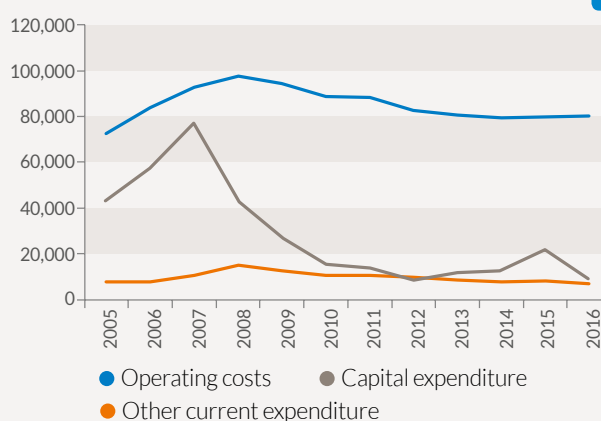
In the case of non-financial expenditure, the decline was even more significant (11.8%), resuming the path of seven consecutive years of reductions which was broken in 2015 with a rise of 9.4%, due to the major increase that occurred in real investments.

If only non-financial expenditure is considered, commune expenditure's share of total administration expenditure rises to 18.9%, 2.5 points less than in the previous year, and also lower than the percentage of non-financial revenue.

As for financial operations, these increased 68.4% due to a major increase both in financial assets (170.8%) and financial liabilities (38.5%), due to debt amortisation.

By chapters, the decrease in commune expenditure can be explained basically by the steep fall in capital expenditure (-56.0%), which compensates the increases over the last three years and leaves

COMMUNES' NON-FINANCIAL EXPENDITURE
(Thousands of euros)



Source: Commune administrations / Department of Statistics.

COMMUNE ADMINISTRATIONS' BUDGET SETTLEMENTS (Thousands of euros)

Table 8.2

	INCOME			EXPENDITURE		
	2016	Var. 16/15	% 2016	2016	Var. 16/15	% 2016
Canillo	13,487.37	5.6	9.7	13,664.95	41.5	11.1
Current	7,534.80	11.1	5.4	6,327.38	0.3	5.1
Capital	5,952.57	-0.7	4.3	2,504.59	49.1	2.0
Financial	0.00	0.0	0.0	4,832.98	189.3	3.9
Encamp	25,404.91	-7.5	18.2	22,398.73	-13.7	18.1
Current	18,153.64	4.3	13.0	17,040.11	0.6	13.8
Capital	7,251.27	-9.9	5.2	708.82	-89.2	0.6
Financial	0.00	0.0	0.0	4,649.80	91.4	3.8
Ordino	11,364.36	-4.5	8.1	9,719.71	-7.1	7.9
Current	6,441.35	0.2	4.6	6,441.35	0.2	5.2
Capital	4,923.01	-10.0	3.5	763.55	-33.0	0.6
Financial	0.00	0.0	0.0	2,514.81	-13.1	2.0
La Massana	13,760.52	3.1	9.9	12,980.22	8.3	10.5
Current	11,438.40	4.2	8.2	7,810.65	-1.4	6.3
Capital	2,322.12	-2.2	1.7	1,202.88	-28.9	1.0
Financial	0.00	0.0	0.0	3,966.70	67.0	3.2
Andorra la Vella	37,908.43	12.4	27.2	31,568.24	-5.4	25.6
Current	30,112.53	17.1	21.6	26,185.95	2.0	21.2
Capital	7,795.90	-3.0	5.6	2,533.83	-48.3	2.1
Financial	0.00	0.0	0.0	2,848.46	1.9	2.3
Sant Julià de Lòria	13,327.01	6.2	9.6	12,977.51	4.8	10.5
Current	7,522.42	11.6	5.4	7,778.30	-18.7	6.3
Capital	5,804.59	-0.1	4.2	220.24	-88.2	0.2
Financial	0.00	0.0	0.0	4,978.97	427.1	4.0
Escaldes-Engordany	24,226.13	-2.2	17.4	20,233.25	-7.3	16.4
Current	19,668.34	19.7	14.1	15,675.46	1.7	12.7
Capital	4,557.79	-28.0	3.3	1,498.76	-58.1	1.2
Financial	0.00	0.0	0.0	3,059.03	7.8	2.5
Total	139,478.73	2.1	100.0	123,542.61	-1.7	100.0
Current	100,871.47	11.5	72.3	87,259.20	-1.1	70.6
Capital	38,607.25	-8.2	27.7	9,432.66	-56.0	7.6
Financial	0.00	-100.0	0.0	26,850.75	68.4	21.7

Source: Commune administrations / Department of Statistics.

the investment figure at 9.4 million euros. In relation to current expenditure, the fall was 1.1% and was concentrated in the decrease in financial expenditure (-20.0%), falling for the fifth consecutive year, a figure that can be explained by debt reduction and interest rates, current transfers (-15.2%) and personnel costs (-0.7%). The latter entry is the most important in volume, with 38.7% of total expenditure and an absolute figure of 47.9 million euros. The fall occurs for the sixth consecutive year and demonstrates the fiscal containment effort being made by the communes.

The trend in expenditure by parish varies greatly.

Finally, the trends in expenditure by parish show very uneven behaviour. There are four parishes that have pursued a reduction in expenditure, allowing for this general decline of 1.7%. So, Encamp reduced expenditure by 13.7%; Escaldes-Engordany by 7.3%; Ordino, by 7.1% and Andorra la Vella by 5.4%. The other three parishes increased expenditure: Canillo, significantly (41.5%), La Massana (8.3%) and Sant Julià de Lòria (4.8%). Anyway, as has been said, Canillo caused this increase in expenditure basically by amortising the debt and through the investments made.

In relative terms, Andorra la Vella is still in first place for volume of expenditure, with 25.6%, followed by Encamp, with 18.1%; on the other hand, Ordino appears as the commune with the lowest volume of expenditure (7.9% of the total).

3. The Social Security System (CASS)

CASS is the body in charge of financing the benefits linked to public health and public pensions, by collecting contributions from businesses, employees and self-employed workers.

Health and pensions, significant influences on future developments in Andorran public finances.

Historically, CASS had presented no issues to Andorra's public finances but, since 2011, deficits from health provision have been financed by the Government budget.

Current contributions are 22% of wages, 10% of which finance the general branch, and 12% the pensions branch. Contributions are divided between the business and the employee, in a proportion of 15.5 points paid by the business and 6.5 points paid by the employee. Self-employed workers pay the same percentage based on the average employee wage in the previous year, with the possibility of discounts based on specific parameters.

The health cost financed by the CASS was, for many years, except in very specific situations, always lower or equal to contributions received. The population was, on average, relatively young and many treatments for chronic illnesses, that are now current, did not exist before.

To correctly evaluate the health costs incurred in Andorra, we must consider not only the health costs financed through the CASS, but also the fact that an additional cost exists that is reflected in the deficit of the SAAS (Health Services) and another section that is financed by co-payment directly by citizens. The figures in this report only use the cost financed through the CASS as a source which, in any case, is very significant in relation to the global cost.

On the other hand, regarding the financing of pensions, the major disproportion between the young population (due to immigration) and the retired population meant that for many years surpluses were very high and deceptive. This created an image of false abundance and resulted in no provision for future obligations, linked to the pension branch.

The future trend, both in health costs and obligations to future pensioners, will be a vital element in Andorran public finances.

CASS is therefore the body in charge of financing two branches relating to totally different activities: the general branch and the pension branch. Moreover, in 2015, a new body was created, the Pension Reserve Fund, which assumes functions that belonged to the CASS until now. This new body takes charge, specifically, of the management of accumulated reserve funds which are solely destined to meeting the future pensions of those who have paid into the CASS.

3.1. General branch of the CASS

The trend reflected in figure 8.8 shows 2006 as a surplus year. In fact, not only 2006 but also all previous years had surpluses or balanced settlements. This historical trend had allowed for the accumulation of 63 million euros in reserves in this branch until that year.

From 2007, the current period of chronic deficits began, with major increases in spending every year. Some spending containment and control measures enabled this trend to be broken in 2012, but from 2014, it again exceeded the health expenditure prior to the containment measures (2011). The health reform announced on several occasions has never materialised. The announced measures, such as allocating GPs and sharing medical histories, although suitable measures in the organisational field, are unlikely to produce significant savings in costs. Currently, the system is in a phase of restructuring of the SAAS and of contractual changes and agreements between the various agents in the health system (CASS, SAAS and health professionals) and the results will become visible in years to come.

The current period of chronic deficits started in 2007, with major increases in spending from year to year.

With respect to revenue, this has evolved in parallel to the economic situation in the country during the years of crisis, with an upturn in revenue in 2013. However, to get a true picture of revenue

for the period 01/03/2015 – 01/04/2016, we must take into consideration the fact that the Government decided to reduce contributions in this branch by two points (from 10% to 8%) to fortify contributions to the pension branch (from 10% to 12%), without incurring extra costs on the businesses or employees. The important reduction in revenue in 2015 (despite being in a phase of economic recovery) is due to this. So, the major quantitative leap in revenue in 2016, apart from the general trend towards slight improvement is, above all, the consequence of the recovery of these two percentage points which had not been paid in the said period.

The deficits in the general branch shown in Figure 8.9 were financed from the Government budget as soon as the accumulated reserves of this branch ran out, in 2011. The 63 million euros accumulated in the reserves of the general branch were used in the period 2007-2011 to offset the deficits.

The legislative reforms that oblige the Government to take charge of the deficits in the general branch are set out in article 86.2 of Law 17/2008 on social security.

The mentioned obligation of the Government in relation to the deficit looks as if it will become permanent henceforth. The aging population

GENERAL BRANCH INCOME AND EXPENDITURE (Thousands of euros)

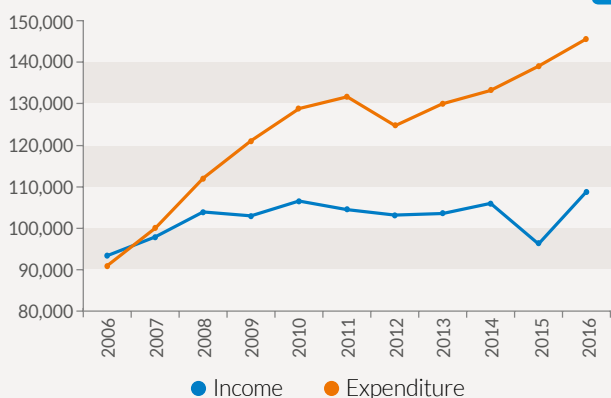


Figure 8.8

GENERAL BRANCH SURPLUS/DEFICIT (Thousands of euros)

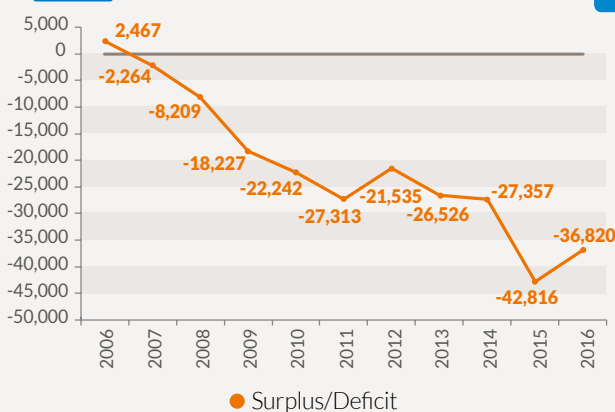
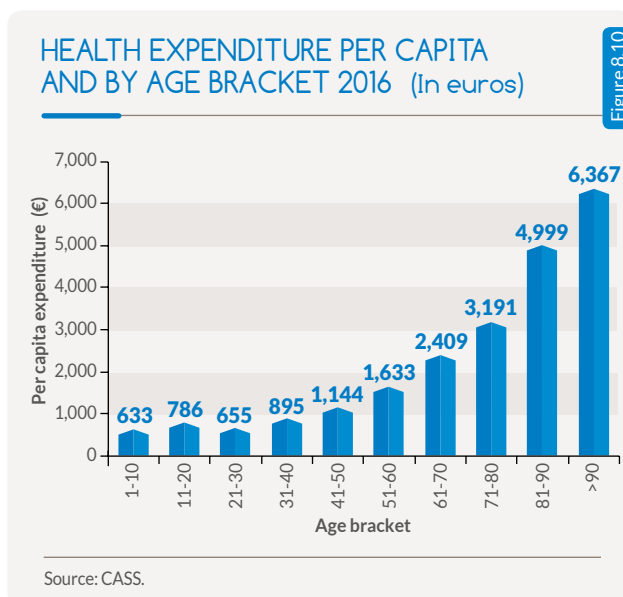


Figure 8.9

Source: CASS.

and growth in chronic illnesses mean that health costs will continue to grow. The age pyramid (on 31/12/2016) in the sections on population and the pension branch clearly shows a large concentration of the Andorran population between the ages of 35 and 55. In twenty years' time, this demographic cohort will still probably be a majority, but 20 years older, with the health and social costs that that implies.

The demographic trend is structural and it can easily be seen in the age pyramids that the bulk of the population is aging and is still the bulk of the population. Figure 8.10 exemplifies the cost by age bracket which CASS finances for people who have consumed health benefits.



It is likely that these populous demographic cohorts, in ten years' time, will reach average levels of unit cost that double current expenditure, generating a serious problem for health financing and, therefore, public finances. In 2016, the resulting average health cost was 1,295 euros per capita. As the years go by, more population will be added to the above-average unit values, with the consequent increase in cost. This problem will become evident progressively and, in a few years, the budget entry for health finance will accelerate.

3.2. CASS pension branch

Andorra's public pension system is defined as a point system. This means that the pension is calculated by considering the contributions over the whole of the working life and the resulting pension is directly proportional to the contributions paid.

If the conversion factor used (proportion between purchase and sale cost of points) is adequate and has been adapted to the continuous increases in life expectancy over the last fifty years, the system will be financially balanced in the long term. The conversion factor relates to the number of expected years from the time when the pension is first paid.

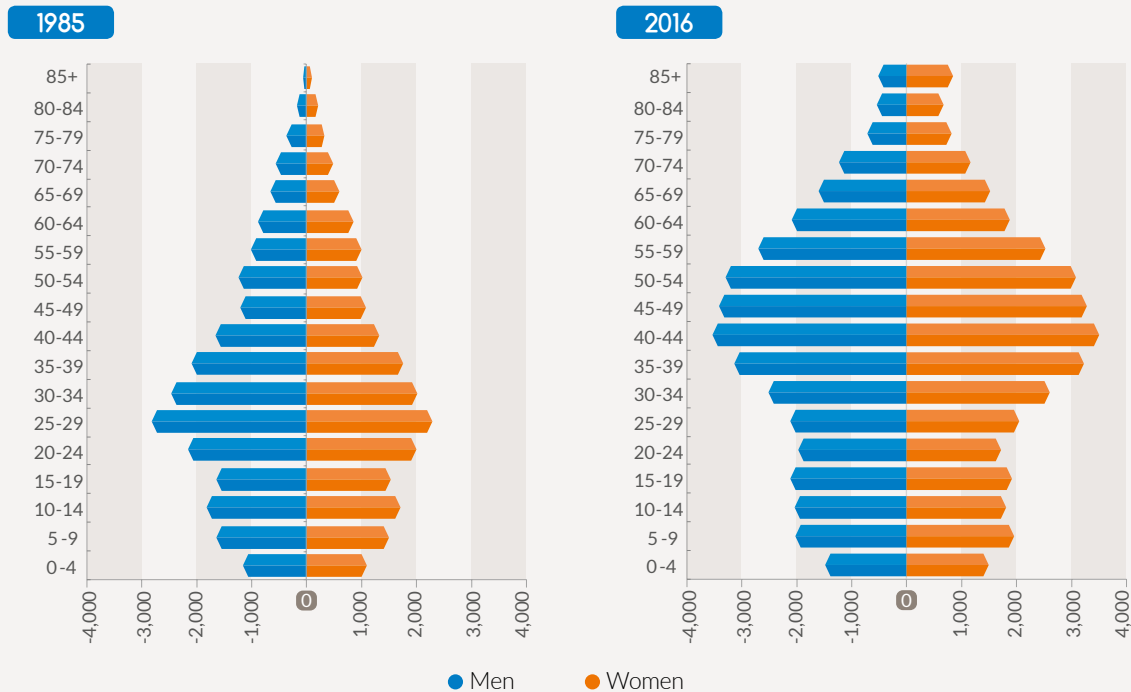
In 1968, the conversion factor was 6.4 and was adequate for the time, when life expectancy was calculated at about 71-72. This conversion factor, which is the basis for calculation of the pension rights, remained unchanged for forty years with no modification to adapt it to the increase in life expectancy. In the last nine years, two reforms have been made (clearly insufficient from an actuarial point of view), which put this conversion factor at 8 (from 01/11/2009) and 9.6 (from 01/03/2015). This value is totally inadequate and far from what it should be, which should be close to 20, if you consider that life expectancy is getting progressively closer to 85.

As has been said in the introduction, the great disproportion between the young population and pensioners meant that over a very long period the annual surpluses were very high, and this allowed for a distorted view of reality, of false abundance, which meant that future obligations linked to acquired rights were not foreseen.

Likewise, the baby boom phenomenon from the end of the 50s until the start of the 70s needs to be considered. Those born in those years are now between the ages of 45 and 60 and represent a major bulk of the population which in the next 10-20 years will expand the pensioner group exponentially.

POPULATION STRUCTURE BY AGE AND GENDER. 1985 & 2016

Figure 8.11



Source: Department of Statistics.

For the pension system to receive new pensioners at a constant rate would be more acceptable than to receive large numbers in a short time. This phenomenon will occur in the next 10-20 years and will either incur great cost on the Government budget or put the system at risk of collapse.

The baby boom population has, to a large extent, spent all or a large part of their professional life in Andorra and, therefore, accumulated an appreciable volume of pension rights (in the form of acquired points). Average pensions for this group will be significantly higher than current average pensions.

As for pensions, Andorra has latent, significant, medium and long-term financial and social problems.

So, the panorama to be expected in a few years' time is that successive populous generations with acquired rights that are disproportionally high to the paid contributions will gradually enter the group of pensioners.

Moreover, as contributions have not been revised in relation to life expectancy, these have remained at very low levels of wages. This means that businesses and workers pay less than other countries. The flip side of this competitive advantage is that the resulting pensions, although generous in relation to the paid contributions, will be low for maintaining living standards.

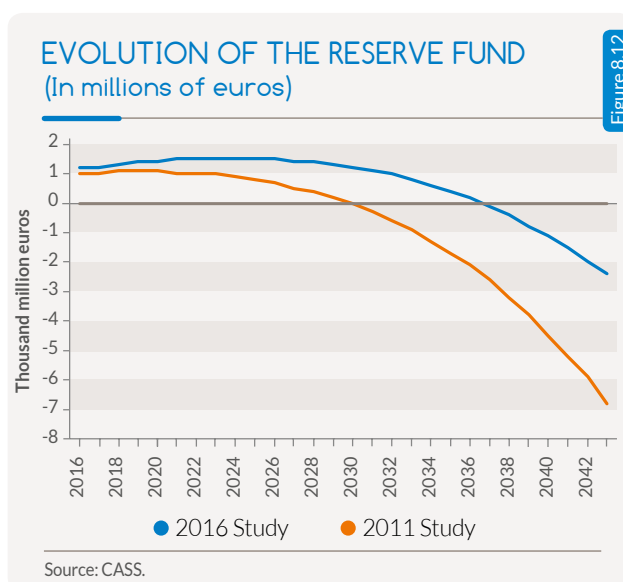
So, in pensions, Andorra has huge latent mid- and long-term financial and social problems.

The warning about this problem is quantified in the actuarial studies of the CASS. Figure 8.12 summarises the conclusions of the last two actuarial studies that have been carried out. Both studies agree in their conclusions.

