

23
number

2017 economic report



CAMBRA
DE COMERÇ
INDÚSTRIA I SERVEIS
D'ANDORRA

With the support of



Andorran Banking
Associació de Bancs Andorrans

EDITED BY

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and Services of Andorra

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WITH THE SUPPORT OF

Andorran Banking

GRAPHIC DESIGN

Jecom disseny

PRINTER

Gràfiques Andorranes

ISBN: 978-99920-3-176-6

LEGAL DEPOSIT: AND.522-2018

2017 | economic report



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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 2017, global economic growth surpassed expectations and experienced the best trend since 2011. The most notable driving factors were monetary policies, which are still expansionary, despite rising interest rates in the US; fiscal easing; an upswing in investment; the favourable trend in financial markets, and a sudden recovery in world trade. The fact that the risks that threatened growth at the beginning of the year did not materialise, such as a hard landing of the Chinese economy, the impact of Brexit or the effect of gradually rising interest rates in the US on emerging economies, also favoured world growth.

In the political arena, it is notable that Trump's rise to power in the US administration did not negatively affect the economy but, on the other hand, increasing international tensions did, especially the threat of a trade war. In Europe, the risk of rising populism did not materialise either in France, where Macron won in 2017, or in Germany, where Angela Merkel re-emerged as Chancellor.

As a result, growth of the world economy in 2017 accelerated to 3.7%, according to International Monetary Fund estimates in July 2018. Among the advanced economies, the Eurozone was the surprise of the year, with higher-than-forecast growth, overtaking GDP growth in the US.

In this context, despite the US having higher interest rates and more favourable economic prospects than the Eurozone – especially after the tax rebate approved by the Trump administration in December 2017 – the dollar depreciated against the euro throughout 2017, interrupting the trend of appreciation that marked the 2014-2016 period. Euro appreciation made European exports more expensive, but dynamic international trade offset this effect. In contrast, the revaluation of the European currency cheapened energy imports, helping to hold down inflation.

In the specific case of the neighbouring economies of Spain and France, the economic situation was also positive in 2017. In 2017, the French economy grew at the highest rate in the last six years (2.2%), though still lower than the whole of the Eurozone. This was greatly encouraged by the favourable international environment, low interest rates and increased economic confidence since the presidential election in May 2017. It should also be emphasised that the new president of the French Republic has begun a period of economic reform and commitment to relaunching the European Union, starting with a historic reform of French labour law at the end of 2017.

As for Spain, the rate of economic activity remained strong (3.1%), higher than initially forecast, allowing it to recover the GDP level it had before the crisis and continue to approach 2008 employment levels. The expansionary trend surpassed expectations, largely thanks to the favourable behaviour of foreign markets, and despite the negative impact of political uncertainty in Catalonia during the fourth quarter, which was very moderate. So, in 2017, the Spanish economy saw new historic records in the figures for exports and foreign tourists, showing the progress that has been made in opening up and internationalising the economy during the period of crisis. Altogether, this resulted in greater consumer and business confidence, reflected in the good trend in consumption and investment.

In this context, the behaviour of the Andorran economy in 2017 was also positive, in global terms, with a similar level of dynamism to that of the previous financial year, resulting in real GDP growth of 1.9%. In nominal terms, total GDP increased to 2,674 million euros, the highest value since 2008. In this way, Andorra continued to extend the phase of economic growth that began in 2013, enabling it to gradually regain pre-crisis levels of activity.

Now, from an international perspective, Andorran GDP growth in 2017 remained below both that of the neighbouring economies of France and Spain and the whole of the EU. On the other hand, the Andorran population has continued to grow much faster than the European (2.3% and 0.2%, respectively). Consequently, Andorra has continued to fall behind its neighbouring economies in terms of per capita wealth. According to official figures, per capita GDP in Andorra stood at 35,747 euros in nominal terms, a similar level to 2014 and 0.5% higher than in the previous financial year.

The growing dynamism of the Andorran economy that has been seen in recent years has been driven largely by the good performance in the international context, above all the Eurozone and, more specifically, Spain. This supportive factor was partly offset by domestic problems suffered by the financial sector in the last three years, both by the bank Banca Privada d'Andorra going into administration in March 2015 and the subsequent process of resolution of the entity, and due to an ever more demanding and competitive regulatory environment that requires major efforts for transformation and adaptation.