The first (carried out in 2012 using data prior to 2011) predicts the deficit to start around 2017-2018 and reserve funds to run out in 2030-2031. Faced with the proximity of these events, reforms were carried out in 2015. The reforms resulted in the said timescales improving notably, with the fund

balance starting to shrink in 2023 and the funds running out in 2037, according to the second actuarial study (carried out in 2016 using data prior to 2015). The main core of the reform was;

- A 2-point increase in contributions.
- Modification of the return per points acquired after 01.03.15, for wages more than four times above the minimum wage.
- Calculation of disability benefit using pension criteria so that those retiring from a normal working situation do not get a lower pension than those with disability status.



- Creation of a sustainability factor which would influence the interannual update of pensions based on a series of variables. This measure has not yet been put into action, while awaiting regulatory definition of the weighting of each variable.

Actuarial studies are based on variables which may evolve over time but which are, in any case, indicative of trends which, with a certain margin of error, are needed to raise awareness of the size of the problem and design solutions or remedial tools.

As an example, Spain is about to exhaust the “pension pot” and it is very likely that at the time of publishing this document, the general budgets of the Spanish state will have to inject liquidity to pay pensions in Spain.

According to the general provisions of Law 17/2008 on social security, articles 86.3 and 88.2 of Law 18/2014, which amends the previous, specifically oblige the Government to make contributions to the pension system from the point when the accumulated funds start to disappear. This principle aims to make future governments react once the problem starts to appear, without allowing the fund to run out totally before the government intervenes. According to the actuarial provision, if no new reforms are made, the Government budget must provide specific budget entries destined for the Reserve Fund (for the first time) from 2023. From that year on, contributions must grow successively and be of a considerable size.

As a conclusion of the chapter dedicated to CASS, it should be noted that two of the most important problems for the future of public finances revolve around this body. The health financing challenge and the pension financing challenge will be primary elements in the political decisions to be taken in the next few years.

4. Pension Reserve Fund (PRF)

Law 6/2015 created a new body called the Pension Reserve Fund (PRF), with the object of managing accumulated reserve funds destined exclusively to covering future pensions of those who have paid into the CASS.

The creation of this body is intended to organise the Fund to be as professional as possible, according to the standards of the most advanced countries in this matter. The investment strategy proposed by

a technical commission must be approved by the Board of Directors of the PRF (consisting of the same members as the Board of Directors of the CASS). Once approved, the strategy is carried out by a depoliticised technical team, with training and experience in financial and asset management. Half of the members of the Board of Directors are appointed by the Government, with the casting vote of the chairman, but independent technical profiles predominate on the Fund Management Committee.

The Fund Law sets the possible investment rates and maximum and minimum weightings of each rate. The legal objective is to invest carefully, with good quality assets and the goal of preserving long-term purchasing power in relation to inflation. Within these parameters and according to the defined strategy, the Management Committee takes the investment decisions, either directly or through management mandates.

Throughout 2015, this new body set up its structure with both human and technical resources, harnessing the synergies and experience of previous years, but it was from January 2016 that it effectively received control of the Fund assets.

The system of transferring funds between the CASS and PRF is provided in art. 20.1 of the Reserve Fund Law. Every quarter, CASS transfers funds from the pension branch surplus it obtains in the process of collecting contributions and paying pensions.

In table 8.3 is a summary of the progress of the Fund's assets in 2015 and 2016.

If the timeline is extended and a long-term series analysed, it can be seen that, except for 2008 (partly offset by 2009), the dynamic was positive, so the purchasing power of the Fund remains constant over time.

PRF ASSETS (In euros)

Table 8.3

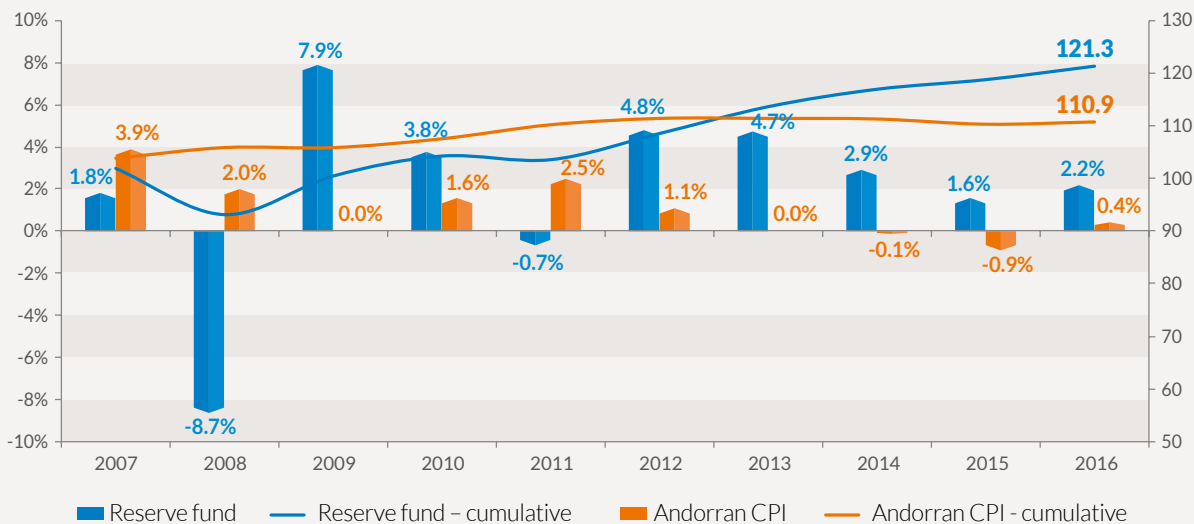
	2015	2016
PRF at start of year	1,042,539,184	1,094,594,019
CASS contributions	39,162,674	48,920,577
PRF returns	12,892,161	24,339,988
PRF at end of year	1,094,594,019	1,167,854,584

Source: Pension Reserve Fund.

The pension reserve fund held assets of nearly 1,168 million euros on 31 December 2016.

ANNUAL RETURNS AND CUMULATIVE PRF AGAINST INFLATION

Figure 8.13



Source: Pensions Reserve Fund.

As can be seen in figure 8.13 in table 8.4, analysing the last ten years, the Fund has gained an average of 0.91 points against inflation every year.

It should be noted that if major crises occur in the global markets, as was the case in 2008, a certain recovery period would be needed to regain lost ground. In the data, it can be seen that the period between 2009 and 2012 was necessary for cumulative returns to recover lost ground against inflation. From 2012, returns exceed inflation every year and increases the cumulative differential between both figures.

If the Fund's returns are measured against inflation over the last five years, the Fund has gained an average of 3.13 points against inflation every year.

In any case, it must be considered that these return data are not directly comparable with the trend in stock market returns. The PRF is composed of a combination of fixed income, monetary market, variable income, real estate and other assets. The PRF Law limits investment in variable income to a maximum of 35% of the Fund, with the intention that the management will not be subject to high levels of volatility, with the subsequent risks.

One of the main challenges faced by the PRF in 2016 is the negative return on high quality fixed income issuances in financial markets, as reflected in box 1.3 of the international economy section. This meant that in 2017, the PRF's investment strategy has authorised the upper limit of 35% variable income provided by the Law.

	LAST 10 YEARS	LAST 5 YEARS
PRF annualised returns	1.95%	3.23%
Andorran CPI	1.03%	0.10%
Differential	0.91%	3.13%

Source: Pensions Reserve Fund.

5. Tax burden

Andorra has always been, by vocation, a country with a low tax burden. Traditionally, commerce was based on achieving a competitive price differential through notably lower indirect taxes than our customers' countries of origin, especially Spain and France.

On the other hand, tax residents in Andorra have also benefited over the years from practically non-existent direct tax. Consumption tax was collected when goods entered the country, as were specific taxes on fuels and tobacco, which were the basic source of finance for this country for many years.

In recent years, especially due to international standardisation, tax forms have been evolving and the great tax reform of Andorra culminated in 2015 with the introduction of the IRPF.

In table 8.5, you can see the taxes and other tax forms which have been used to calculate the tax burden. These are at both state and commune levels and include CASS contributions.

Globally, as has always been the tradition in Andorra, indirect taxes are the most important in volume. Among these, the growth in both IGI and consumption tax are notable. These two tax forms are representative of the volume of consumption (both domestic and tourist) and volume of imports. Both magnitudes are correlated and show the growth in the Andorran economy.

Also notable is the growing contribution from income tax, especially the growing importance of the IRPF, which was non-existent until 2014. In contrast, withholding tax on savings income is gradually losing importance, which Andorra collected to implement Law 11/2005, of 13 June, on implementation of the Agreement between the Principality of Andorra and the European Community, relating to the establishment of measures equivalent to those provided in Council Directive 2003/48/EC on taxation of savings income in the form of interest payments. 2017 will be the last year when withholding tax will be applied to income obtained by foreign tax residents in 2016, as the tax transparency Agreement between Andorra and countries of the European Union comes into force.

ACCRUED TAXES 2015-2016

Table 8.5

Accrued tax (€)	2015	2016	Variation 16/15	% total 2016
D2. Tax on production and imports	279,896,276.51	303,755,183.36	8.5%	46.5%
D21. Product tax	275,886,751.40	297,470,932.57	7.8%	45.5%
D211. VAT-type taxes	119,169,872.20	134,461,203.74	12.8%	20.6%
ISI Insurance	2,739,683.50	2,997,595.43	9.4%	0.5%
ISI Banking & Finance	0.00	3,622,725.00	-	0.6%
IGI	116,430,188.70	127,840,883.31	9.8%	19.6%
D212. Taxes & duties on imports, excluding VAT-type taxes	146,122,857.70	152,586,092.29	4.4%	23.4%
Consumption tax	101,165,418.69	106,882,702.55	5.7%	16.4%
Common Foreign Tax (TEC)	646,100.98	661,109.53	2.3%	0.1%
Antidumping	25,172.45	13,507.13	-46.3%	0.0%
Special taxes	44,286,165.58	45,028,773.08	1.7%	6.9%
D214. Product tax excluding VAT and import tax	10,594,021.50	10,423,636.54	-1.6%	1.6%
ITP (Property Transfer Tax)	2,314,280.75	2,356,787.27	1.8%	0.4%
Bingo tax	1,447,428.85	1,316,878.63	-9.0%	0.2%
Gambling tax	0.00	19,285.85	-	0.0%
ITP (Communes)	6,832,311.90	6,730,684.79	-1.5%	1.0%
D29. Other production taxes	4,009,525.11	6,284,250.79	56.7%	1.0%
Tax on activities (G)	3,613,026.11	6,077,152.94	68.2%	0.9%
Business vehicle tax	396,499.00	207,097.85	-47.8%	0.0%
D5. Current taxes on income and assets	103,696,813.55	116,246,802.29	12.1%	17.8%
D51. Income tax	83,505,761.99	95,440,284.82	14.3%	14.6%
Capital gains tax	1,295,633.92	1,940,703.39	49.8%	0.3%
IS/IAE (Company/Business tax)	33,601,502.39	40,800,287.21	21.4%	6.2%
IRPF (Personal Income Tax)	17,482,110.70	28,510,440.85	63.1%	4.4%
Savings income withholding tax	9,494,904.96	6,209,420.88	-34.6%	1.0%
Non-resident's Income tax	15,845,028.50	11,646,711.47	-26.5%	1.8%
Rental income tax (Communes)	5,786,581.52	6,332,721.02	9.4%	1.0%
D59. Other current taxes	20,191,051.55	20,806,517.47	3.0%	3.2%
Private vehicle tax	4,203,868.27	4,409,790.93	4.9%	0.7%
Tax on activ. to open 24/24	27,560.00	24,783.82	-10.1%	0.0%
Direct taxes (Communes)	15,959,623.28	16,371,942.72	2.6%	2.5%
D61. Social contributions	209,310,753.98	233,437,051.83	11.5%	35.7%
D611. Effective social contributions	209,310,753.98	233,437,051.83	11.5%	35.7%
Accrued total (euros)	592,903,844.04	653,439,037.48	10.2%	100.0%

Source: Department of Statistics.

INDIRECT & DIRECT TAXES & SOCIAL CONTRIBUTIONS (Millions of euros)

Table 8.6

	2010	2011	2012	2013	2014	2015	2016
Production and import taxes	252.00	273.73	292.55	266.34	280.11	279.90	303.76
Current taxes on income and assets	38.85	55.56	70.97	92.85	102.32	103.70	116.25
Social contributions	206.07	205.51	200.62	200.15	204.36	209.31	233.44
Accrued total	496.92	534.80	564.14	559.34	586.79	592.90	653.44
GDP	2,533.55	2,476.22	2,463.02	2,471.69	2,525.45	2,535.12	2,584.10

Source: Department of Statistics.

In parallel, significant growth occurs in revenue from corporate tax. This increase is a symptom of the improvement in business results, in line with the improvements seen in other macroeconomic magnitudes.

Social contributions, in the form of contributions to the general and pensions branches of the CASS, saw major growth in 2016 due to the two-point increase in general branch contributions from 1 April.

To analyse the impact of social contributions, the legislative amendments to general and pensions branch contributions mentioned in the relevant chapter of CASS must be considered, causing a respective decrease and increase of 2 points on 1 March 2015 and 1 April 2016.

From the advance GDP figures, it can be established that the tax burden in 2016 was 25.3%, representing an increase of practically two points against 2015 (23.4%).

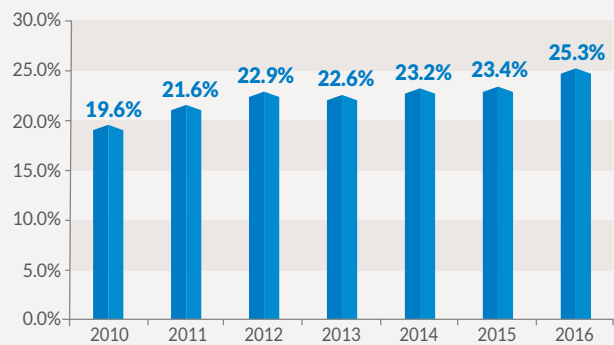
From a historical perspective, it can be seen that the tax burden has increased over the last few years, with the exception of 2013. Since 2010, when the tax burden was 19.6% of GDP, it has been increasing to the current 25.3%.

The increase in revenue from indirect taxes (IGI and consumption tax mainly) and direct taxes (basically IRPF) basically explains the increase of +10.2% in revenue from accrued taxes, greater than the +1.9% growth in nominal GDP. As for the impact on the tax burden from the different tax forms, indirect tax predominates (46.5% of the total), followed by social contributions (35.7%) and direct taxes (17.8%), although the latter has been gaining in importance in recent

The tax burden has risen almost two points, to 25.3% of GDP, a figure that sets a new historic high and contrasts with the 19.6% in 2010.

ANDORRA'S TAX BURDEN (% of GDP)

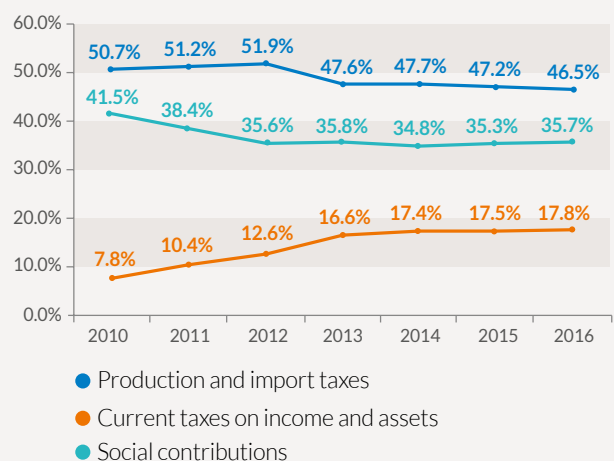
Figure 8.14



Source: Department of Statistics.

TAX BURDEN TAXATION STRUCTURE As % of total revenue

Figure 8.15



Source: Department of Statistics.

years with the introduction of new tax forms, culminating in 2015 with the introduction of the IRPF.

To conclude this chapter, it can be said that Andorra has a tax-friendly tax burden. In comparison with other European countries, Andorra is highly competitive in the tax field as, with 2015 data, which are the last available at the time of writing this text, it stands in the back at 23.4%.

A factor to be considered in analysing Andorra's tax burden is that a very large part of indirect taxes is on products or services acquired by visitors. The proportion of consumption attributable to visitors compared with strictly domestic consumption means that a significant part of the tax burden is not directly incurred on the resident population.

If the Irish tax burden stays the same (or shrinks) in 2016, this will be the only country with a lower tax burden than Andorra. Slightly above Andorra are countries such as Switzerland, Bulgaria, Lithuania, Latvia and Romania.

Spain and France have notably higher tax burdens at 34.6% and 47.9% of GDP, respectively (2015 data).

TAX BURDEN BY EUROPEAN COUNTRY. 2015 As % of GDP

Table 8.7

	2015
France	47.9
Denmark	47.6
Finland	44.1
Italy	43.5
Eurozone (19 countries)	41.4
Germany	40.0
European Union (28 countries)	39.9
Luxembourg	39.1
Portugal	37.0
United Kingdom	34.9
Malta	34.7
Spain	34.6
Latvia	29.5
Lithuania	29.4
Bulgaria	29.0
Romania	28.1
Switzerland	28.1
Ireland	24.4

Source: Eurostat.



The Andorran economy: developments in the main sectors

IX. Primary sector

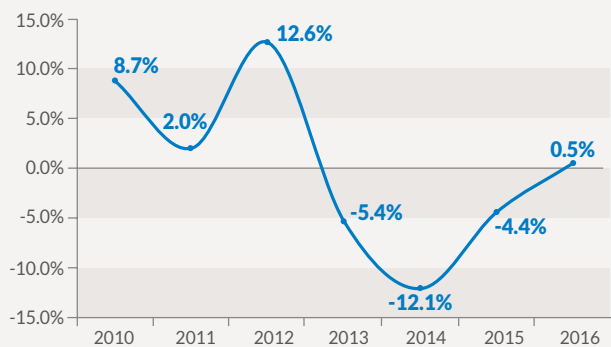
The primary sector is the smallest area of activities in the Andorran economy. According to the official figures for advance GDP, its influence on Andorran GVA stands at 0.5% and the trend was slightly positive in 2016, with an increase in GVA of 0.5% in real terms. This confirmed the change in trend in the primary sector that began to be seen in 2015 – when the rate of fall in GVA decelerated notably, recording a decrease of 4.4%, much gentler than the record downturn of 12.1% in 2014.

According to official GDP figures, the primary sector's contribution to Andorran GVA stands at 0.5%.

In 2016, the number of employees in the primary sector increased, from 164 in 2015 to 171 in 2016. This represents growth of 4.5% and the continuation of the trend which started in the previous year, when there was an increase of 2.4%. Monthly average wages also rose, by 3.5%, to 1,454.53 euros, regaining the levels of four years ago. In contrast, the number of businesses has continued the process of shrinking that occurred over the last three years: the sector went from 245 businesses in 2013 to 232 in 2016. In the last year, the decrease in businesses was 2.5%. Equally, over time the network of businesses in the primary sector has grown considerably, from 131 businesses in 2009 to 232 in 2016. It may be that these decreases are the consequence of a normal process of adjustment, after the significant rise in the number of businesses dedicated to the primary sector which occurred in 2013, by 61.2%. In any case, the business structure based on micro-businesses has endured, as 95.3% of businesses in this sector have between 1 and 5 workers.

In 2016, 315 farms were registered, the same number as in the previous year, although the total farmed surface area increased moderately by 0.9%. The parish with most activity is still Sant Julià de Lòria, with 64 holdings, while Escaldes-Engordany closes the ranks with only 28.

PRIMARY SECTOR GVA
Real variation in %



Source: Department of Statistics.

FARMS BY PARISH

	2016	% total 2016
Canillo	48	15.2%
Encamp	46	14.6%
Ordino	37	11.7%
La Massana	55	17.5%
Andorra la Vella	37	11.7%
Sant Julià de Lòria	64	20.3%
Escaldes-Engordany	28	8.9%
Total	315	100%

Source: Department of Agriculture.