The positive trend in the Andorran economy can be seen in the rise in most indicators of activity and demand, although improvement is at relatively low levels in some cases. Among the most significant are the increases in imports, numbers of tourists, employment, car registrations, imports of capital goods, government operating costs and public investment, all higher than in 2016. Also significant is the dynamism in numbers of businesses and registrations of industrial vehicles. Only energy consumption and credit were negative.

By sector, Andorran economic growth continued to be led by services, especially activities linked to tourism which, in turn, depend basically on a good performance in foreign demand. Also notable is the contribution from construction, continuing its gradual path to recovery that started in 2016. In contrast, the rate of activity in industry and agriculture appeared to weaken in comparison with the previous financial year.

Specifically, in 2017, growth of real GVA in the primary sector slowed to 3.3%. This slowdown was accompanied by falling employment, in a context where the utilised agricultural area and tobacco harvest also shrank, in a year of rather complicated meteorological conditions for growing tobacco.

For its part, the construction sector saw real GVA growth of 3.5%, surpassing that of 2016. This upturn is significant because it reaffirms the trend of recovery that started in 2016, after nine years of deep crisis, with steep falls in GVA that, in 2015, stood 60% below the maximum achieved in 2006. The improvement in construction can also be seen in the trend in most available indicators of activity in the sector. So, in 2017, there were increases in the numbers of employed and establishments, authorised square metres and imports of building materials. Moreover, public investment saw a strong increase, after the serious downturn in 2016. Along the same line, the results of the Chamber's surveys show a gradual recovery in the sector. So, the trend in business activities has been positive for five consecutive half-years, while the replies from businesses about the trend in contracted and executed works consolidates the trend of improvement that started in 2016, if still at very low levels.

As for the industry and manufacturing sector, the trend in 2017 was weak. So, real industrial GVA stagnated, compared with the 3% increase seen in 2016. This weakness in overall industrial and manufacturing activity was reflected in the falling numbers of employed, and stagnation in the number of businesses in the sector. However, a trend has also been seen towards gentle improvement in the climate of confidence in the sector, reflected in businesses' replies to the Chamber's surveys. Moreover, businesses' opinions of business activity remained at positive levels, though declining a little in comparison with the previous financial year, as occurred in production.

As for services, in 2017, they were still the most dynamic sector of the economy, led by the improvement in activities linked to tourism. Altogether, the real GVA of the subsector Commerce, hotels and catering, transport, information and communications combined three years of quite high growth, with an increase of 4.4%, compared to 3.1% in 2016. This positive trend continued to be driven by the increase in the numbers of tourists (6.5%), although the numbers of same-day visitors fell slightly. The upward trend in tourism was also evident in the increase in ski days sold and the increase in total overnight stays. In commerce, on the other hand, the increase in activity was much more modest, as shown by the slight growth in most sector indicators. Altogether, this resulted in a much higher increase in the numbers of employed and establishments in hotels and catering, than in commerce.

Growing dynamism in tourism was also reflected in the Chamber's surveys on the hotel sector, with a better evaluation of business activity than in 2016, and levels that had not been seen for many years. The surveys also indicate rising sales figures and investment, if more moderate than the previous year. In contrast, businesses in commerce were less optimistic, with a less favourable opinion of business activity than in 2016 and, moreover, accompanied by a slight downturn in sales and stagnation in investment.

The finance subsector was the branch of services that saw the least favourable trend, as had already occurred in 2015 and 2016. Official GDP figures in 2017 show a slight increase in GVA in the subsector Financial, real estate, professional and technical activities, specifically 0.5%, although this is an improvement in comparison with the declines of the previous two years. The weakness of activity was seen in reductions in gross lending to customers and deposits, which resulted in a decline in profits in the banking sector, for the fourth consecutive year, and a cut in employment in the whole financial and insurance sector. It should be said that these figures need to be viewed within the special context that marked the sector from 2015, both due to the bank Banca Privada d'Andorra being put into administration by the Andorran National Institute of Finance (INAF), ending with the resolution of the entity, and the transformation of the sector to adjust to international transparency and cooperation standards.

Regarding the public sector, its contribution to activity in 2017 was more favourable than the previous year, thanks to the implementation of a less restrictive fiscal policy by both the central and Comú governments. So, both operating costs and real investment showed a more positive trend than in 2016, with increases in aggregate data for both levels of government, of 4.3% and 19%, respectively. In parallel, fiscal pressure fell seven tenths to 24.5%, after reaching a historic high in 2016. Altogether, this resulted in a decline in the public surpluses of both the central and Comú governments (to 0.3% and 1.2% of GDP, respectively).