TOBACCO HARVEST BY PARISHES (Kilogrammes)

Table 9.2

	2015	2016	Var. 16/15 (%)	% total 2016
Canillo	14,127.2	15,933.4	12.8%	6.5%
Encamp	29,465.1	29,461.5	0.0%	12.1%
Ordino	31,671.8	31,652.8	-0.1%	13.0%
La Massana	45,539.6	45,512.6	-0.1%	18.6%
Andorra la Vella	30,073.5	30,078.7	0.0%	12.3%
Sant Julià de Lòria	80,389.1	80,075.1	-0.4%	32.8%
Escaldes-Engordany	11,370.2	11,369.6	0.0%	4.7%
Total	242,636.5	244,083.7	0.6%	100%

Source: Department of Agriculture / Association of Andorran Tobacco Product Manufacturers (AFPTA).

Making an analysis over time, in the last five years there has been a progressive fall in the number of farms: in 2011, there were 359 farms and in 2016, 315, yet the total cultivated area grew from 20.7 km² to 21.2 km², indicating that the average size of farms is increasing. By type of farm, in the last five years the surface area dedicated to fallow, aromatic and medicinal plants and potatoes has fallen significantly; on the other hand, the surface area dedicated to hay, tobacco, grazing and market gardening has increased.

By type of crop, 61.1% of the total surface area of farms is dedicated to grazing, 25.4% to hay and 7.4% to tobacco. In 2016, there was notably strong growth in the agricultural area dedicated to market gardening (30.9% growth), although it only represents 0.8% of the total surface area.

In 2016, the tobacco harvest saw moderate growth of 0.6% against the previous year, much lower than in 2015, which was 1.9%. This can be explained fundamentally by the significant increase in the Canillo harvest (12.8%), recovering from the bad result of the previous year. The other parishes maintained similar or slightly lower harvest levels than in 2015. In total, the volume produced, after adjustment for the quotas allocated to farmers, was 244,084 kg, 1,447 kg more than the previous year. Sant Julià de Lòria remains the parish with the largest harvest, with 80,075 kg, followed by La Massana, Ordino, Andorra la Vella and Encamp. The 2016 season saw no significant incident either during planting or the growing period. The number of cultivated plants reached usual levels and the number of plants affected by hail remained at similar levels to the previous season.

As for livestock, in 2016, the number of livestock fell 5.0%, with 5,211 registered units, representing two consecutive years of decreases (in 2015, it fell 7.5%). This downward trend occurred as a result of a drop in sheep

breeding and farming, which fell 9.6% to reach 2,727 heads, and also in the decrease in goats, which fell 16.0%, leaving the total number of heads at 242. In contrast, the number of cattle increased 3.2%, to 1,585 heads, and the number of horses increased 2.0% to 657 units, after the strong decline seen in 2015 (-20.2%). The process that was started in October 2013 to market Andorran veal under the seal of quality "Carn de qualitat controlada d'Andorra" (Andorran quality-controlled meat) and the Protected Geographical Indication seal "Carn d'Andorra IGP" (Andorran Meat PGI) still had a positive impact on the trend in numbers of cattle in 2016.

Agricultural and livestock farmers are making efforts to introduce improvements and diversify production.

On the other hand, 2016 was the second year in which the Andorran livestock company, Ramaders d'Andorra SA, marketed horsemeat under the quality seal. The Regulations relating to the use of

LIVESTOCK BY PARISH (Heads)

Table 9.3

	2015	2016	Var. 16/15 (%)	% total 2016
Canillo	521	531	1.9%	10.2%
Encamp	1,891	1,764	-6.7%	33.9%
Ordino	334	383	14.7%	7.3%
La Massana	752	382	-49.2%	7.3%
Andorra la Vella	133	136	2.3%	2.6%
Sant Julià de Lòria	1,806	1,987	10.0%	38.1%
Escaldes-Engordany	46	28	-39.1%	0.5%
Total	5,483	5,211	-5.0%	100%

Source: Department of Agriculture.

the official quality seal “Carn de qualitat controlada d’Andorra” for the production of horsemeat, on 11 February 2015, guarantees the high quality of the horsemeat production. The certification processes of the Government or authorised bodies ensure that the animals, born in Andorra, are nursed by their mother for six months in open pastures (valley floors, clearings and mountains), fattened with concentrated feed specially formulated for the breeding conditions in Andorra, and then slaughtered at the National Slaughterhouse. The animals are marketed in the Principality of Andorra to supply the national market, but also largely exported to other countries. In 2016, marketing of the meat in Andorra was a success and a growing consumer loyalty for the product has been noted.

In the distribution of livestock by parish are notably Sant Julià de Lòria, with 38.1% of the total, followed by Encamp, with 33.9% of the total. Notable variations from the previous year are the fall in the number of heads of cattle of 49.2% in the parish of La Massana and 39.1% in the parish of Escaldes-Engordany.

Tobacco cultivation is essential to farming in Andorra because it supports other farming activities which would otherwise not be viable. Initiatives have been started to reduce the current dependency on tobacco but the long process of bringing agricultural activities to maturity makes it hard to convert the sector. One example is the cooperative project, Sabors i Aromes, based on cultivating quality potatoes and aromatic plants, into which much time and resources were invested, but which had to be dropped in the end.

In the negotiations being carried out for the association agreement with the European Union, the exclusion of tobacco products is being sought, for a long enough period to enable agriculture to wean itself off its dependency on tobacco. The possibility of a 20-year transition period is being considered. It is clear that without tobacco, the current farming and livestock structures would disappear.

On the other hand, major efforts have been noted in what is seen as emerging niches, such as wine and turnips, and the effort to produce quality meat production continues. The Programme of indirect aid to local and artisanal agrifood production has been maintained, which engages about twenty producers. This initiative was started in 2014 and has developed with the elaboration of a wide variety of articles. Apart from wine, there are other products such as beer, traditional cured meats, jams, liqueurs, honey, potatoes, fir syrup and even natural cosmetics. This aid does not consist of direct subsidies but rather support and assistance in carrying out administrative formalities and help with marketing.

X. Industry

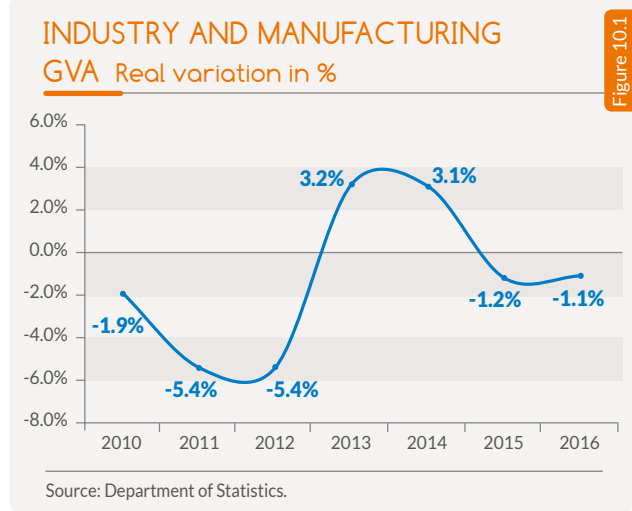
According to the official advance GDP figures, the industry and manufacturing sector, representing 4.9% of GVA in 2016, has had negative real variation rates for the last two years (-1.2% in 2015 and -1.1% in 2016), while being positive in the previous two years, as shown in diagram 10.1. Some indicators have improved in the sector as a whole, but others still show signs of weakness.

After three years in which the number of businesses increased 27.6%, to 305, the number fell in 2016 to 303. On the other hand, the number of industrial establishments rose 1.9% to reach the figure of 375.

Of the establishments existing in 2016, those with a greater presence are: products of the printing industry, graphic arts and reproduction of recorded media, with 27.2%; food production and beverage industries, with 13.6%, and wood and cork industries, except furniture, basketwork and esparto, with 11.7%.

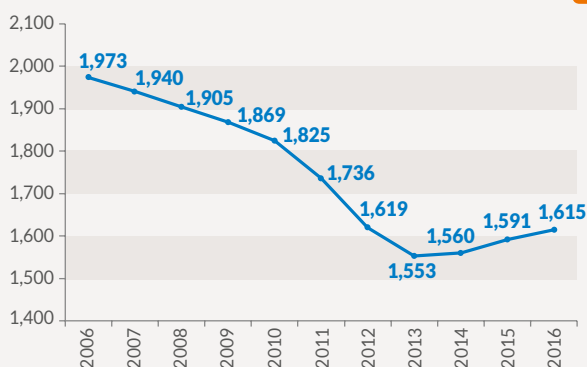
As for the distribution of businesses by number of workers, the industrial sector is clearly dominated by businesses with up to five workers, forming 68.7% of total businesses in the sector, increasing from 52.5% in 2005. Businesses with 6-10 workers represent 13.9% of the total, those with 11-25 workers represent 13.5% of the sector total and the other 3.9% are businesses with more than 25 workers.

Concerning the industrial sector, an increase in the total number of employees occurred for the third consecutive year, reaching 1,615 in 2016, a figure that is still far from the 1,973 employees in 2006. As can be seen in diagram 10.2, the number of employees fell continuously over the period 2006-2013, although in the last few years it has started a slight upward trend. In effect, the number of employees grew 1.5% in 2016, less than the 2.0% recorded in 2015. Average monthly wages rose slightly in recent years to 2,178.9 euros, a minor overall increase since of 2.2% 2012.



The trend in the industry and manufacturing sector was still negative, although the rate of fall in activity slowed since 2015.

TREND IN THE NUMBER OF EMPLOYEES IN INDUSTRY (annual average)



although in the last few years it has started a slight upward trend. In effect, the number of employees grew 1.5% in 2016, less than the 2.0% recorded in 2015. Average monthly wages rose slightly in recent years to 2,178.9 euros, a minor overall increase since of 2.2% 2012.

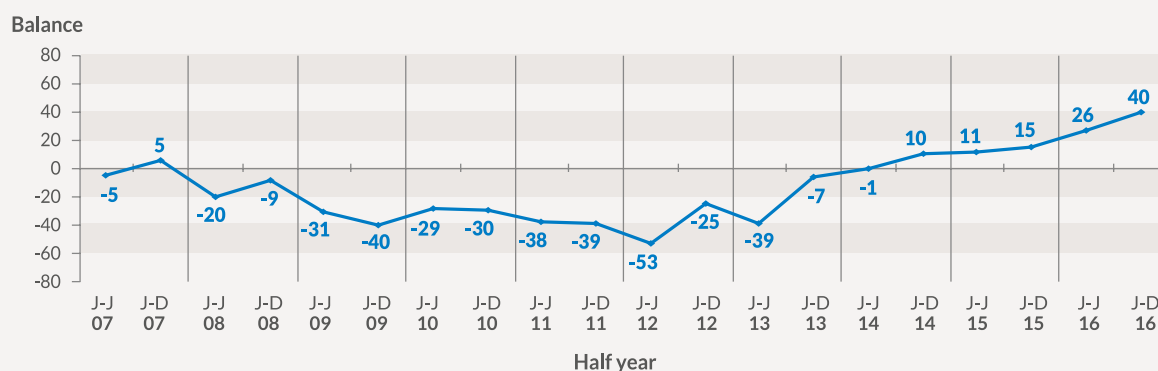
The Chamber's business opinion surveys reflect an increase in activity in the industrial sector since the second half of 2014. This improvement was marked in 2016, especially in the second half.

This improvement is mostly sustained by the overall increase in production seen by businesses, but there are still indicators that show that the recovery is still far from desired levels for the sector and the economy as a whole.

Businesses' opinions about business activity show a more favourable climate over the last thirteen years. Specifically, the percentage of businesses which consider that business activity is positive increased to 46% in the second half of 2016, and only 6% consider it bad. The improvement is notable if you consider that in the first half of 2014, 20% of businesses considered business activity to be good compared with 21% who considered it bad.

BUSINESSES' OPINION ABOUT BUSINESS ACTIVITY - INDUSTRIAL SECTOR

Figure 10.3



Balance: Difference between extreme responses (positive and negative), as a percentage.

Source: Chamber of Commerce, Industry and Services of Andorra.

Regarding the level of orders, in the second half of 2016, 29% of businesses considered them low and only 15% considered them high. Although the result of this indicator is still negative, it has improved considerably and constantly in the last few half-years. For example, in the first half of 2014, 53% of businesses considered the level of orders low and only 3% considered it high. On the other hand, the average productive capacity utilisation rate increased slightly from about 65% in the two previous years, to 67% in 2016, but still shows very low levels, confirming that demand is still lower than desired for the sector. In the industry sector, there is under-use of productive capacity which is a problem for optimising production costs. When fixed costs are not combined with optimised production, the result is an increase in unit production costs and a loss of competitiveness for the business.

Businesses' opinion of sale prices has improved slightly in comparison with the two previous years, but is still negative. Specifically, in the second half of 2016, 12% of businesses considered that prices fell in comparison with the previous half-year, compared with 7% which felt they were higher. This result is logical if you consider the global downward pressure on prices.

Employment stayed stable in the last two years, after the increase which occurred in 2014. This is due to businesses' lack of confidence in the economic recovery, due to rising competition and their difficulties in finding qualified workers.

The fact that the opinion of business activity is more favourable than the overall series of indicators in this survey can be explained in part by the clear improvement that has occurred since the worst time of the crisis, an improvement which has resulted in a marked recovery in business spirits. However, levels of activity are still very modest and lower than desired for the sector.

BUSINESSES' OPINIONS OF DEVELOPMENTS IN INDUSTRY (% of businesses)

Table 101

		2014			2015			2016		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
1. Business activity (reviewed half year)	Good	20	27	23.5	26	31	28.5	36	46	41
	Normal	59	56	57.5	60	53	56.5	54	48	51
	Bad	21	17	19	15	16	15.5	10	6	8
	Balance	-1	10	4.5	11	15	13	26	40	33
2. Orders (reviewed half year)	High	3	15	9	10	13	11.5	11	15	13
	Normal	43	45	44	50	57	53.5	60	56	58
	Low	53	40	46.5	40	30	35	29	29	29
	Balance	-50	-25	-37.5	-30	-17	-23.5	-18	-14	-16
3. Stocks of finished products (reviewed half year)	Excessive	5	10	7.5	10	6	8	9	6	7.5
	Adequate	57	34	45.5	45	46	45.5	47	44	45.5
	Insufficient	3	3	3	2	0	1	3	4	3.5
	No stocks	35	53	44	44	49	46.5	41	46	43.5
	Balance	2	7	4.5	8	6	7	6	2	4
4. Average production capacity utilisation (reviewed half year)	(as %)	64.7	65.0	64.8	64.0	65.2	64.6	67.7	66.9	67.3
5. Production (compared with same half of previous year)	Higher	25	45	35	27	32	29.5	33	45	39
	Similar	46	28	37	53	44	48.5	45	38	41.5
	Lower	29	28	28.5	20	24	22	22	17	19.5
	Balance	-4	17	6.5	7	8	7.5	11	28	19.5
6. Sales prices (compared with previous half year)	Higher	5	6	5.5	7	4	5.5	13	7	10
	Equal	65	79	72	77	78	77.5	74	81	77.5
	Lower	30	15	22.5	16	17	16.5	13	12	12.5
	Balance	-25	-9	-17	-9	-13	-11	0	-5	-2.5
7. Number of employees (compared with previous half year)	More	10	16	13	8	10	9	6	12	9
	Equal	82	81	81.5	82	83	82.5	86	75	80.5
	Less	8	3	5.5	10	7	8.5	9	13	11
	Balance	2	13	7.5	-2	3	0.5	-3	-1	-2

Source: Chamber of Commerce, Industry and Services of Andorra.

The confidence indicator regained a positive balance in the second half of 2016, after almost twelve consecutive years in negative territory.

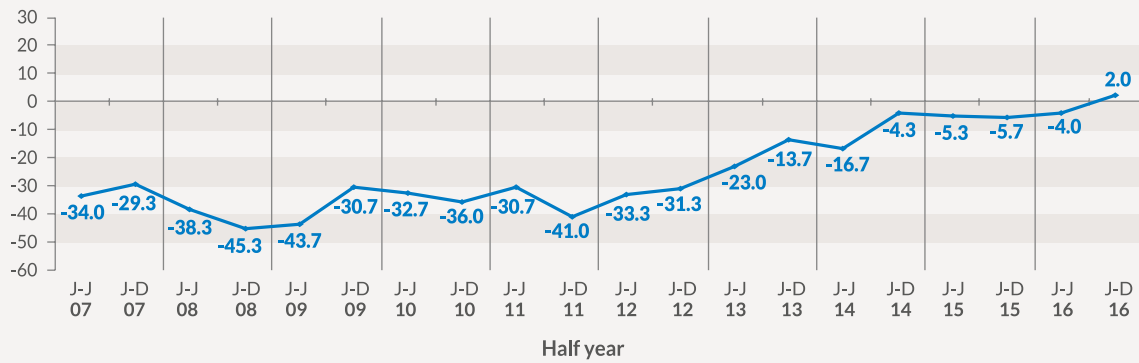
Businesses' forecasts for the first half of 2017 predict that the improvement of the last few half-years may continue over the next year. Specifically, in a comparison of the second half of 2016 with the second half of 2015, there is an increase in the number of businesses that expect

an improvement in business activity (37% in 2016 compared with 19% in 2015), those that predict an increase in orders (26% in 2016 compared with 15% in 2015) and those that believe the production trend will rise (37% in 2016 against 22% in 2015). An improvement is also seen in employment prospects, although this occurs more from a reduction in the percentages of businesses that declare that they have no intention of reducing the workforce than through an increase in businesses planning to increase it. On the other hand, businesses do not expect sales prices to increase.

To summarise the global situation of the activity, the industrial climate indicator also reflects a progressive recovery in feelings of business confidence. In particular, this index has confirmed the

CONFIDENCE INDICATOR⁽¹⁾ - INDUSTRY SECTOR

Figure 10.4



(1) Average balance of the total order book, production trends and stocks of finished products turned around. Balance: Difference between extreme responses (positive and negative), as a percentage.

Source: Chamber of Commerce, Industry and Services of Andorra.

recently-observed trend of improvement and seen an increase of 6 points against the previous half-year, to the point where it has regained a positive balance, of +2.0 points, after twenty-three consecutive half-years of minimum levels.

The percentage of businesses that state that weak demand limits the increase in activity stood at the lowest level in the last eleven years, but nevertheless, it is still the main obstacle mentioned, with a frequency of 55%, compared with the increase in competition, which was indicated by 42% of businesses. As for the other factors, the lack of qualified workforce and rising operating costs stand out, two obstacles which have increased in relevance and were already mentioned by 36% of the surveyed industries.

Box 10.1

ENERGY AND ENVIRONMENT

52% of national energy demand relates to the transport sector, while the other part is divided between electricity consumption (24%), heating fuel consumption (22%) and thermal water (2%).

National dependency is 94.3% of the national demand, as imports of fossil fuels represent 74.2% of the national energy demand, and electricity imports, 20.1%.

47% of the electricity comes from Spain and 36% from France. The rest (17%) is nationally-produced electricity. National production is mostly hydroelectric power (84.5%). Energy from waste represents 15.1% of the total, and the other 0.4% is solar power.

As for the supply that meets this demand, in 2016 there was the FEDA (Forces Elèctriques d'Andorra) plant, the Waste Treatment Centre and 32 solar-power installations on buildings.

In December 2016, the first national cogeneration plant started to operate in Soldeu, inaugurated in February 2017. Two objectives were met by this new infrastructure: electricity production and heat production for distribution through an urban network in the town of Soldeu and its surroundings. This plant represents the start of a new national energy policy with the objective of increasing own production and moving towards a more sustainable energy model that is not as dependent on foreign sources.

The new cogeneration plant and the installation of the network of charging points for electric vehicles were FEDA's two core focuses of action in 2016.

If we analyse energy intensity (EI), which is defined as the relation between a country's energy consumption (E) and gross domestic product (GDP), we can see that since 2007, Andorra's EI has remained relatively

stable, between 98 and 116 toe/€, figures that are comparable to the 118-122 toe/€ of the Eurozone.

According to information published by the Department of the Environment regarding selective collection, surface water and air quality:

In 2016, 49% of the fractions of paper and cardboard, glass and packaging have been collected selectively and sent for recycling. This percentage is similar to the previous year.