The prospects of the Andorran economy for 2018 are still moderately positive. So, the results of the Chamber's surveys indicate continued expansion within relatively modest but quite robust levels. By sectors, the positive trend is expected to continue to be led by services, especially those linked to tourism, together with a gradual recovery in building activities. In contrast, according to the same surveys, industry and commerce will maintain more modest behaviour, in line with 2017. In all three sectors, positive replies exceed negatives on the trend in business activity and investment for 2017, the difference being more notably favourable in the case of hotel activity and slighter in the case of commerce.

It can also be expected that the external environment will continue to boost Andorran economic activity in 2018, considering the predicted good performance of the Spanish economy, and that of the European economy to a large extent, already confirmed in the first half of this year. As a result, it is expected that Andorra's economy will see GDP growth in 2018, for the sixth consecutive financial year, not far from the level in 2017. This is indicated by the GDP data for

the first quarter of 2018, which show Andorran year-on-year real economic growth of 2%, six tenths more than one year before, but seven tenths less than the previous quarter.

The trend in the main available indicators of activity for the first few months of 2018 also show continued economic growth, within moderate levels. In effect, a generalised upward trend can be seen although, in the case of some key indicators, this is less intense than in the previous year. In particular, a slowdown in growth in imports until June and numbers of tourists until May was seen, plus deceleration in car registrations. In contrast, employment was very dynamic until April, stronger than in the same period of 2017, thanks to the boost from services, and there was also a notably positive change in the financial sector and construction. The strong growth in imports of building materials until June was important, highlighting the recovery that this sector is experiencing.

In summary, an overview of the first few months would lead us to believe that the Andorran economy will continue to grow throughout 2018. This growth will continue to be driven by the tourism sector, thanks to continued dynamism in the Spanish and European economies, and will be favoured by a growing contribution from construction and a slowly recovering financial sector.

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, reaching its twenty-third edition this year. 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 central and Comú governments and CASS 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.

Miquel Armengol Pons

President



The external environment of the Andorran economy

I. The international economy

1. The main features of economic development in 2017

In 2017, world economic growth surpassed expectations with the best trend since 2011. Moreover, growth was synchronised between advanced and emerging regions, which had not occurred for seven years. The driving factors were: (i) monetary policies, which are still

expansionary despite rising interest rates in the US; (ii) fiscal easing through the reduction of interest payments and increase in tax revenues; (iii) the upturn in investment; (iv) the favourable trend in financial markets, and (v) the sudden recovery in world trade in goods and services, which more than doubled from the previous year (5.1% in 2017 compared with 2.2% in 2016).

The world economy grows at the fastest rate since 2011, driven by the recovery in investment and world trade.

The fact that the risks that threatened growth at the beginning of the year did not materialise, such as a hard landing of the Chinese economy, the impact of Brexit or the effect of the gradual rise in US interest rates on emerging economies, also favoured world growth. In the political arena, it is notable that Trump's rise to power in the US administration did not negatively affect the economy. On the other hand, international tensions increased with China and Russia due to the trade war, and also in Israel and Palestine due to the US embassy transferring to Jerusalem in May 2018. In Europe, the risk of increasing populism did not materialise either in France, where Macron won in 2017, or in Germany, where Angela Merkel re-emerged as Chancellor.

As a result, in 2017, the rate of growth of the world economy accelerated to 3.7%, five tenths higher than in 2016, according to International Monetary Fund (IMF) estimates in July 2018.

Growth was synchronised between advanced and emerging regions.

The acceleration in world growth can be explained by the increased rate of growth in both developed economies, going from global growth of 1.7% in 2016 to 2.4% in 2017, and emerging and developing economies, growing at a rate of 4.7% in 2017, three tenths higher than in the previous year.

Emerging and developing countries were favoured by the emergence of Brazil, Russia and Argentina from recession, and the gentle increase in oil prices that boosted the economies of exporting countries. China and India were the countries with the highest rates of GDP growth: China grew more than the previous year thanks to the impetus from domestic demand, whereas growth decelerated in India due to the effects of abolishing the highest-value banknotes to tackle corruption and introducing a consumption tax.

As for the advanced countries, the Eurozone was the surprise of the year by growing above expectations and surpassing the GDP growth rate of the USA (2.4% compared with 2.3% in the US). Japan also almost doubled its growth of the previous year (1.7% compared with 1%).