At monitoring stations, it has been seen that 85% of surface water quality is excellent or good (in 2015, this percentage was close to 80%).

The air quality surveillance network monitors issue levels. A slight improvement can be seen in relation to the previous year, as it was excellent or good for 92% of the time.

80% of the network of monitoring stations meet the quality targets set by the noise registry, although this percentage was around 90% during the period 2014-2015.

The biological quality of the rivers was considered excellent or good in 52% of cases. This has fallen constantly since 2013 due to the autumn drought, and the low water level in rivers.

XI. Construction

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In 2016, the construction sector continued the trend towards recovery that began last year, although this is very slow and levels of activity are still very low. In 2015, construction GVA saw a variation in real terms of +0.2%, an increase which, although modest, represented a shift towards stability after a period of eight years of uninterrupted steep falls in activity. In 2016, according to the advance GDP published by the Department of Statistics, GVA saw a positive real variation of 1.2%, one point more than in 2015, confirming the trend of gentle improvement in construction activities. As a result, the construction percentage of total GVA stabilised at 5.8%, a figure that contrasts with the high of 12.6% that it reached in 2006. Along the same line, it can be seen that in 2016 employment in the construction sector only represents 41% of what it was in 2006, and imports of building materials are still only 37% of the figure before the crisis.

The construction sector has continued the path of recovery it started last year, but at a very slow rate.

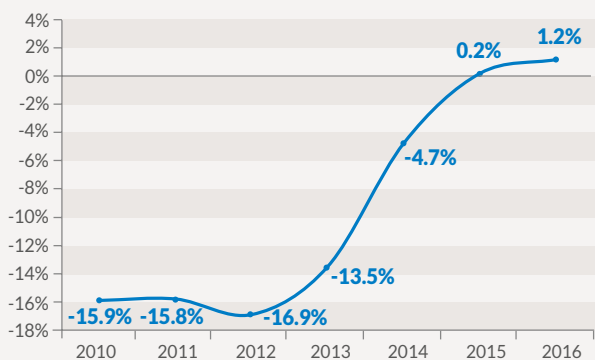
Since 2015, sector figures are positive and confirm a slow, progressive recovery in activity. A first set of indicators of the trend in the sector refers to the number of business establishments, which went from 808 in 2015 to 830 in 2016. These figures indicate a net creation of 22 establishments, greater than in 2015, when it was 13 establishments. Moreover, the number of businesses in 2016 was 638, representing an increase of 1.9% against the previous year. As for the number of businesses per number of employees, 71.2% of businesses have five or less workers, 24.9% have between 6 and 25 employees and only the other 3.9% surpass 25 workers.

Sector employment increased 2.1% and reached 2,816 employees. After eight years of continuous falls in the number of employees in the sector, the trend reversed in 2015, with employees growing 0.9%. However, as we mentioned, the level of employment is still far from that of 2006, as the number of employees in that year (6,788) easily doubled the current figure.

CONSTRUCTION SECTOR GVA

Real variation in %

Figure 11.1

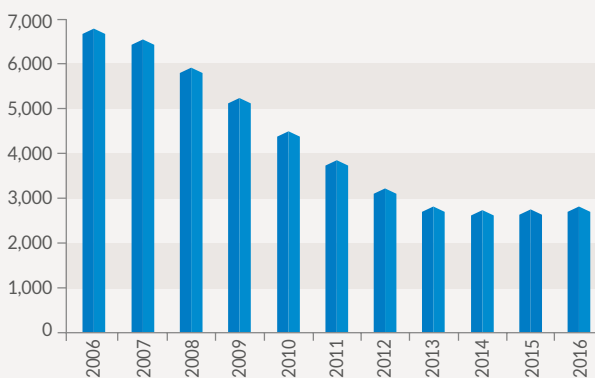


Source: Department of Statistics.

To put the job creation data into perspective, table 11.1 shows the trend in the sector's percentage of the whole Andorran economy in relation to the number of employees. In the period 2006-2013, the downward trend is very clear: the construction workers' percentage of total employees in Andorra falls to half, from 16% to 8%. Developments over the last three years break the downward trend and clearly show stabilisation of this indicator at around 7.7%.

DEVELOPMENTS IN THE NUMBER OF EMPLOYEES IN THE CONSTRUCTION SECTOR

Figure 11.2



Source: CASS / Department of Statistics.

The crisis also had an impact on the trend in wages, although the downturn in average wages in the sector was not notable until 2013, when it fell to €1,915.37, having surpassed €2,000 in 2009. In 2015, it continued to fall at a slower rate, to €1,880.77. In 2016, after four consecutive years of falls, the average wage stood at €1,908.19, representing an increase of 1.5% against the previous year.

Electricity consumption in construction shrank 1.6%, after increasing 6.9% in 2015, the first increase in nine years.

As construction projects generally have a relatively long completion period, it is important to have indicators that detect the beginning of the processes of setting up and operating a project. So, in 2016, 35 new-build permits were granted, 20.7% more than in 2015, and the authorised surface area was

41,677 square metres, representing a drop of 8.1% against the previous year. It should be remembered that in 2015 there was a significant increase in square metres of authorised surface area, of 128%, a rate of increase that broke with three consecutive years of decline.

In 2016, Andorra la Vella, La Massana and Escaldes-Engordany stand out as the parishes with most authorised area for building. By type of building, 44.8% of the authorised area relates to houses, 29.0% are multi-family housing and the other 26.3% are other buildings, such as offices, stores and hotels.

CONSTRUCTION WORKERS AS A PERCENTAGE OF TOTAL EMPLOYEES IN ANDORRA

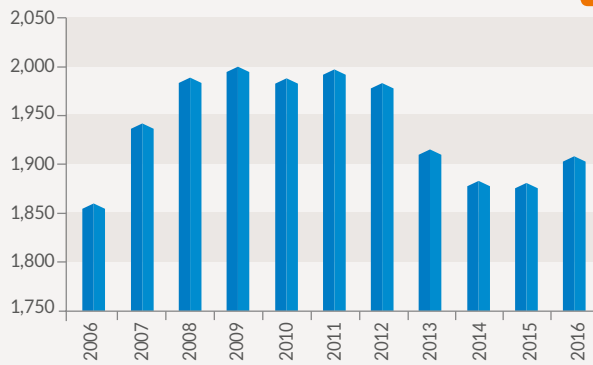
Table 11.1

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Construction employees: % of total	16.0%	15.5%	14.5%	13.2%	11.6%	10.3%	9.0%	8.0%	7.7%	7.7%	7.7%

Source: CASS / Department of Statistics.

TREND IN AVERAGE CONSTRUCTION WAGES

Figure 11.3



Source: CASS / Department of Statistics.

On the other hand, according to data from the Andorran Official Architects Association, 514 projects were authorised in 2016, 85 more than in the previous year. 60.8% of the authorised m² relate to new builds, and the other part to refurbishments (28.7%), extensions (1.7%) and demolitions (8.8%).

The data over the next few financial years needs observing to see if they confirm the trend towards growth in projects with an average smaller surface area per project. The fact that in 2016, the most significant increase in authorised surface area was in single-family houses (with an increase of close to 10,000 m²) at the expense of multi-family housing (with a

drop of nearly 20,000 m² against 2015) may be the start of this trend.

Another relevant sector indicator are imports of building materials. Diagram 11.4 shows the clearly falling trend in imports for the period 2007-2012. From 2014, a slight recovery began, which resulted in two years of consecutive increases in imports (2.5% in 2014 and 7.2% in 2015). In 2016, the trend in imports of building materials was not as favourable, as it saw an interannual fall of 1.6%.

The fall in public investment contributed to the lack of momentum in the construction sector. In this financial year, both the government and the communes made lower real investments than in 2015. Specifically, real investments settled by the Government in 2016 rose to 44.5 million euros, a figure that represents a drop of 3.2% compared with the investment made in the previous year. For their part, communes' real investments fell steeply, by 51.5%, from 18.5 million euros in 2015 to 9.0 million euros in 2016.

The rate of progress in activity was still modest and levels were very low.

The Chamber's situation surveys show that construction is the sector that follows the weakest trend, despite showing clear signs of improvement and then more stable behaviour.

In 2016, the valuations of business activity were more favourable than in the previous two years and show a progressive recovery in business confidence.

AUTHORISED SURFACE AREA FOR BUILDING BY PARISH (Square metres)

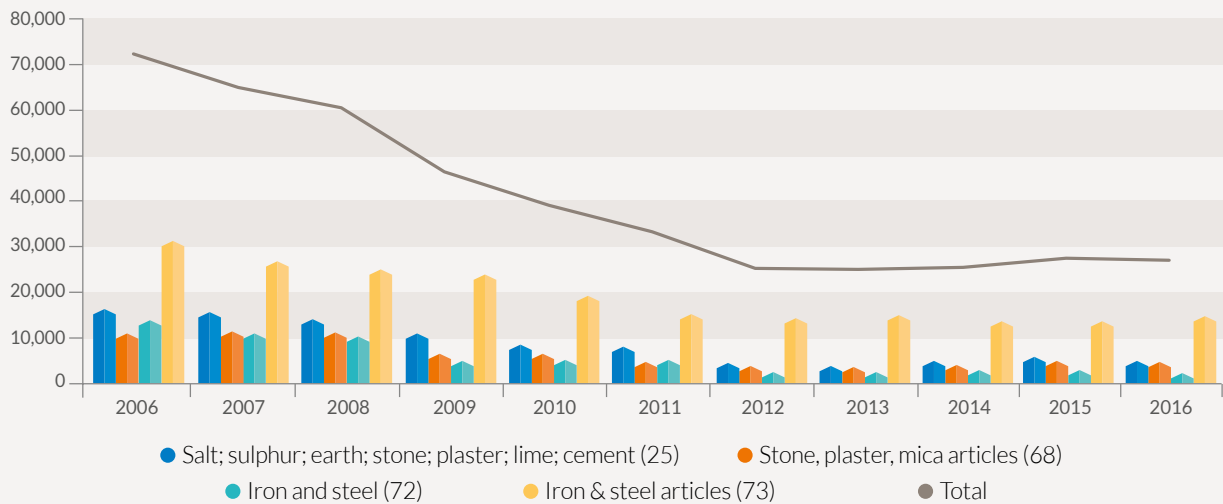
Table 11.2

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Canillo	29,291	12,059	21,002	2,656	6,316	5,040	1,250	1,842	3,704	169	1,605
Encamp	6,173	4,975	14,901	11,016	18,566	18,816	1,134	4,219	2,214	8,563	1,186
Ordino	10,682	3,090	15,059	19,075	2,363	3,055	29,232	2,517	1,486	2,560	907
La Massana	5,699	34,567	9,122	8,512	5,021	6,570	7,121	3,592	2,600	647	11,132
Andorra la Vella	4,943	4,314	10,071	15,893	2,244	2,324	2,293	21,163	1,702	5,410	15,610
Sant Julià de Lòria	26,941	7,183	14,784	22,990	3,113	34,865	11,692	4,270	3,015	21,847	2,607
Escaldes-Engordany	27,734	12,497	19,471	28,098	18,986	2,184	760	14,810	5,171	6,155	8,630
Total	111,463	78,685	104,410	108,241	56,610	72,853	53,482	52,413	19,892	45,350	41,677

Source: Commune administrations / Department of Statistics.

IMPORTS OF BUILDING MATERIALS (Thousands of euros)

Figure 11.4



Source: Own preparation based on data from the Department of Tax and Frontiers.

In the second half of 2016, executed works saw a slight increase compared with the same months of the previous year, although in general, they remained at very low levels. The data indicate the weak dynamic of public works and also the scarce demand for new residential building. For its part, the volume of contracted works recovered a little in relation to the previous year, but still shows rather unsatisfactory levels.

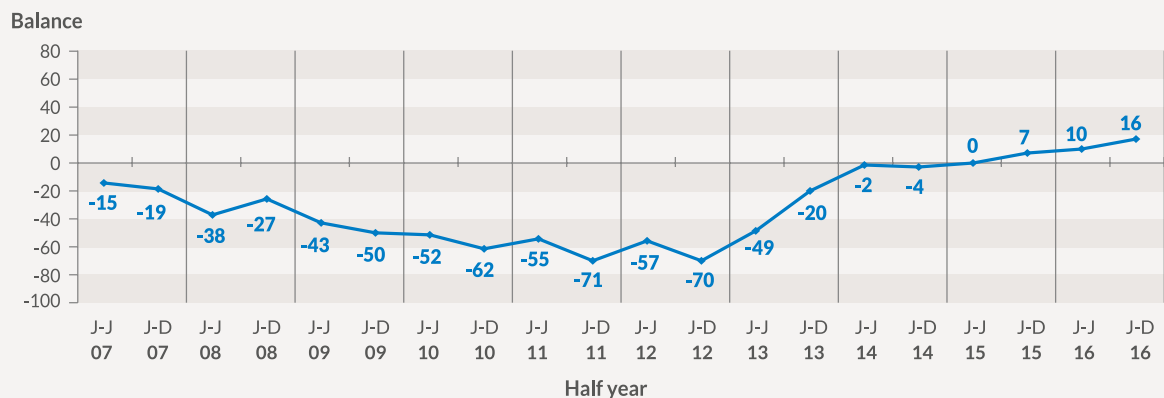
By type of works, the volume of contracts continued to show a very depressing trend in the branch of housing construction, with activity remaining at a low. This indicates that activities relating to remodelling and refurbishment are not taking off as expected, a sign that the final home user is still struggling and that public remodelling policies, despite being an important stimulus to the sector, do not manage propel the situation. As for the other branches – non-residential building and civil works – the rate of contracts also remained quite low, continuing the trend of previous years.

The prospects for businesses for the first half of 2017 do not show any substantial change and on the whole, continue to indicate a certain generalised lack of confidence in achieving a sustained recovery in activity; despite the sector showing some signs of improvement, many difficulties can still be seen that impede a clear trend to recovery.

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BUSINESSES' OPINION ABOUT BUSINESS ACTIVITY - CONSTRUCTION SECTOR

Figure 11.5



Balance: Difference between extreme responses (positive and negative), as a percentage.

Source: Chamber of Commerce, Industry and Services of Andorra.

BUSINESSES' OPINIONS ABOUT DEVELOPMENTS IN THE CONSTRUCTION SECTOR (% of businesses)

Table 113

		2014			2015			2016		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
1. Business activity (reviewed half year)	Good	20	19	19.5	15	24	19.5	31	28	29.5
	Normal	59	58	58.5	70	59	64.5	49	60	54.5
	Bad	22	23	22.5	15	17	16	21	12	16.5
	Balance	-2	-4	-3	0	7	3.5	10	16	13
2. Volume of executed works (compared with same half of previous year)	Higher	28	42	35	32	29	30.5	38	45	41.5
	Equal	41	26	33.5	42	36	39	26	26	26
	Lower	31	33	32	26	36	31	36	29	32.5
	Balance	-3	9	3	6	-7	-0.5	2	16	9
3. Contract unit prices (compared with previous half year)	Higher	5	0	2.5	0	2	1	0	2	1
	Equal	68	58	63	68	74	71	83	79	81
	Lower	27	42	34.5	33	24	28.5	18	19	18.5
	Balance	-22	-42	-32	-33	-22	-27.5	-18	-17	-17.5
4. Number of employees (compared with previous half year)	More	24	9	16.5	5	15	10	15	10	12.5
	Same	59	72	65.5	82	75	78.5	69	71	70
	Less	17	19	18	13	10	11.5	15	19	17
	Balance	7	-10	-1.5	-8	5	-1.5	0	-9	-4.5

Source: Chamber of Commerce, Industry and Services of Andorra.

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The excess supply of buildings pending sale and, in relation to demand, investors' low confidence and more restrictive conditions on access to credit are not helping to reactivate activity in the short term.

Among the factors that limit business activity, weak demand (cited by 61% of those surveyed) remains the main obstacle to improvement in activity, followed closely by increased competition, which rose to 58%. On the other hand, businesses also point to the lack of qualified workforce, a factor that is gaining importance and is already as worrying as rising operating costs, indicated by 49% of constructors.

This factor is the result of the large number of specialised workers in this sector who left the country during the crisis and do not plan to return until growth is effectively consolidated.

XII. Services

The service sector is the most important, central nucleus of the Andorran economy, concentrating 88.8% of the economy's total GVA and 87.4% of employees. The latter percentage continued at the same level as in 2015 and is

the highest in the available historical series. The major importance of this sector means that its trends clearly determine the evolution of annual GDP in the Andorran economy, so any variations are reflected systematically in the main macroeconomic magnitudes. Following the trend in 2015, the services sector continued to be the driving force of the Andorran economy, in a context where the improvement in tourism favoured a recovery in services related most directly to tourism – commerce,

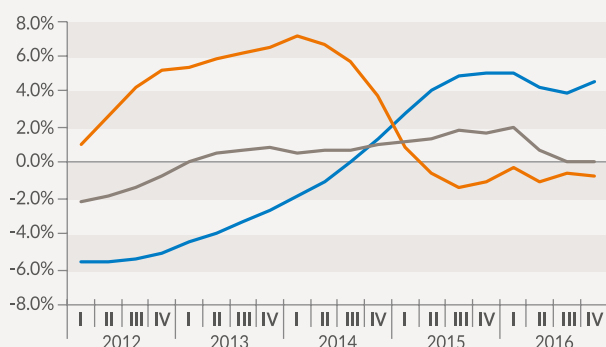
The service sector concentrates 88.8% of the economy's total GVA and 87.4% of employees.

hotels & catering, etc. Specifically, in 2016, the service sector grew an annual 1.4%, the same increase as in 2015, although the annual balance varies according to subsector:

- Commerce, hotels & catering, transport, information and communications saw a notable increase in real GVA, by 4.4%, two tenths more than in 2015;
- The subsector of Public administration, education, health, social and personal services saw real growth of 0.7%, continuing the tone of moderate increase in the last three years;
- In contrast, the subsector of Financial, real estate, professional and technical activities still had negative annual variation rates, with a drop in real GVA of 0.7%, a slightly higher rate of fall than in the previous year (-0.5%).

QUARTERLY TRENDS IN GROSS VALUE ADDED - SERVICE SECTOR Real variation (%)

Figure 12.1



- Commerce, Hotels & catering, Transport, Information & Communications
- Financial, Real estate, Professional & Technical
- Public admin., Education, Health, Social and Personal services

Source: Department of Statistics.

In December 2016, there were 6,878 businesses in the services sector, 5.9% more than in the previous year. If we observe the bulk of the business network, disaggregated by subsector, we can see how commerce and vehicle repairs concentrates 28.6% of the total volume (with 1,964 businesses and growth of 3.8%), followed by real estate activities and business services, with a percentage of 27.9% (1,918 businesses with very high growth of 13.2%) and, in third place, hotels and catering, with 12.4%, 852 businesses and a drop of 0.4% against 2015.

If we compare the current number of service sector businesses compared with those that existed in 2007, considered the last year before the crisis, we can see that the number of businesses

NUMBER OF BUSINESSES IN THE SERVICE SECTOR *

Table 12.1

	2007	2015	2016	% total 2016	Var. 16/15
Commerce and motor vehicle repairs (etc.)	1,592	1,892	1,964	28.6%	3.8%
Hotels & catering	746	855	852	12.4%	-0.4%
Transport, storage & communications	230	281	287	4.2%	2.1%
Financial system	80	108	114	1.7%	5.6%
Real estate and rental activities; business services	862	1,695	1,918	27.9%	13.2%
Public administration, defence & compulsory social security	36	36	35	0.5%	-2.8%
Education	48	80	94	1.4%	17.5%
Health & veterinary activities, social services	246	397	448	6.5%	12.8%
Other social act. and community services; personal services	396	587	610	8.9%	3.9%
Extraterritorial bodies	7	7	6	0.1%	-14.3%
Special regimes	-	1	1	0.0%	0.0%
Domestic work for the community	550	558	549	8.0%	-1.6%
Total	4,793	6,497	6,878	100%	5.9%

*Not including households employing domestic staff and voluntary declarations of no activity.
Note: Data for December of the relevant year.

Source: CASS.

has grown significantly. Overall, it appears that no significant changes occurred until 2013 but then, a major interannual increase in the number of businesses occurred.

Regarding the size of these businesses, 81.2% have less than 6 workers and, therefore, microbusinesses form a large part of Andorra's business structure. On the other hand, compared with 2015, the most important variation is in enterprises of 26-100 workers (+9.5%) and those with 1-5 employees (+6.4%).

If we analyse the growth in the number of businesses by number of employees from the start of the crisis, the greatest dynamism in job creation is in microbusinesses, with an average interannual growth rate of 5.1%. Other businesses saw average interannual growth below 1%, except those considered to be large (more than 100 workers), which saw a rate of increase of 1.9%.

As for employment in the sector, in 2016, employees increased 1.9%, 0.2 points more in than the previous year. The total number of employees in the services sector reached 32,002, of which 8,754 are working in the commerce sector, 4,702 in hotels & catering, 4,571 in real estate activities and business services and 4,317 in public administration. Globally, these four subsectors concentrate 69.8% of total employees in the services sector: commerce holds 27.4%; hotels & catering 14.7%; real estate activities 14.3%, and public administration 13.5%.

In 2016, the most notable growth in employment was seen in health activities (6.6%), education (6%); real estate activities and business services (4.9%), and transport, storage and communications (4.3%). In contrast, the number of employees saw decreases in public administration (-2.0%) and in the financial system (-0.7%).

NUMBER OF BUSINESSES BY NUMBER OF EMPLOYEES IN THE SERVICE SECTOR *

Table 12.2

	2007	2015	2016	% total 2016	Var. 16/15
1 - 5	3,573	5,245	5,583	81.2%	6.4%
6 - 10	591	620	630	9.2%	1.6%
11 - 25	397	398	414	6.0%	4.0%
26 - 100	185	179	196	2.8%	9.5%
> 100	47	55	55	0.8%	0.0%
Total	4,793	6,497	6,878	100%	5.9%

*Not including households employing domestic staff and voluntary declarations of no activity.

Note: Data for December of the relevant year.

Source: CASS.

NUMBER OF EMPLOYEES IN THE SERVICE SECTOR (Annual average)

Table 12.3

	2007	2015	2016	% total 2016	Var. 16/15
Commerce and motor vehicle repairs (etc.)	10,950	8,667	8,754	27.4%	1.0%
Hotels & catering	5,414	4,553	4,702	14.7%	3.3%
Transport, storage & communications	1,245	1,056	1,102	3.4%	4.3%
Financial system	1,611	1,960	1,947	6.1%	-0.7%
Real estate and rental activities; business services	4,188	4,358	4,571	14.3%	4.9%
Public administration, defence & compulsory social security	4,145	4,405	4,317	13.5%	-2.0%
Education	555	552	585	1.8%	6.0%
Health & veterinary activities, social services	1,436	1,807	1,926	6.0%	6.6%
Other social act. and community services; personal services	2,432	2,655	2,733	8.5%	2.9%
Households employing domestic staff	1,357	1,162	1,138	3.6%	-2.1%
Extraterritorial bodies	24	19	17	0.1%	-11.8%
Domestic work for the community	216	221	209	0.7%	-5.2%
TOTAL	33,574	31,415	32,002	100%	1.9%

Source: CASS / Department of Statistics.

Despite the increase in the number of employees seen in the last three years, it has still not recovered the numbers in 2007, before the crisis, when it reached 33,574, 1,572 more than in 2016. It is interesting to see that at the same time as the sector was losing employees, a notable increase in the number of microbusinesses occurred. It is very likely that part of the destruction of jobs in this sector led to the creation of small businesses.

Monthly wages for the whole service sector grew 4.7%, an increase that compensates the decrease of 3.4% which occurred in 2015. The subsectors where this increase was most notable are the financial sector (22.5%), real estate activities and business services (3.4%), other social activities and community services (3.1%) and public administration (2.9%).

The calculation of the average wages in the financial sector relating to 2016 is probably free of the distortions that appeared in 2014 (with an increase of 19.5%) and 2015 (with a decrease of 23.9%) linked to the introduction of the IRPF. Average interannual growth from 2013 to 2016 was 6.0%, a more realistic percentage than the nominal increases and decreases produced in the last three years.

The increase in the average wage in public administration is the result of normalisation of staff pay after several years of a policy of freezing the highest wages and triennis (seniority payments).

1. Commerce

Commerce is a key sector within the national economy, with a percentage of GVA at about 16%. Andorra is a shopping destination; proof of this is that shopping is the main reason for visiting the country. So, sales in the sector depend to a large extent on the influx of foreign visitors, which in 2016 saw an increase for the third consecutive year and, moreover, a little stronger than the previous year. Specifically, the total number of non-resident visitors increased an annual 2.6%, compared with 0.7% in 2015.

The main indicators for the commercial sector confirm the signs of recovery which began to emerge in 2015.

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In 2016, the main indicators of the commercial sector confirm the symptoms of recovery which began to be seen in 2015, although the improvement in the situation is still very slow and weak.

So, sector employment grew 1.0%, after nine years of continuous falls and one year (2015) of zero growth. Average wages grew 1.6%, compared with 0.5% growth in 2015. The number of establishments grew 2.9% (81 new establishments), divided between three branches: 14 new establishments in motor vehicle sales, maintenance and repairs; 62 new wholesalers, and 5 more retail establishments. Despite the increase in the number of establishments, electricity consumption fell 0.7%, after modest growth in 2015 (0.6%).

On the other hand, imports of goods, a good indicator of commercial activity, also showed generally favourable behaviour. Overall, imports grew 4.9% compared with 2015, but if we exclude construction materials (-1.6%), tobacco (+0.7%) and fuels (-21.6%), the other articles actually destined for commerce grew 8.0%, compared with 1.9% in the previous year.

After the first analysis of the strategic shopping tourism plan in March 2016, where some failings and some strong points of the commercial sector were mentioned, on 8 November 2016, a second phase of the plan was presented to the commercial and business sector of Andorra, focussed on strategy and actions to be carried out in the short, medium and long term, to position Andorra as a flagship shopping destination.

As a result of this study, 111 actions were proposed, 59 of which were on a national scale and 52 on a sectoral scale, involving both the public and private sector. The study established eleven priority actions:

1. To carry out the series of projects aimed at tourism and leisure, currently under study: Green Infrastructures Plan, Thyssen Museum (opened in March 2017), The Cloud, Multifunctional area, Casino, Wild water park.
2. To improve border access, optimise aerial transport.
3. To carry out a global remodelling plan of the town and entrance to the town of Pas de la Casa.
4. To carry out town planning for the Meritxell/Vivand sector.
5. To create more prestigious events, mostly cultural.
6. To develop the quality of the supply at Pas de la Casa to complete the “One Day Shopping” position by installing outlet stores.
7. To attract new brands / propose commercial areas that meet their expectations.
8. To implement a loyalty programme for the sector.
9. To focus communication on the shopping experience in Andorra.
10. To train staff and shop owners to improve the quality of their service.
11. To hold more top-level sports events.

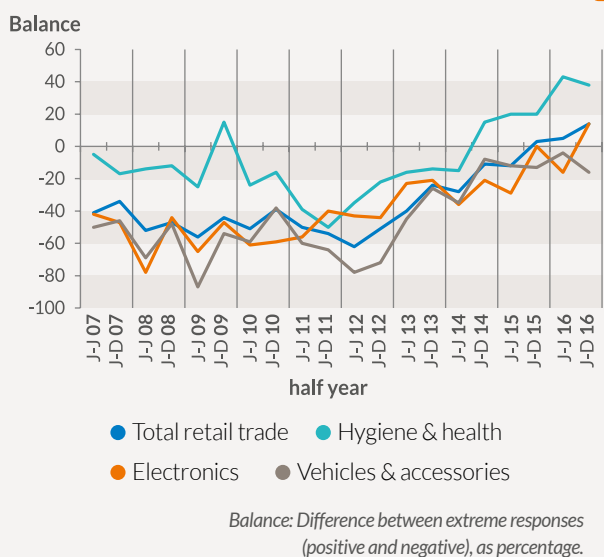
The Chamber’s situation survey also confirms a slight improvement in the commercial situation over 2016, as it shows clearer signs of stabilisation of levels of activity, a trend that breaks with the tone of strong cumulative decline since 2005. However, this impetus in activity has been very weak and mostly appears because the sector starts from very low figures, rather than a clear reactivation in private consumption, which still appears undynamic.

The Chamber’s situation survey also confirms a faint improvement in the commercial situation throughout 2016.

According to the results of the second half of 2016, assessments of business activity showed a positive balance for the third consecutive half-year and, moreover, reflect a moderate increase in the level of optimism compared with the previous year.

BUSINESSES’ OPINION ABOUT BUSINESS ACTIVITY - RETAIL TRADE

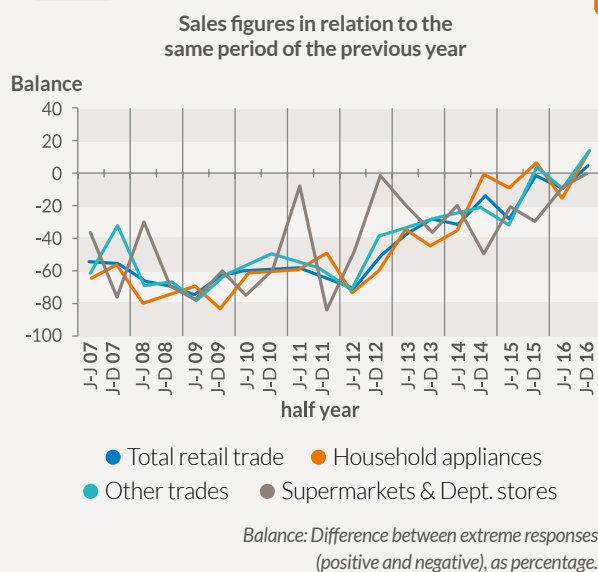
Figure 12.2



Source: Chamber of Commerce, Industry and Services of Andorra.

BUSINESSES’ OPINION ABOUT SALES FIGURES - RETAIL TRADE

Figure 12.3



Source: Chamber of Commerce, Industry and Services of Andorra.

BUSINESSES' OPINIONS OF THE TREND IN THE RETAIL TRADE (% of businesses)

Table 12.4

I. Business activity (reviewed half year)		2014			2015			2016		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
Total retail trade	Good	12	17	14.5	16	25	20.5	27	32	29.5
	Normal	47	56	51.5	56	53	54.5	51	51	51
	Bad	40	28	34	28	22	25	22	18	20
	Balance	-28	-11	-19.5	-12	3	-4.5	5	14	9.5
Food	Good	12	19	15.5	12	29	20.5	26	29	27.5
	Normal	49	59	54	58	46	52	62	59	60.5
	Bad	39	22	30.5	30	26	28	12	12	12
	Balance	-27	-3	-15	-18	3	-7.5	14	17	15.5
Clothing & footwear	Good	3	12	7.5	9	16	12.5	23	26	24.5
	Normal	49	50	49.5	59	54	56.5	46	54	50
	Bad	49	38	43.5	32	30	31	31	20	25.5
	Balance	-46	-26	-36	-23	-14	-18.5	-8	6	-1
Household appliances	Good	19	17	18	15	26	20.5	19	41	30
	Normal	32	53	42.5	50	61	55.5	50	41	45.5
	Bad	48	30	39	35	13	24	31	18	24.5
	Balance	-29	-13	-21	-20	13	-3.5	-12	23	5.5
Hygiene & health	Good	11	25	18	20	35	27.5	43	48	45.5
	Normal	63	65	64	80	50	65	57	43	50
	Bad	26	10	18	0	15	7.5	0	10	5
	Balance	-15	15	0	20	20	20	43	38	40.5
Electronics	Good	7	29	18	0	14	7	15	27	21
	Normal	50	21	35.5	71	71	71	54	60	57
	Bad	43	50	46.5	29	14	21.5	31	13	22
	Balance	-36	-21	-28.5	-29	0	-14.5	-16	14	-1
Vehicles & accessories	Good	17	15	16	16	13	14.5	20	19	19.5
	Normal	30	62	46	56	61	58.5	56	46	51
	Bad	52	23	37.5	28	26	27	24	35	29.5
	Balance	-35	-8	-21.5	-12	-13	-12.5	-4	-16	-10
Other trades	Good	16	15	15.5	22	30	26	33	32	32.5
	Normal	50	62	56	49	51	50	49	54	51.5
	Bad	34	23	28.5	29	19	24	18	14	16
	Balance	-18	-8	-13	-7	11	2	15	18	16.5
Supermarkets & Dept. stores	Good	0	10	5	20	30	25	25	30	27.5
	Normal	70	40	55	50	20	35	33	40	36.5
	Bad	30	50	40	30	50	40	42	30	36
	Balance	-30	-40	-35	-10	-20	-15	-17	0	-8.5

Source: Chamber of Commerce, Industry and Services of Andorra.

By subsectors, positive opinions of business activity predominated in most branches. However, the more optimistic opinions in the branch of household appliances and, in particular, the subsector of hygiene and health stood out, showing the most enthusiastic assessments for the whole of commerce for the third consecutive year. Equally notable is the more favourable behaviour of business activity in the electronics branch and the signs of improvement in the segment of clothing and footwear, a subsector which recently presented the most disappointing levels for the whole of commerce and which, this year, saw an appreciable recovery in activity, despite being still at unsatisfactory levels. The only branches that did not share this more positive trend were vehicles and accessories, which showed a certain slowdown in the rate of activity, and supermarkets and department stores, which displayed a trend of stability.

For the whole of commerce, in the second half of 2016, the sales figures saw a small interannual increase in relation to the same period in the previous year, for the first time since the start of the crisis, although sales in most establishments were still at very low levels. Specifically, 36% of shops saw an increase in levels of invoicing, compared with 31% of establishments which indicated an interannual decrease in sales.

BUSINESSES' OPINIONS OF THE TREND IN THE RETAIL TRADE (% of businesses)

Table 12.5

2. Sales figures (Reviewed half-year compared with same half of previous year)		2014			2015			2016		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
Total retail trade	Higher	16	27	21.5	17	30	23.5	24	36	30
	Similar	36	33	34.5	37	39	38	41	33	37
	Lower	48	40	44	46	31	38.5	35	31	33
	Balance	-32	-13	-22.5	-29	-1	-15	-11	5	-3
Food	Higher	22	36	29	13	29	21	29	30	29.5
	Similar	19	29	24	35	38	36.5	35	30	32.5
	Lower	59	36	47.5	52	32	42	35	41	38
	Balance	-37	0	-18.5	-39	-3	-21	-6	-11	-8.5
Clothing & footwear	Higher	11	22	16.5	13	26	19.5	21	38	29.5
	Similar	28	31	29.5	22	49	35.5	35	34	34.5
	Lower	61	47	54	66	26	46	44	28	36
	Balance	-50	-25	-37.5	-53	0	-26.5	-23	10	-6.5
Household appliances	Higher	17	25	21	25	27	26	13	36	24.5
	Similar	30	50	40	41	53	47	58	39	48.5
	Lower	53	25	39	34	20	27	29	24	26.5
	Balance	-36	0	-18	-9	7	-1	-16	12	-2
Hygiene & health	Higher	6	29	17.5	25	45	35	48	35	41.5
	Similar	61	41	51	55	35	45	48	30	39
	Lower	33	29	31	20	20	20	5	35	20
	Balance	-27	0	-13.5	5	25	15	43	0	21.5
Electronics	Higher	7	29	18	0	29	14.5	23	36	29.5
	Similar	57	7	32	36	21	28.5	23	29	26
	Lower	36	64	50	64	50	57	54	36	45
	Balance	-29	-35	-32	-64	-21	-42.5	-31	0	-15.5
Vehicles & accessories	Higher	23	36	29.5	23	23	23	17	30	23.5
	Similar	36	28	32	50	23	36.5	42	35	38.5
	Lower	41	36	38.5	27	55	41	42	35	38.5
	Balance	-18	0	-9	-4	-32	-18	-25	-5	-15
Other trades	Higher	21	23	22	17	31	24	23	41	32
	Similar	35	33	34	33	43	38	44	32	38
	Lower	44	44	44	50	26	38	33	27	30
	Balance	-23	-21	-22	-33	5	-14	-10	14	2
Supermarkets & Dept. stores	Higher	10	0	5	20	30	25	36	36	36
	Similar	60	50	55	40	10	25	18	27	22.5
	Lower	30	50	40	40	60	50	46	36	41
	Balance	-20	-50	-35	-20	-30	-25	-10	0	-5

Source: Chamber of Commerce, Industry and Services of Andorra.

By type of commerce, a slight recovery can be seen in sales in the branches of household appliances, clothing and footwear and in establishments in the section "other trades". On the other hand, the only branches which still had negative trends in sales, although with a very moderate profile, were the branches of food and vehicles and accessories. The rest of the subsectors, in general terms, managed to maintain a level of invoicing very similar to one year before.

The volume of stocks was mainly deemed excessive in the segments of clothing and footwear and hygiene and health, while in the other branches, stocks were considered to be rather low.

The number of employees maintained a tone of general stability in most trades and sales prices continued to fall, if in a less marked way, except for supermarkets and department stores and the section "other trades", in which prices rose slightly.

Businesses' prospects for the first half of 2017 show a generally more positive tone but do not indicate yet a background improvement in commercial activity, in a context, moreover, in which the

recovery in consumption is still very limited by the slow improvement in the labour market and the loss of household purchasing power.

Retailers trust in a more favourable trend in business activity and also expect the sales figures to continue to recover very slowly, although still at very low levels. This slight impetus to activity will result in a rising trend in sales prices and a moderate increase in the number of workers in the sector.

Among the obstacles impeding the increase in activity, weak demand (mentioned by 54% of commerce) remains the main limitation, followed closely by the increase in competition (50%), which has risen one place, higher than the increase in operating costs (45%), and loss of attractiveness in the area (42%).

2. Financial system

The financial system is one of the main pillars of the Andorran economy, consisting principally of the banking sector and the insurance sector, with about 21% of total GVA, so its result greatly influences the development of the whole economy. Over the long years of crisis, it was the financial sector that reacted first and more strongly and therefore contributed, decisively, to the change in trend that the economy saw from the second half of 2013. In 2015, financial and insurance activities suffered a decrease in nominal GVA of 3.5%, which contrasted with the approximate increases of 10% which had been seen in the three previous years. This downturn in activity occurred in a particularly difficult context, due to the Andorran National Institute of Finance (INAF) putting Banca Privada d'Andorra into administration, which was a hard test for the sector to withstand.

Despite these difficulties, the Andorran financial system confirmed its soundness throughout 2016. On 31 December, there were 114 businesses in the financial sector, 5.6% more than in 2015, and 170 establishments, four more than in the previous year. The number of employees for the financial sector as a whole saw a very moderate decline of 0.7%, giving a figure close to 1,950 employees. In contrast, average wages in this sector, which are the highest for all the sectors of the Andorran economy, saw a major increase (22.5%), which offsets the fall of a similar size in 2015 (-23.9%). Equally, we should remember that wage variations in 2014 and 2015 were influenced partly by the entry into force of the IRPF tax in 2015, motivating a one-off advance of tax incentives in some businesses which, logically, distorted the comparison.

The nucleus of the Andorran financial system is the banking system, made up of a total of five banking groups: Andbank, MoraBanc, Crèdit Andorrà, BancSabadell d'Andorra and Vall Banc.

In 2016, the process ended that had started in the previous year, relating to the note from the US administrative authority Financial Crimes Enforcement Network (FinCEN), which led to Banca Privada d'Andorra (BPA) being put into administration by the INAF, and the subsequent creation of a new entity by the National Agency for the Resolution of Banking Entities (AREB), named Vall Banc, to receive the lawful clients, assets and liabilities of the former BPA. In April 2016 – one year and one month after the note from FinCEN – the sale of the new entity went through, for the

AGGREGATE DATA FOR THE ANDORRAN BANKS

Table 12.6

Thousand euros	2015	2016
Total assets	14,411,802	14,492,462
Gross loans & discounts	6,278,629	6,299,918
Assets under management	45,214,084	45,434,271
Results	168,548	155,933
ROE	10.93%	9.73%
ROA	1.19%	1.03%
Efficiency ratio	54.15%	59.98%
Solvency ratio	22.78%	25.10%
Liquidity ratio	71.24%	61.41%

Note: 2016 data include the new entity Vall Banc, which started operating on 11 May 2016.