Regarding monetary policy, interest rates in the US reached a range of 1.25-1.5% at the end of the year, after four rate increases (one in December 2016 and three more in 2017).

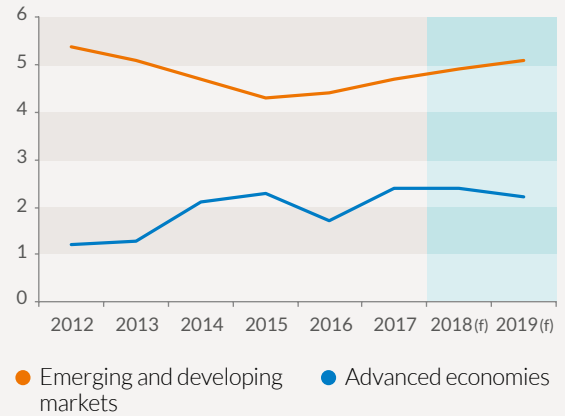
Interest rates rose in the USA and remained stable in the Eurozone.

The Federal Reserve is expected to make additional rises in interest rates in 2018 on top of those made in March and June 2018, which put the new range of interest rates at 1.75-2%. The increases were made gradually to avoid provoking sudden changes in the financial markets. This policy of raising interest rates was accompanied by a reduction in the Federal Reserve balance, after the bond-buying programme was finalised in 2014.

In the Eurozone, official interest rates are still at 0% and are not expected to rise until autumn 2019, if the economic forecasts are confirmed. Equally, since 1 January 2018, the European Central Bank halved the volume of bond-buying (30,000 million euros per month compared with 60,000 million previously), according to the decision taken by the ECB Council in October 2017. In June 2018, the ECB again decided to halve bond-buying (to 15,000 million euros per month) and finally abandon this policy in December 2018, unless inflation is very low or economic prospects worsen. In total, the special asset-buying measures in the Eurozone (quantitative easing) will have been in place for more than three and a half years.

GLOBAL GDP GROWTH
Annual variation rates at constant prices, in %

Chart 1.1

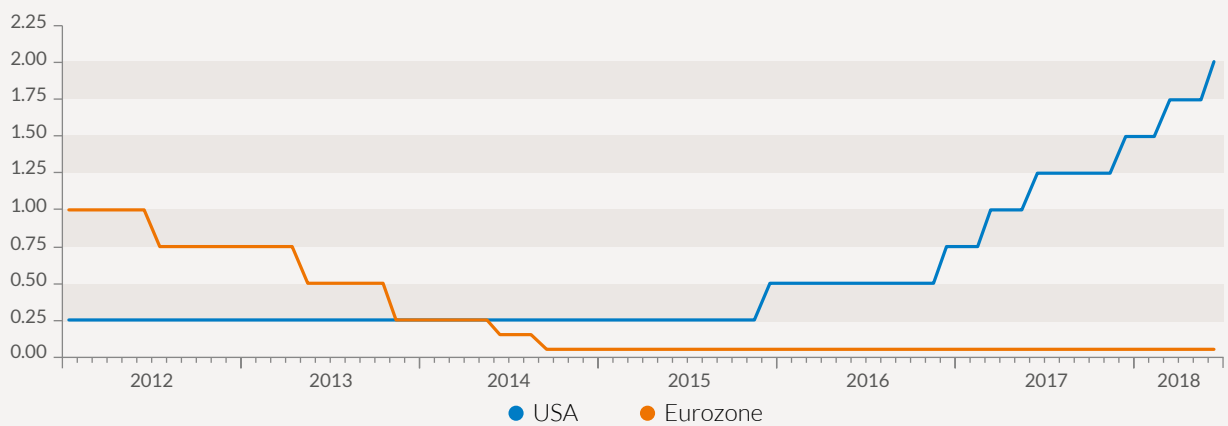


f: IMF forecasts (July 2018).

Source: IMF.