Source: Andorran Banking Association and annual reports from the banking entities.

amount of 29 million euros, to the US-owned investment fund J.C. Flowers and, on 11 May 2016, Vall Banc started operating.

In any case, it can be stated that the Andorran banking system has withstood all these problems very well and that, despite the complex national and international economic environment, the negative interest rates and structural costs, the sector has demonstrated its soundness and solvency throughout 2016, with stability in the main magnitudes.

The credibility and rigour of the Andorran financial system, together with the development of a large range of products and services with added value and the progressive consolidation of the process of international expansion by Andorran banks, have allowed for sustainable, profitable growth in activities in this sector in recent years. This growth was accompanied by an increase in its structures and an increase in the aggregate number of employees.

In 2016, the total value of assets of the Andorran banks have grown 0.6%, to reach 14,492 million euros, and assets under management, i.e. customers' deposits and customer intermediation, custodial or not, have also increased 0.5% to reach 45,434 million euros, a figure that marks a new historical high.

Within assets, net lending, which is the component with the highest percentage (42% of the total), saw a slight decrease of 0.4%, so it reached 6,079 million euros. For its part, the securities portfolio shrank 7.7%, although it is still a significant percentage of total assets, representing 29%. The entry of cash and banks increased 18.3% and stands close to 3,000 million euros.

In 2016, the banks' assets under management increased 0.5%, to reach 45,434 million euros, a figure that represents a new historic high.

ANDORRAN BANK BALANCE SHEETS (2015-2016)

Table 12.7

(Thousands of euros)	ANDBANK GROUP		MORABANC GROUP		CRÈDIT ANDORRÀ GROUP		BANCSABADELL D'ANDORRA		VALLBANC		ANDORRAN BANKS AGGREGATE BALANCE SHEET	
	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016
ASSETS												
Cash and banks	1,107,229	1,737,407	706,768	439,899	583,659	374,892	63,480	94,439	-	264,687	2,461,136	2,911,324
Loans & discounts ⁽¹⁾	1,816,948	1,604,343	1,021,877	1,004,513	2,908,672	2,768,771	355,846	336,748	-	364,591	6,103,343	6,078,966
Securities portfolio	1,646,256	1,149,804	695,703	662,257	2,035,989	2,040,649	194,608	224,189	-	142,379	4,572,556	4,219,278
Tangible assets	93,298	103,732	105,041	98,323	326,959	310,568	33,155	31,513	-	47,828	558,453	591,964
Intangible assets	85,115	99,581	10,204	13,800	62,538	61,385	2,762	2,829	-	3,839	160,619	181,434
Other assets	315,150	293,811	44,272	35,151	188,803	165,507	7,470	7,846	-	7,181	555,695	509,496
TOTAL ASSETS	5,063,996	4,988,678	2,583,865	2,253,943	6,106,620	5,721,772	657,321	697,564	-	830,505	14,411,802	14,492,462
LIABILITIES												
Share capital	78,842	78,842	42,407	42,407	70,000	70,000	30,068	30,068	-	30,000	221,317	251,317
Reserves ⁽²⁾	419,535	449,788	231,461	240,617	489,945	525,328	36,819	40,811	-	9,615	1,177,760	1,266,159
Profit	54,048	47,472	34,885	23,006	72,005	65,044	7,610	8,513	-	11,898	168,548	155,933
Subordinate liabilities	50,000	50,000	52,216	41,088	150,000	150,000	-	-	-	70,000	252,216	311,088
Financial intermediaries	494,312	556,338	61,077	35,141	229,649	185,594	35,710	67,447	-	10,312	820,748	854,832
Deposits	3,634,453	3,440,745	2,101,160	1,806,394	4,883,694	4,454,616	501,074	528,113	-	668,619	11,120,381	10,898,487
Other liabilities	332,806	365,493	60,659	65,290	211,327	271,190	46,040	22,612	-	30,061	650,832	754,646
TOTAL LIABILITIES	5,063,996	4,988,678	2,583,865	2,253,943	6,106,620	5,721,772	657,321	697,564	-	830,505	14,411,802	14,492,462

(1) Net lending to clients.

(2) Reserves includes minority interests, dividends on account and profit/loss from previous financial years pending allocation.

Source: Andorran Banking Association and annual reports by banking entities / Own preparation.

As for liabilities, in 2016 deposits decreased 2%, to drop below 11,000 million euros (specifically 10,898.49 million euros), a figure that represents 75.2% of the total liabilities. Moreover, reserves increased 7.5% and share capital increased 13.6%.

In 2016, the Andorran banks strengthened their balances and improved solvency, a sign of the entities' will to maintain high levels of capitalisation. On 31 December 2016, the aggregate solvency ratio of the five banks stood at 25.10%, a figure that exceeds that of the previous year (22.78%) and doubles the requirements of Andorran banking regulations which fix this coefficient at a minimum of 10%.

For its part, the aggregate liquidity ratio at the end of 2016 was 61.41%, 10 points lower than the previous year but, nevertheless, a ratio that is well above the 40% requirement of Andorran banking regulations.

The operating margin fell 19.9%, resulting in a fall in aggregate profit of 7%, to the figure of 156 million euros, and also a slight decrease in the average return on equity (ROE), which stands at 9.73% (in 2015, it was 10.93%) and the average return on assets (ROA), which stands at 1.03% (in 2015 it was 1.19%).

A significant legislative event was the signing of an automatic tax information exchange agreement, on 12 February 2016, between the Principality of Andorra and the European Union, which entered into force on 1 January 2017. This agreement, which amends the Agreement signed in 2004 between the Principality of Andorra and the European Community on taxation on saving income, adapting it to new international tax transparency standards, involves the basic commitment between Andorra and the European Union to exchange information automatically about the financial accounts of their respective residents.

On 30 November 2016, the General Council passed Law 19/2016, which regulates the legal framework needed to fulfil this automatic tax information exchange agreement. Within the framework of this agreement, Andorra will gather bank data in 2017 in advance, to exchange them with EU member states from 2018.

3. Tourism

Economic activity in the country and the results of the economic financial year are marked by the performance of tourism, which strongly influences hotels, catering, commerce and skiing, among many other activities which depend on visits from potential clients. In this context, the more favourable trend in tourism was fundamental to explaining the improvement in Andorra's economic situation in 2016. The tourism sector has undergone three years of considerable growth thanks, on the one hand, to the situational improvement and, on the other, to various stimulus actions carried out by both the public sector and private operators. According to official GDP figures, the sector of hotels and catering represent approximately 8% of Andorran GVA.

The more favourable trend in tourism encouraged the improvement in Andorra's economic situation.

Increase in the total number of visitors for the third consecutive year.

This improvement in tourist activity is reflected in the increase in the total number of visitors which occurred again in 2016 (2.6%), for the third consecutive year, and puts the total number of visitors at 8,057,325. These values are similar to those of 2011, but still far from those for 2010 (8.5 million) and very far from the 11 million before the crisis.

TOTAL VISITORS BY NATIONALITIES AND FRONTIERS

Table 12.8

		2011	2015	2016	% total 2016	Var. 16/15
Total by nationalities	Spanish	3,976,718	3,884,645	4,123,246	51.2%	6.1%
	French	3,471,122	3,370,665	3,294,883	40.9%	-2.2%
	Others	535,039	595,101	639,196	7.9%	7.4%
Spanish frontier	Spanish	3,681,354	3,674,261	3,884,654	48.2%	5.7%
	French	272,941	298,350	324,697	4.0%	8.8%
	Others	346,291	441,485	485,425	6.0%	10.0%
French frontier	Spanish	295,364	210,384	238,592	3.0%	13.4%
	French	3,198,181	3,072,315	2,970,186	36.9%	-3.3%
	Others	188,748	153,616	153,771	1.9%	0.1%
TOTAL VISITORS		7,982,879	7,850,411	8,057,325	100%	2.6%

Source: Department of Statistics.

By nationalities, growth in the number of Spanish is a fact both in total visitors (6.1%) and in the subdivision: tourists (5.9%) and same-day visitors (6.4%). At these levels, the importance of Spain as the main country of origin of visitors consolidates and exceeds 50% (51.2% of the total). The composition of Spanish visitors is balanced between tourists and same-day visitors (48.8% tourists and 51.2% same-day visitors).

Unlike the Spanish, the composition of French visitors is very unequal, as same-day visitors (86.2%) easily exceed tourists (13.8%). In 2016, French visitors decreased globally by 2.2%, although an increase in the number of tourists of 3.9% occurred, not enough to offset the 3.2% reduction in same-day visitors.

Visitors of other nationalities have grown 7.4%, so their percentage of total visitors has reached 7.9%. The trend in tourists and same-day visitors in this group has been positive in both cases (11.9% and 2% growth, respectively).

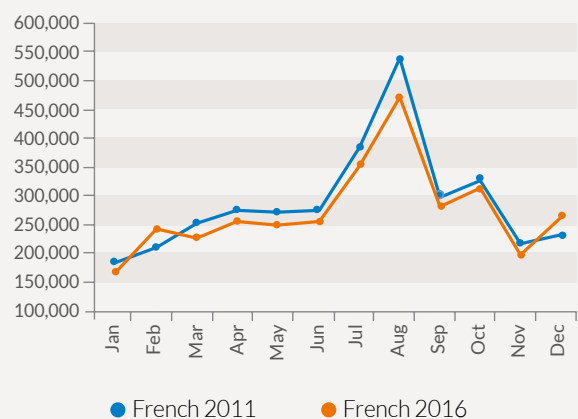
To see the seasonal behaviour of our visitors and whether there has been any development in recent years, we compare the trends in 2016 and 2011, which have been very close in relation to the global number of visitors.

Analysing by nationality, the concentration of French visitors in August becomes evident. So, this is a very seasonal group with a predominance of same-day visitors. It can be seen that between 2011 and 2016, French visitors decreased in a regular manner in almost every month, so an almost identical seasonal pattern continues, but with less visitors.

The behaviour of Spanish visitors is clearly different. In August, there is a notably strong influx, but at levels comparable with other seasons of the year, such as the skiing months and, secondly, Easter Week. From a comparative

NUMBER OF FRENCH VISITORS PER MONTH

Figure 12.4



Source: Department of Statistics.

perspective between 2016 and 2011, very similar behaviour occurs in summer and also a notable improvement in the skiing months. The difference that can be appreciated in March and April is the result of Easter Week, which was in April in 2011, and March in 2016.

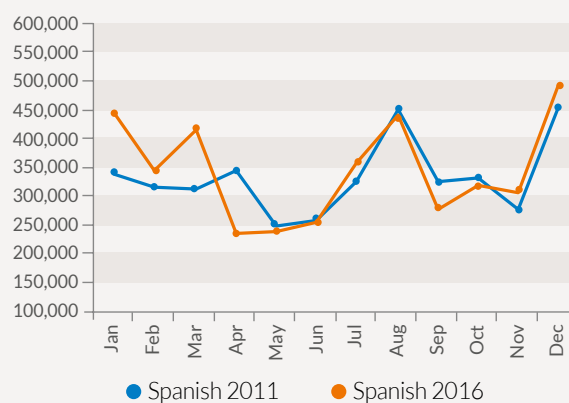
Regarding what visitors state as their motives for coming to Andorra, shopping stands out as the main motive, which takes first place in all the months of 2016, in percentages that vary between 33.2% and 51.8%, based on the month of statistics collection. This means that the main reason for visiting for more than one third of our visitors is commercial attractiveness, with points exceeding 50%.

Also notable are visitors who state that the motive of their visit is pure tourism, to discover the country. This type of visitor is important and quite constant throughout the year, with percentages varying between 20.8% and 30.9%.

Clearly, in the winter months there is an important group of visitors that links their motivation to skiing. This group is between 17.5% and 25.8% in the months from December to March.

NUMBER OF SPANISH VISITORS BY MONTH

Figure 12.5



Source: Department of Statistics.

PASSES/DAYS SOLD BY SEASON

Table 12.9

Season	Ski days (Passes/days sold)	Interannual variation
2000 - 2001	2,255,650	-
2001 - 2002	2,482,000	10.0%
2002 - 2003	2,458,000	-1.0%
2003 - 2004	2,519,333	2.5%
2004 - 2005	2,554,000	1.4%
2005 - 2006	2,528,000	-1.0%
2006 - 2007	1,892,990	-25.1%
2007 - 2008	2,282,000	20.6%
2008 - 2009	2,342,427	2.6%
2009 - 2010	2,331,105	-0.5%
2010 - 2011	2,214,342	-5.0%
2011 - 2012	1,994,028	-9.9%
2012 - 2013	2,181,533	9.4%
2013 - 2014	2,356,664	8.0%
2014 - 2015	2,344,876	-0.5%
2015 - 2016	2,447,112	4.4%
2016 - 2017	2,480,000	1.3%

Note: For passes for the whole season, it is estimated that they are used for 20 days per pass.

Source: Ski Andorra.

In the winter months, the importance of activity linked to skiing is also evident from the indicator of passes sold. Sales of passes in the 2016-2017 season show positive results in relation to the previous season (+1.3%).

After some years in which the crisis had been evident in this activity, the 2016-2017 season came close to levels before the crisis, in which sales of passes managed to stabilise at about 2.5 million.

The increase in tourists in 2016 also led to an increase in the number of overnight stays, if more modest than the increase between 2015 and 2014. In 2015, the number of tourists increased notably but, above all, the average overnight stay increased. In 2016, an increase in tourists of 6.3% occurred but only produced an increase in overnight stays of 2.6%. The reason is that the average overnight stay fell from 3.05 nights to 2.94.

The trend in average overnight stays between 2011 and 2016 shows us an almost constant number that varies between 2.87 and 3.05 nights. Undoubtedly, an increase in the average number of overnight stays is the object of

AVERAGE OVERNIGHT STAY

	2011	2012	2013	2014	2015	2016	Var. 16/15
Average overnight stay	2.91	2.97	3.00	2.87	3.05	2.94	-3.5%
Tourists	2,241,562	2,237,939	2,328,124	2,363,436	2,663,341	2,831,440	6.3%
Overnight stays	6,514,859	6,636,279	6,975,867	6,780,065	8,111,390	8,325,735	2.6%

Source: Department of Statistics.

Table 12.10

national tourism policy but it cannot be ignored that a large number of tourists are weekenders and this will always bias the data notably. An increase in visitors will also be an increase in weekend visitors.

This growth in overnight stays was generated in all types of accommodation, with the exception of tourist apartments, in which they fell 13.2%, putting the percentage of this type of accommodation at 13.6% of the total. Hotels saw an increase in overnight stays of 2.3% and are still by far the most important accommodation, with 59.5% of total overnight stays. Among the others are notably the important increase in overnight stays in aparthotels (45.3%), which puts their percentage at 6.7% of the total; those that take place at homes of friends or family (7.5%), an option that already represents 10.6% of the total, and overnights in own accommodation (6.3%) with 6.2% of the total.

The supply of classified tourist accommodation continues to fall for the eighth consecutive year.

Despite this increase in visitors, the supply of classified tourist accommodation continues to fall for the eighth consecutive year. In 2016, there were 235 tourist accommodations, with a drop of 1.7% against 2015. Of this supply, 167 are hotels; 28 are tourist apartments; 23 aparthotels; 10 hostals or residencies, and 7 pensions. The fall in supply is focussed on hotels (-1.8%) and tourist apartments (-3.4%).

With this trend, in 2016, there were 32,963 beds, 1.9% less than in 2015, due to a loss of beds in all supply options: hotels (-1.5%), hostals or residencies (-10.9%), pensions (-4.5%), aparthotels (-7.0%), with the one exception of tourist apartments, where the number of beds increased 1.7%.

Although the number of beds made available by traditional tourist accommodation is shrinking, at the same time, clear growth in one market niche is appearing, which is for furnished holiday

NUMBER OF BEDS IN TOURIST ACCOMMODATION BY TYPE OF ESTABLISHMENT

	2012	2013	2014	2015	2016	% total 2016	Var. 16/15	Var. 2012-2016
Hotels	28,378	28,354	28,228	27,726	27,300	59.5%	-1.5%	-3.8%
Hostals, resid. & pensions	690	789	772	754	692	1.5%	-8.2%	0.3%
Aparthotels & tourist aparts.	5,203	4,919	5,019	5,133	4,971	10.8%	-3.2%	-4.5%
Total tourist accommodation	34,271	34,062	34,019	33,613	32,963	71.9%	-1.9%	-3.8%
Furnished apartments	5,868	6,773	8,890	9,807	11,146	24.3%	13.7%	89.9%
Others* (beds/spaces)	1,412	1,482	1,659	1,697	1,736	3.8%	2.3%	22.9%
Total Other tourist accommodation	7,280	8,255	10,549	11,504	12,882	28.1%	12.0%	77.0%
Total beds/spaces	41,551	42,317	44,568	45,117	45,845	100%	1.6%	10.3%

*Includes other tourist accommodation such as rural accommodation, holiday homes, campsites, youth hostels, summer camps and mountain huts.

Source: Department of Tourism.

Table 12.11

SUPPLY OF TOURIST ACCOMMODATION BY PARISH

Table 12.12

	2013		2014		2015		2016	
	Establ.	Beds	Establ.	Beds	Establ.	Beds	Establ.	Beds
Canillo	48	6,915	48	7,061	49	7,079	45	7,014
Encamp	48	6,029	48	5,981	49	5,970	49	6,068
Ordino	29	2,269	28	2,233	29	2,313	27	1,927
La Massana	37	5,317	38	5,413	37	5,341	38	5,406
Andorra la Vella	36	6,387	35	6,153	34	6,095	35	6,097
Sant Julià de Lòria	11	1,177	10	1,165	8	820	8	774
Escaldes-Engordany	34	5,968	34	6,013	33	5,995	33	5,677
Total	243	34,062	241	34,019	239	33,613	235	32,963

Source: Department of Tourism.

apartments. Most furnished holiday apartments are concentrated at the foot of the ski slopes of Pas de la Casa and Canillo. The trend in beds in this type of accommodation practically doubles the supply existing between 2012 and 2016. It is even possible that this calculation may undervalue the percentage of this type of accommodation, as probably not all the available beds are duly registered as such. The supply of beds in 2016 was 11,146, a figure that would put this niche in the tourist supply well above the other types, except hotels. No doubt, this relates to the market inertia which is evident in other countries. Tourist movement beyond traditional tourist structures is in full growth.

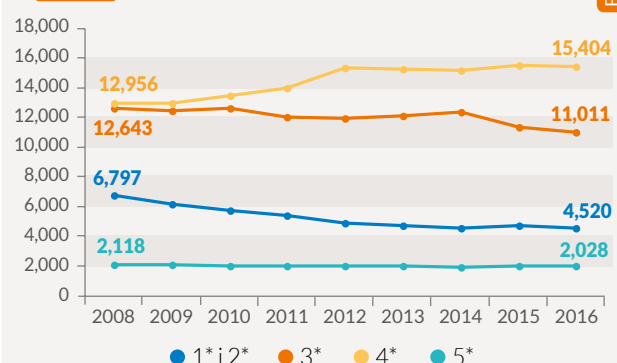
Considering the supply of accommodation (beds) by parish, a high concentration can be seen in parishes we classify as at the “foot of the ski slopes” (Encamp 18.4%, Canillo 21.3% and La Massana 16.4%) and also in central parishes (Andorra la Vella 18.5% and Escaldes-Engordany 17.2%). In Sant Julià de Lòria (2.3%) and Ordino (5.8%), despite having important infrastructures within their boundaries, the distance between town centres and infrastructures diminishes the “foot of the ski slopes” effect.

Disaggregation by parish demonstrates that, in 2016, a reduction in accommodation occurs in Canillo (4 less) and Ordino (2 less). Equally, a decrease in beds occurs in Sant Julià de Lòria (46 less beds), Escaldes-Engordany (318 less beds), Canillo (65 less beds) and Ordino (386 less beds). Despite the decrease, Canillo is still the parish with the highest concentration of beds, followed by Andorra la Vella, Encamp and Escaldes-Engordany. The figures showing such a major decrease in beds in Ordino, in relation to its total supply, can be partly explained by the closure of two establishments which offered approximately 200 beds, but may also be due to the adaptation of rooms by some hotels.

As for the category of tourist accommodation, 53% of beds supplied are of a superior quality (4 and 5 stars). In 2016, the beds supplied in lower categories lost percentage, which is an unequivocal sign of the sector laying its bets on quality. Once again, hotels are improving the category of their supply of beds with the objective of attracting clients with higher

TREND IN NUMBER OF BEDS BY CATEGORY OF TOURIST ACCOMMODATION

Figure 12.6



Source: Department of Tourism.

purchasing power. Clients with more basic accommodation needs can also find an acceptable, ample supply in other types of accommodation, such as furnished holiday apartments.

The 2016-2017 ski season started on 26 November and ended on 17 April (one week later than the 2015-2016 season), so it was open for a total of 143 days. Ski resorts have made investments to improve and equip the installations of 16.55 million euros, 17% less than in the 2015-2016 season. They have persisted in organising major events and activities to make the destination attractive. On closing the season, a major incident arose regarding the future of the joint operation of ski resorts under the Grandvalira brand. At the time of editing this report, it is still uncertain whether the passes for the ski resort Pas de la Casa – Grau Roig and Soldeu – El Tarter will be marketed jointly or separately in the next season.

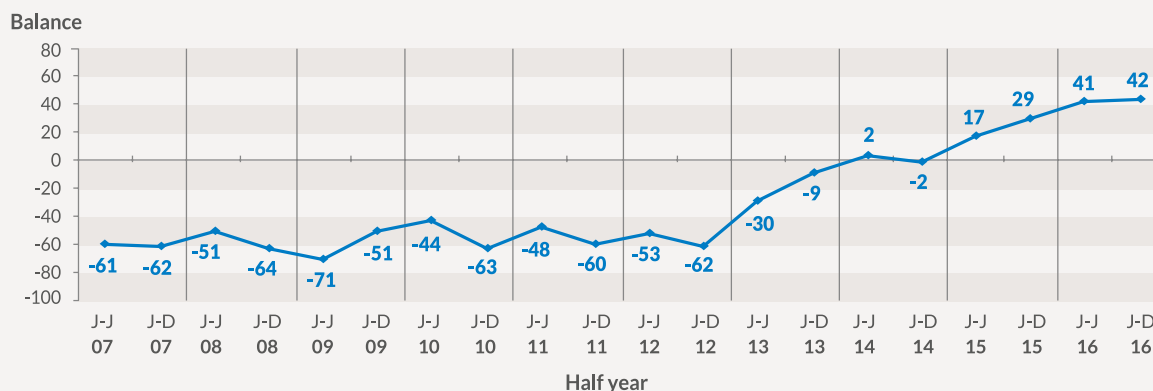
As for the spa, Caldea, the operating company (SEMTEE, SA) continues to progress with the business strategy aimed at increasing the average frequency and entry per user, with new projects such as Caldea Likids (spa designed for children). In 2016, the centre sold 385 thousand entries (Caldea sold 232 thousand and Inuu 62 thousand), figures that represent an increase in sales of 65,000 tickets in two years. Moreover, in 2016, Caldea reached 2,113 members. The effect on results was annual income of 14.8 million euros (11% higher than in 2015), with a net result of nearly 64 thousand euros in losses compared with losses of almost 1 million euros in the previous year. The forecast of imminent profits after a long period of losses has enabled Caldea to offer dividends again to its shareholders, to be paid in 2017.

The Ice Palace shows better results in 2016 than in the previous year. Operating income increased 11.2% and current expenditure grew 1.9%, with current subsidies falling 2.2%, so the result of the financial year was positive (127 thousand euros) and higher than in 2015 (74 thousand euros), which allowed for debt levels to be reduced.

As for La Rabassa snow resort, the 2016-2017 winter season closed with 43,239 visitors, a figure that means a drop in visitors of 19.4%, basically from the change in calendar which meant it was closed 25 more days than in the previous season (the season ran from 1 December 2016 to 17 April 2017). For its part, in 2016, Naturlandia received 183,100 visitors, with a decrease from 2015 of 1.8%.

If we focus interest on the sector of hotels and catering, in 2016, the main indicators of the sector confirm the good situation it is experiencing. Specifically, the number of employees in the sector grew 3.3%, more than double the growth that occurred in 2015 (1.4%), which was the first time it showed positive growth after nine years of continuous falls. Average wages grew 2.1%, after

BUSINESSES' OPINION OF BUSINESS ACTIVITY - HOTEL SECTOR



Balance: Difference between extreme responses (positive and negative), as percentage.

Source: Chamber of Commerce, Industry and Services of Andorra.

Figure 12.7

BUSINESSES' OPINIONS ON THE TREND IN THE HOTEL SECTOR (% of businesses)

Table 12.13

		2014			2015			2016		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
1. Business activity (reviewed half year)	Good	20	25	22.5	25	40	32.5	55	51	53
	Normal	61	49	55	67	49	58	31	40	35.5
	Bad	18	27	22.5	8	11	9.5	14	9	11.5
	Balance	2	-2	0	17	29	23	41	42	41.5
2. Average distribution of clients (%) (reviewed half year)	Catalonia	35	46	40.5	42	39	40.5	36	43	39.5
	Rest of Spain	23	23	23	23	27	25	27	25	26
	France	23	17	20	20	21	20.5	18	21	19.5
	Others	20	13	16.5	14	13	13.5	19	11	15
3. Level of reservations (reviewed half year)	High	6	6	6	8	19	13.5	25	13	19
	Adequate for period	61	58	59.5	65	51	58	55	67	61
	Low	31	35	33	27	26	26.5	18	20	19
	Reservations not taken	2	0	1	0	4	2	2	0	1
	Balance	-25	-29	-27	-19	-7	-13	7	-7	0
4. Average level of occupancy (compared with same half of previous year)	Higher	33	20	26.5	47	49	48	48	55	51.5
	Equal	33	51	42	33	42	37.5	40	39	39.5
	Lower	33	29	31	20	9	14.5	13	7	10
	Balance	0	-9	-4.5	27	40	33.5	35	48	41.5
5. Prices paid by clients (compared with previous half year)	Higher	23	18	20.5	31	11	21	36	36	36
	Equal	56	47	51.5	53	49	51	53	38	45.5
	Lower	21	35	28	16	40	28	11	27	19
	Balance	2	-17	-7.5	15	-29	-7	25	9	17
6. Number of employees (compared with same half of previous year)	More	10	10	10	16	19	17.5	11	25	18
	Equal	78	77	77.5	65	70	67.5	87	73	80
	Less	12	13	12.5	18	11	14.5	2	2	2
	Balance	-2	-3	-2.5	-2	8	3	9	23	16

Source: Chamber of Commerce, Industry and Services of Andorra.

growth of 0.3% in 2015, and the number of establishments grew 3.8% (38 new establishments), making a total volume of 1,029 establishments, the highest figure in the whole available series. In line with this growth, electricity consumption increased 2.7% in the case of hotels and catering, and 30.1% in the case of the ski resorts.

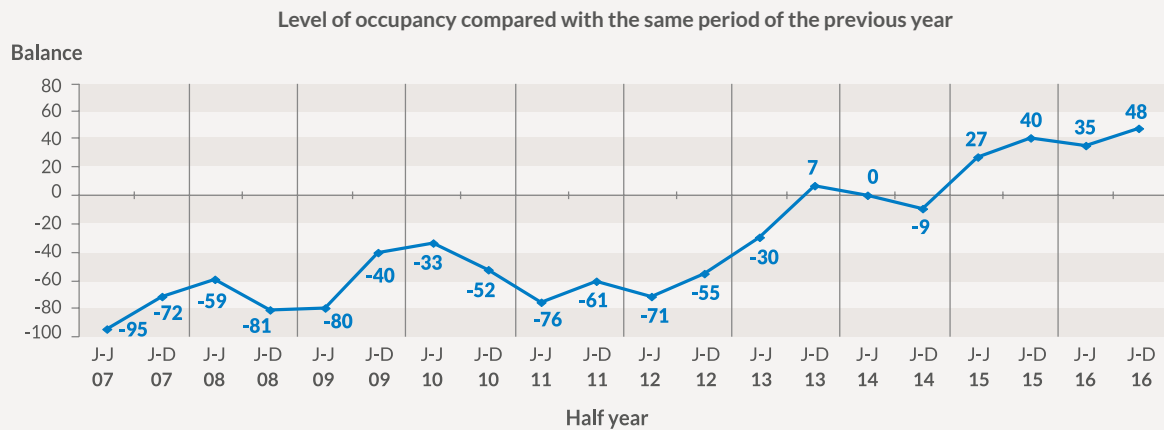
The results of the Chamber's situation surveys show that, for the second consecutive year, the trend in the hotel sector again presented one of the most positive scenarios in the current situation. So, tourism is gradually recovering after a prolonged period of weakness and is consolidated as the main driving force of the economic recovery in Andorra.

Based on hoteliers' replies, the trend in business activity in the second half of 2016 was satisfactory on the whole and much more positive than for the same months of the previous year.

From a territorial point of view, the commercial areas that are traditionally most dynamic outside the ski season were not the only ones to show a positive trend in business activity; the high parishes, especially Canillo and La Massana, also achieved good levels of activity. In contrast, as had happened previously, the parish of Sant Julià de Lòria had notably more modest results.

BUSINESSES' OPINION OF THE AVERAGE LEVEL OF OCCUPANCY - HOTEL SECTOR

Figure 12.8



Balance: Difference between extreme responses (positive and negative), as percentage.

Source: Chamber of Commerce, Industry and Services of Andorra.

In most parishes, hotel occupancy figures for the previous year were easily surpassed.

The good dynamic in the hotel sector is reflected, above all, in the interannual trend in the average level of occupancy which, since early 2015, depicts a clearly rising trend. So, in most of the parishes, the levels of occupancy

recorded one year earlier were easily surpassed, except only for the areas of Ordino and Sant Julià de Lòria, which maintained similar volumes of occupancy to the same period of 2015.

This more positive trend in the demand in Andorran hotels can be explained, above all, by the increase in proximity tourism, with a more favourable tone among Spanish tourists, while less dynamic among the French, according to the specific situation of their economies.

In the businesses' opinion, the rate of growth in the number of employees increased in relation to one year before and sales prices have followed a very moderate rising trend in general.

As for the distribution of clients by nationalities, clients from Spain, with a share of 68%, gained representation among total clients, thanks, above all, to the increase in Catalan travellers, who are becoming more dominant as the main market in the numbers of clients, to represent 43% of the total. In second place in the ranking are French clients – with a 21% share of total clients – followed by other nationalities, with 11%.

In relation to the first half of 2017, hotels' expectations are a little more positive than one year earlier and suggest that the recovery in hotel activity will become more solid, although in a very gradual manner.

Businesses hope that business activity will continue to improve and the average level of occupancy will tend to increase in most parishes, although the levels of activity will remain modest.

The percentage of businesses that consider that weak demand is an obstacle to improvement in activity have reached 36%, the lowest level since 2001. In contrast, 67% of businesses feel limited by the lack of qualified personnel – a factor that is currently the main obstacle to good progress in activity – and 64%, by the increase in operating costs.

4. Transport and communications

In 2016, the main indicators in the transport and communications sector confirm the signs of recovery.

The number of employees in the sector has grown 4.3%, after the drop of 0.6% in 2015, basically from the increase in employment in the activities of mail and telecommunications (8.5%) and land transport (4.5%).

Average wages grew 0.9%, after growth of 0.6% in 2015, above all due to the contribution from the subsector of mail and telecommunications, where wages increased 2.6%, offsetting wage decreases which occurred in all other subsectors.

Fourth consecutive year of increasing numbers of vehicle registrations (13.5%), with a total of 3,852 registrations.

For their part, the number of establishments fell 1.4%, after increases in the previous two years (2.7% in 2015 and 0.2% in 2014). In this way, the total number of establishments is 408, six less than in 2015, due to a drop in land transport and transport related activities.

2016 is the fourth consecutive year of increase in the number of vehicle registrations (13.5%), with a total of 3,852 registrations, the highest figure since 2007. This increase occurred in all types of vehicles, except mopeds (in which there was a decrease of 10.5%) and snow bikes (with a decline of 36.8%). Of note is the percentage increase in lorry registrations, which increased 78.8% compared with 2015. Car registrations, which represent practically 70% of all vehicles, increased 10.5%.

With these figures, the number of vehicles grew 2.6%, more than double the growth one year earlier (1.2%). The number of vehicles per thousand inhabitants (estimated population) is 1,111, if counting total vehicles, and 751 if counting only cars. This figure reveals that Andorra is one of the countries with most vehicles per inhabitant in the world, according to the study by the World Health Organisation (WHO) on the global road safety situation in 2015.

Very good response to the incentive programmes to buy eco-friendly vehicles (Engega Plan).

A large part of this upward trend was driven by the measures taken by the Administration to reactivate activity in this sector, with incentives to buy eco-friendly vehicles (Engega Plan). This programme was well received: the first offer

VEHICLE REGISTRATIONS (Units)

	2005	2013	2014	2015	2016	Var. 16/15	% total 2016
Cars	4,491	1,682	2,194	2,431	2,686	10.5%	69.7%
Motorcycles	1,266	426	525	574	718	25.1%	18.6%
Vans	397	149	167	200	244	22.0%	6.3%
Lorries	147	31	45	33	59	78.8%	1.5%
Special vehicles	185	28	39	29	37	27.6%	1.0%
Mopeds	106	17	14	19	17	-10.5%	0.4%
Snow bikes	23	67	16	19	12	-36.8%	0.3%
Others*	158	87	79	89	79	-11.2%	2.1%
Total	6,773	2,487	3,079	3,394	3,852	13.5%	100%

*Consisting of private trailers and agricultural tractors.

Source: Department of Transport.

VEHICLE REGISTRATIONS BY FUEL (Units)

Table 12.15

	2015	2016	Var. 16/15	% total 2016
Diesel	1,945	1,876	-3.5%	48.7%
Petrol	1,327	1,661	25.2%	43.1%
Electric 100%	3	84	2,700.0%	2.2%
Plug-in petrol hybrid	4	82	1,950.0%	2.1%
Petrol hybrid, not plug-in	18	45	150.0%	1.2%
Plug-in diesel hybrid	0	0	-	0.0%
Diesel hybrid, not plug-in	2	0	-100.0%	0.0%
Without fuel or not available	95	104	9.5%	2.7%
Total	3,394	3,852	13.5%	100%

Source: Department of Transport.

Box 12.1

LIST AND KILOMETRAGE OF VARIOUS TUNNELS

- La Tàpia tunnel:** part of the Northern section of the Sant Julià de Lòria bypass. It has three lanes: two lateral, one in each direction, and a reversible central lane (MPC); it is part of the CG1 main road and connects the new Laurèdia square with the Aixovall roundabout. The basic features of the infrastructure are: length: 502m, free height: 5m, section type: 1m pavement on both sides, 10.5m road in 3 lanes of 3,5m width; it has an emergency tunnel in the middle, about 80m long.
- Pont Pla tunnel:** has two lanes for traffic and connects the axis formed by Carrer Valira and Carrer de la Unió with the CG3. The basic features of the infrastructure are: length: 1,291m, free height: 5m; it has a parallel emergency tunnel with seven access points on the right-hand side.
- La Pedrera tunnel:** starts at PK 2+300 and ends at PK 2+432 on the CG3 north of Pont Pla tunnel. Formed of one 3-lane tunnel (one descending towards Andorra la Vella and two lanes climbing towards La Massana). The tunnel is 132m long.
- Sant Antoni tunnel:** starts at PK 3+289 and ends at PK 3+550 on the CG3 north of the Pont Pla tunnel. Formed of one tunnel with one lane (descending towards Andorra la Vella), 278m long, and a second tunnel with two lanes (towards La Massana), 261m long. The two tunnels are interconnected by a tunnel 34m long.
- Dic d'Arinsal tunnels:** consist of two bidirectional road tunnels with one lane in each direction (tunnels 1 and 3) forming part of the CS-530, which starts at the end of the CG-5, and a water tunnel. Tunnel 1 is 183m long, tunnel 2 is 36m long, and tunnel 3 is 197.5m long.
- Arcalís tunnel:** starts at approximately PK 21+810 and ends at PK 22+000 of the CG3. Consists of one bidirectional tunnel. Length: 190m.
- Dos Valires tunnel:** consists of two one-directional tubes with two lanes and a central emergency and service tunnel, which interconnects the main tubes at eleven points. Includes access viaducts of the west mouth (La Massana), and the roundabout connecting to the CG3, at the north exit of the Sant Antoni tunnels. Also consists of access viaducts at east mouth (Encamp), with the raised roundabout of the CG2. The basic features of the infrastructure are: north tube length: 2,910m, south tube length: 2,913m, free height: 5m. Provided with emergency and service tunnel, 2,912 metres long, with eleven accesses from main tubes, uniformly distributed at intervals of 250m and located between the two road tunnels.
- Ràdio Andorra tunnel:** has two one-directional tubes with two lanes in each tube, forms part of the CG2 and connects the Valira Nova area with Encamp town centre. The basic features of the infrastructure are: east tube length: 180m, west tube length: 160 metres, and free height: 4.5m.

Source: Ministry of Land Planning.

from the Engega Plan 2016, backed by the amount of 1 M euros (750,000 euros in grants to buy electric and plug-in hybrid vehicles, and the other 250,000 euros to cover scrapping) ran out within almost 30 days in mid-May, and the second offer, backed by 300,000 euros, ran out in June.

The result of the Plan can be seen by analysing registrations of vehicles by fuel-type. So, we can see that the number of totally electric vehicles went from 3 units to 84 units in one year and the volume of registered plug-in hybrid vehicles went from 4 units to 82. These two vehicle categories represent 4.3% of the total. This proportion puts Andorra among the leading countries in the presence of this type of vehicle.

As for infrastructures, in recent years, major investment has been made to provide the country with a modern road network which would cope with the tourist traffic accessing places of interest, provide internal communications inside the country and minimise the effects of traffic jams at different times. The road network has a total of 273.50 km, distributed along 92.90 km of main roads and 180.60 km of secondary roads. In box 12.1 you can see the list and kilometrage of various tunnels.

As for the communications branch, the same dynamic of the last four years is confirmed, with an increase in the number of mobile subscriptions (6.7%), leaving the total figure at 76,132 lines, together with a drop in the number of landline subscriptions (-8.1%), putting the total number of lines at 41,406. There are also 32,490 fibre optic lines, representing an increase of 5.9%.

This dynamic is consolidated when observing the trend in telephone traffic: in 2016, national landline traffic fell 20.8%, while mobile traffic increased 17.6%. International traffic, both by landline and mobile, fell 11.2% in the case of incoming traffic, and 8.5% in the case of outgoing traffic. In contrast, Internet telephone traffic by fibre optic grows strongly: national traffic almost doubled (growing 98.7%) and international increased 15.0%; equally, mobile internet traffic increased 69.1%.

Internet telephone traffic by fibre optic grows strongly.

Box 12.2 expands the information about the main projects carried out by Andorra Telecom over the year.

Box 12.2

MAIN ACTIONS BY ANDORRA TELECOM IN 2016

On 31 December 2016, Andorra became one of the first countries in the world to stop using copper landlines. So ended the long process of installing fibre optic throughout the country, which began in 2008 and saw its first major milestone when ADSL was turned off forever on 31 December 2014.

Throughout 2016, the changeover process was carried out in homes that still had copper cables. The process was divided into two stages: 31 July was the deadline to convert to fibre optic in the central, more populated parishes of Andorra la Vella and Escaldes-Engordany, and 31 December for the rest of the country.

Currently, in the Principality, there are 79 million metres of fibre optic installed. The use of FTTH technology gives advantages to the users, especially in the case of professionals and businesses, and represents savings on network management costs. The change was also used to lower the visual impact of lines by burying the network underground in many sections.

Another great change in 2016, from the technological point of view, was the substitution of the telephone exchange and the change of access to Internet, basic changes to guarantee landlines and Internet.

One of the company's main courses of action in 2016 was to reduce the cost of the customers' *Roaming Out* service. The cut in roaming charges for customers abroad, achieved thanks to new agreements with international operators, resulted in a notable increase in connections by Andorran mobiles outside the country and exponential growth in data use. Also in 2016, decisive steps towards diversification of the company's activities continued, faced with the prospect of a reduction in *Roaming In*.

The new agreements with the main foreign operators allowed for gradual adaptation to the new regulatory framework of the European Union and managed to soften the impact of falling revenue over several financial years. Reducing the charges that foreign operators pass on to their customers when roaming in Andorra has resulted, and will continue to result, in exponential growth in data consumption, which will help to offset the impact of falling charges. Revenue from *Roaming In* was 48% of the total business figure, with 49.8 million euros invoiced.

On the other hand, in this financial year, the ESPIC international contact centre was put into operation, the result of setting up the company ANSEAC, SA, owned equally by Andorra Telecom and MST (Medios y Servicios Telemáticos, SAU), a Spanish company specialising in customer relations and services in the European market. The company ended its first year of activities with positive results.

Another important step in the company's growth policy was the purchase of 2.69 percent of shares

in the fourth largest Spanish mobile operator, the company MásMóvil, for a total of 10.5 million euros. This transaction converts Andorra Telecom into a shareholder in one of the most prestigious businesses and opens up the possibility of exploring the development of interesting synergies in various fields (Andorrans roaming in Spain, contact centre services, etc.). Along with this diversification, the first national cloud was also launched, marketed under the name Som Cloud ("We are Cloud").

The desire to promote the new building project of The Cloud also marked 2016, freeing up administrative, commercial and technical spaces, and starting steps prior to deconstruction of existing buildings. This emblematic project, classified of national interest, will be an attraction with the power to transform the town centre of Andorra la Vella.

Finally, regarding economic and financial data, Andorra Telecom maintains a sustained level of investment. The 23.8 million invested in 2016 are equal to a ratio of 22.9% of the volume of invoicing. Andorra Telecom's investment indices in technical infrastructure remain well above those of other operators in the sector. If the annual average investment by a telecommunications company varies between 12 and 15% of its revenue, up to 25% in an exceptional financial year, the annual average investment by Andorra Telecom reached 24 million between 2004 and 2016, a figure that represents 28% of its annual revenue.

Source: Andorra Telecom.

Comparative analysis with other economies

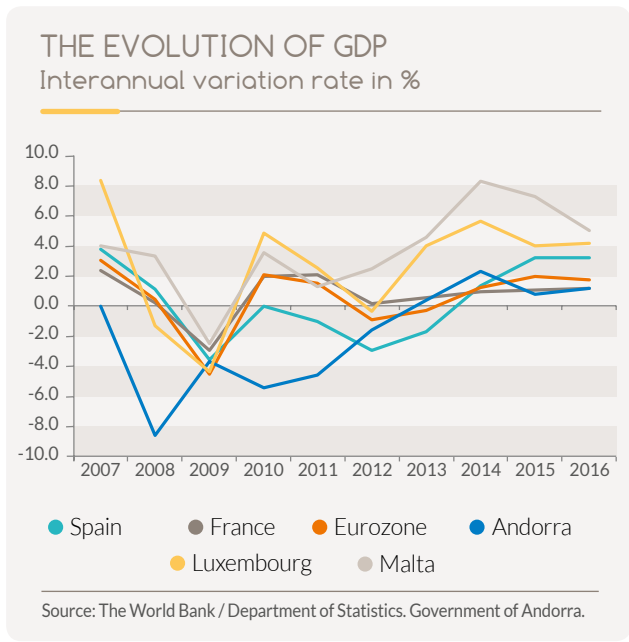
In this section, some of Andorra's main macroeconomic indicators are compared with those of surrounding economies, specifically its neighbouring countries (France and Spain), the Eurozone as a whole, and Malta and Luxembourg. The latter two countries have been chosen as representing smaller territories and therefore, theoretically, more comparable with Andorra. Even though countries like Liechtenstein, Monaco or San Marino would appear more similar to Andorra in size, the international statistical sources used do not provide updated data for them on an annual basis.

MACROECONOMIC DATA 2013-2016

		2013	2014	2015	2016
Andorra	GDP (annual variation %)	0.4	2.3	0.8	1.2
	Public deficit (in % GDP)	1.8	0.9	0.4	2.5
	Debt (in % GDP)	43.9	42.5	42.2	41.6
	GDP per capita (PPP\$)	46,785	47,657	46,374	-
	Tax burden (in % GDP)	22.6%	23.2%	23.4%	25.3%
France	GDP (annual variation %)	0.6	0.9	1.1	1.2
	Public deficit (in % GDP)	-4.0	-3.9	-3.6	-3.4
	Debt (in % GDP)	92.3	94.9	95.6	96.0
	GDP per capita (PPP\$)	39,488	40,221	41,178	41,466
	Tax burden (in % GDP)	47.4	47.8	47.9	-
Spain	GDP (annual variation %)	-1.7	1.4	3.2	3.2
	Public deficit (in % GDP)	-7.0	-6.0	-5.1	-4.5
	Debt (in % GDP)	95.5	100.4	99.8	99.4
	GDP per capita (PPP\$)	32,602	33,658	34,696	36,310
	Tax burden (in % GDP)	34.0	34.5	34.6	-
Eurozone (19 countries)	GDP (annual variation %)	-0.2	1.2	2.0	1.8
	Public deficit (in % GDP)	-3.0	-2.6	-2.1	-1.5
	Debt (in % GDP)	93.7	94.3	92.5	91.5
	GDP per capita (PPP\$)	38,979	39,980	41,123	41,999
	Tax burden (in % GDP)	41.3	41.5	41.4	-
Malta	GDP (annual variation %)	4.6	8.3	7.3	5.0
	Public deficit (in % GDP)	-2.6	-2.0	-1.3	1.0
	Debt (in % GDP)	68.7	64.3	60.6	58.3
	GDP per capita (PPP\$)	31,240	33,854	35,881	39,899
	Tax burden (in % GDP)	33.6	35.1	34.7	-
Luxembourg	GDP (annual variation %)	4.0	5.6	4.0	4.2
	Public deficit (in % GDP)	1.0	1.4	1.4	1.6
	Debt (in % GDP)	23.4	22.4	21.6	20.0
	GDP per capita (PPP\$)	95,697	101,832	104,206	105,882
	Tax burden (in % GDP)	39.8	39.4	39.1	-

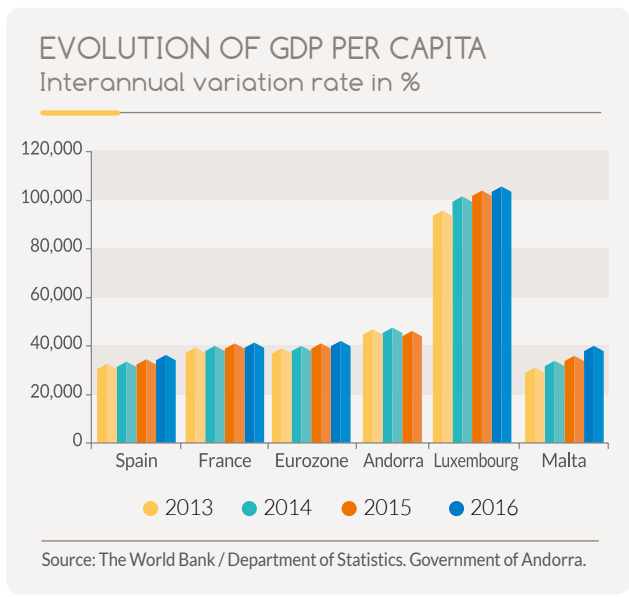
Source: Eurostat / The World Bank / Department of Statistics of the Government of Andorra.

GDP. Andorra's economy has been affected in recent years by the financial crisis which started in 2008 and was suffered by most Eurozone countries, but also by structural factors which resulted in a clearly more negative evolution of GDP than in surrounding countries. In effect, GDP in 2008 fell 8.6%, when the greatest fall in Spain was 3.6% in 2009, and in France 2.9% in the same year. Over the last four years, Andorra has had positive GDP growth rates, although in 2015 and 2016 these were lower than the rates of surrounding countries. Malta and Luxembourg stand out, with growth rates over 4% from 2013.



As for the GDP composition of different countries, Andorra and Luxembourg have the largest percentage in the service sector (close to 90%), with the lowest in agriculture (under 1%). The GDP contribution from both the industrial sector and the primary sector is more significant in other countries. In fact, the service sector's percentage of GDP is under 80% in neighbouring countries.

GDP PER CAPITA. The GDP per capita data are standardised as dollars PPP (purchasing power parity), an indicator that enables GDP to be compared as a purchasing power capacity that is comparable between countries. In the case of Andorra, we do not have the 2016 data at the time of drawing up this report.



Luxembourg stands out in the comparative analysis, with GDP per capita over 100,000 dollars and, moreover, showing growth throughout the analysed four years. Malta also shows a clear improvement, with GDP per capita at levels close to 40,000 dollars in 2016.

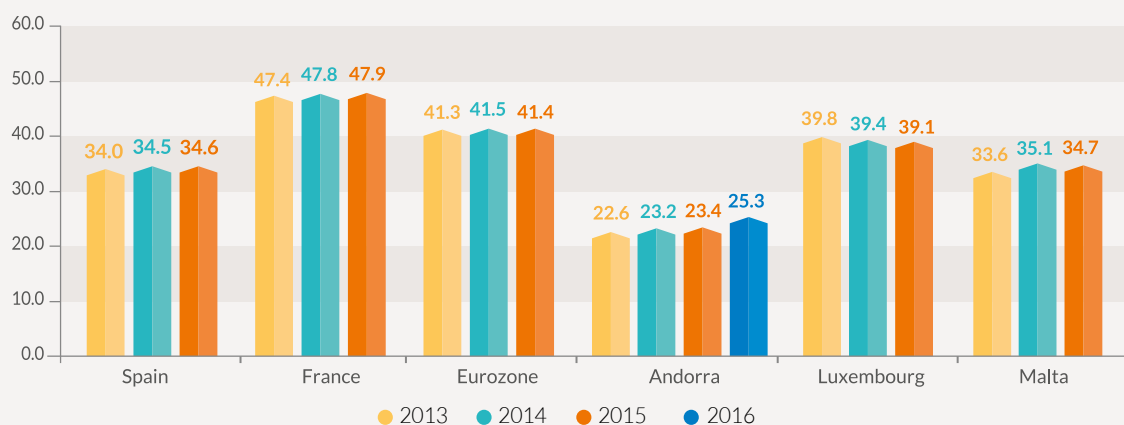
Spain, at 36,310 dollars, is below France (41,466 dollars) and the whole of the Eurozone (41,999 dollars). Andorra, from 2015 data (46,374 dollars,) has higher GDP capita PPP than the rest of these countries, except Luxembourg.

TAX BURDEN. As for the tax burden, the latest available data from Eurostat for the other countries we are comparing refer to 2015. In the case of Andorra, we have used the most recent, relating to 2016.

In 2013, Andorra's tax burden was 22.6%, clearly the lowest in Europe and well below the Eurozone countries as a whole (41.3%), neighbouring countries (34.0% Spain and 47.4% France), and other small European countries such as Malta (33.6%) and Luxembourg (39.8%).

In recent years, Andorra, despite its low tax burden compared with other European countries, has gradually raised it by introducing new forms of tax and increasing social contributions. In fact,

EVOLUTION OF TAX BURDEN (% of GDP)



Source: Eurostat / Department of Statistics. Government of Andorra.

in 2016, Andorra's tax burden increased 1.9 points to 25.3%, while those of Spain, France and the Eurozone as a whole remained quite stable in 2015. In contrast, Luxembourg's tax burden decreased slightly and Malta's had more erratic behaviour. In 2015, France became the European country with the highest tax burden.

Regarding the percentage for each type of tax of each of these countries, Andorra stands out for its percentage of indirect taxes (IGI and consumption taxes mostly) within taxation as a whole. The low percentage of social contributions in Malta and the significance of direct taxes in Luxembourg stand out. The other countries are in line with the Eurozone average.

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ACCRUED TAXES BY TYPE Percentage of total (%)

	Taxes on production and imports	Current taxes on income and assets	Social contributions	Others	Total
Eurozone	32.1	30.4	37.0	0.5	100.0
Spain	34.7	29.3	35.5	0.4	100.0
France	33.5	26.3	39.5	0.7	100.0
Andorra	46.5	17.8	35.7	0.0	100.0
Malta	39.4	40.5	19.5	0.5	100.0
Luxembourg	31.3	37.2	31.1	0.4	100.0

Data updated to 2016 for Andorra and 2015 for other countries.

Source: Eurostat / Department of Statistics. Government of Andorra.

DEBT. Both Spain and France show a very high level of public debt (close to 100%), above the Eurozone average. In the case of Spain, it can be seen that from 2015, the tendency is towards a slight decrease in GDP (99.4% in 2016). In the case of France, on the other hand, the level of debt has been increasing in recent years, reaching 96.0% in 2016.

Luxembourg stands out for two reasons: because it has a very low level of debt compared with other countries (20.0% in 2016), and because this has been falling over recent years. Malta's debt, for its part, has decreased significantly during the analysed period, and in 2016 reached a level of 58.3% (10 points less than in 2013).

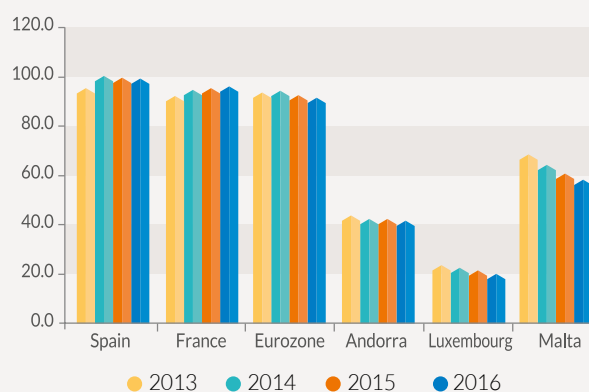
Andorra maintains a level of debt that is notably lower than the Eurozone average and that of Malta, but double that of Luxembourg (41.6% in 2016). It is notable that this calculation includes

both the Government debt (36.0%) and the Commune debt (5.5%). Moreover, Andorra has been gradually reducing the level of debt in relation to GDP (2.3 points since 2013). To a large extent, this reduction is the result of the Communes' efforts in recent years.

PUBLIC DEFICIT. Interpretation of the evolution of the deficits is quite similar for France, Spain, the Eurozone and Malta. All show a tendency to reduce their deficit. In the case of Spain, this reduction results in higher percentages than the rest; in the case of France, over the Eurozone average, and in the case of Malta, a reversal of the trend in 2016 and the beginning of a surplus. On the other hand, Luxembourg's public finances produce growing surpluses every year.

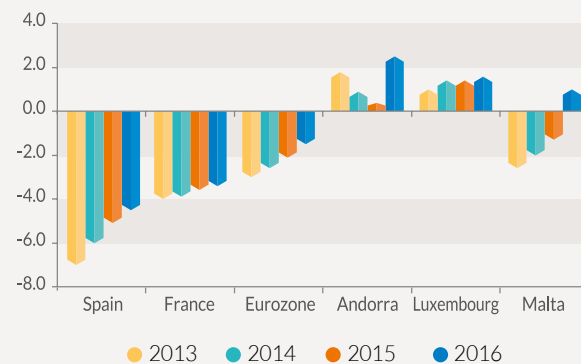
As for Andorra, the aggregate non-financial cash deficits and surpluses of the Government and Communes were used. As can be seen, surpluses have been produced every year on the whole, but without a clear trend like Luxembourg.

PUBLIC DEBT In % of GDP



Source: Eurostat / Department of Statistics. Government of Andorra.

PUBLIC DEFICIT In % of GDP



Source: Eurostat / Department of Statistics. Government of Andorra.

Timeline of the most significant economic developments in 2016

January

- ▶ January 1, Double Taxation Agreement (DTA) with France implemented.
- ▶ January 1, the Pensions Reserve Fund (PRF) receives the assets from the CASS pension fund, taking over their management.

February

- ▶ February 12, Andorra and the EU sign the automatic Tax Information Exchange Agreement (enters into force on January 1, 2017).
- ▶ Standard & Poor's rating agency maintains Andorra rating at BBB-/A-3 with a negative outlook.
- ▶ February 26, DTA with Spain implemented.
- ▶ Alpine Ski World Cup competition held in Andorra.

March

- ▶ March 7, DTA with Luxembourg enters into force (implemented January 1, 2017).
- ▶ Law 4/2016 passed, on 10 March, on the promotion of electric vehicles (amended by Law 15/2016 of 20 October).
- ▶ Fitch Ratings, the international agency, assesses Andorra's sovereign debt and maintains the BBB rating with a stable outlook.
- ▶ National Budget for 2016 passed (Law 2/2016, of 10 March).
- ▶ March 23, a public debt issuance (bonds) of 260 million euros is approved, to refinance a loan of 260 million euros.
- ▶ March 30, a public debt issuance (bonds) of 100 million euros is approved, to refinance a previous issuance of 70 million euros and formalise a new debt of 30 million euros.

April

- ▶ The percentages of contributions to the general branch of the CASS (Social Security System) for employees and the self-employed are modified. Total contribution percentages rise from 20% to 22% (6.5% charged to the employee and 15.5% to the business).
- ▶ The Paris Agreement is signed, an international agreement adopted within the framework of the 21st Conference of the Parties within the UN Framework Convention on Climate Change.
- ▶ The Government closes the water bottling plant in Arinsal.

May

- ▶ May 11, Vall Banc starts to operate as a bank.
- ▶ May 11, a debt issuance (bonds) of 100 million euros is approved, to refinance a previous issuance of 100 million euros.

June

- ▶ The Trial World Championship is held in Andorra.

July

- ▶ Andorra Telecom becomes a shareholder in the company MásMóvil, the fourth largest Spanish mobile operator, buying 2.7% of the shares in the Spanish company.
- ▶ Standard & Poor's agency improves Andorra's outlook from "negative" to "stable" and maintains Andorra's rating at BBB-/A-3.
- ▶ The electronic signature is put into operation.
- ▶ The Tour de France reaches Andorra.

September

- ▶ Fitch Ratings maintains Andorra's rating at BBB with a stable outlook.
- ▶ September 20, the DTA with Malta is signed.
- ▶ September 21, a public debt issuance (bonds) of 100 million euros is approved, to refinance a previous issuance of 100 million euros.
- ▶ The Mountain Bike World Cup is held.

November

- ▶ The presentation is made of the Strategic Shopping Tourism Plan, to promote Andorra as an upmarket shopping destination.
- ▶ November 21, the DTA with Liechtenstein comes into force (implemented on January 1, 2017).
- ▶ Law 19/2016, of 30 November, on automatic tax information exchange is passed (entry into force on January 1, 2017).
- ▶ November 30, the DTA with Portugal is ratified (implemented on January 1, 2018).
- ▶ November 30, public debt issuance (bonds) of 150 million euros approved, to refinance a previous issuance of 150 million euros.

December

- ▶ December 1, Convention on mutual administrative assistance on tax matters enters into force.
- ▶ First Andorran cogeneration plant starts operating in Soldeu.
- ▶ December 21, the Tax Information Exchange Agreement with the Republic of Korea enters into force.
- ▶ December 22, the accounting framework applicable to entities operating within the Andorran financial system and collective investment schemes under Andorran law is approved, in compliance with the international financial reporting standards adopted by the European Union (EU-IFRS) and which have also been adopted by Andorra (Andorra-IFRS) (entry into force on January 1, 2017).
- ▶ December 31, Andorra becomes one of the first countries in the world to permanently stop using copper landlines.

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