OFFICIAL INTEREST RATES IN THE US AND EUROZONE - As %

Chart 1.2



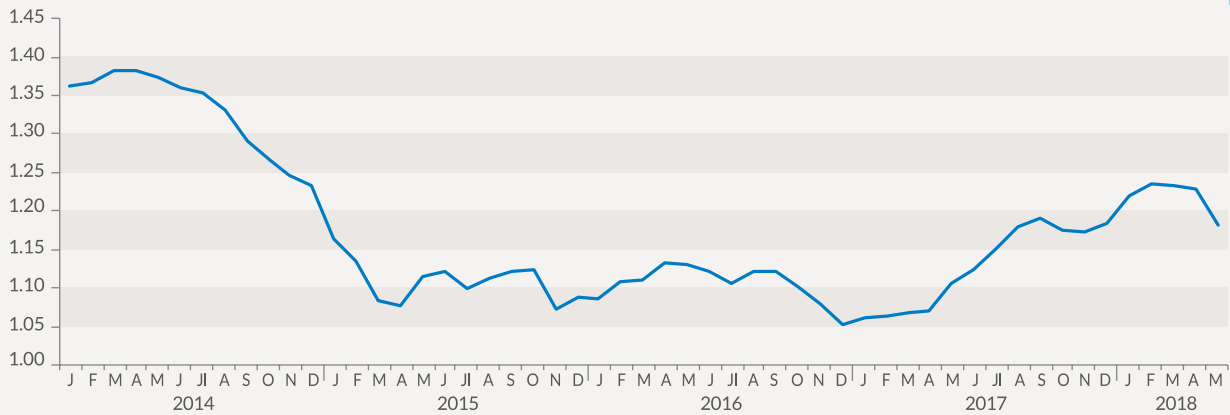
Source: Federal Reserve and ECB.

Although the US has higher interest rates and more favourable economic prospects than the Eurozone – especially after the tax cuts approved by the Trump administration in December 2017 – the dollar depreciated against the euro throughout 2017, breaking the trend to appreciate that marked the 2014-2016 period. The dollar/euro market price reached 1.184 in December 2017, 12% higher than in December 2016 (1.054 \$/€). In the Eurozone, euro appreciation made

The dollar depreciated and the interest rate rose in the US.

\$/€ EXCHANGE RATES

Chart 1.3



Source: BCE.

European exports more expensive, but dynamic international trade managed to offset that effect. In contrast, the revaluation of the European currency cheapened energy imports, helping to keep inflation down.

In 2017, oil prices continued to rise, especially in the second part of the year, and accentuated more in the first few months of 2018. Specifically, between June 2017 - when the price of a barrel reached the yearly minimum of 47.5 dollars - and December 2017 - when it reached a maximum of 64 dollars - the cumulative increase was 35%. This rise is added to that of the previous year (45%). Equally, in the Eurozone, the impact of rising oil prices was softer due to the counter-effect of euro appreciation. The increase in crude oil prices in 2017 is the result, on the one hand, of a reduction in the production quota approved by OPEC and Russia; on the other hand, of lower production by Venezuela (the world's largest producer) and, lastly, of an increase in global demand. Another factor was added in 2018 - the escalating tension between Iran and the US after President Trump decided to pull out of the nuclear agreement signed in 2015, with the opposition of the main European economies.

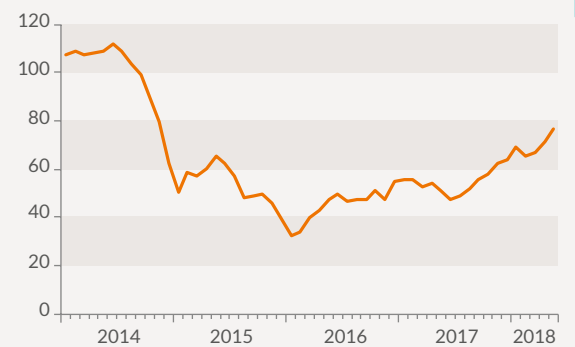
In 2017, strong economic growth and rising prices of oil and raw materials pushed up the prices of goods and services throughout the economic areas. Average inflation of developing countries rose from 0.8% in 2016 to 1.7% in 2017, but is still below the goal of the main central banks. Despite this general trend, some countries have already reached or surpassed 2%, such as the United Kingdom, the USA and Spain. In Japan, prices saw an increase of 0.5%, contrasting with the deflation of the previous year. Global inflation in emerging and developing countries was 4% (4.3% in 2016).

Stability returned to capital markets in 2017.

The IBEX-35 of the Spanish stock market rose 7.4% (between December 2016 and December 2017), after two continuous years of gains, a similar trend to the one seen in the European index, Euro Stoxx (6.5%). The revaluation was greater in the USA, where the Dow Jones index closed the year with gains of 25%, and in Japan, where the Nikkei rose 19.1%.

OIL PRICES - \$ per barrel of Brent

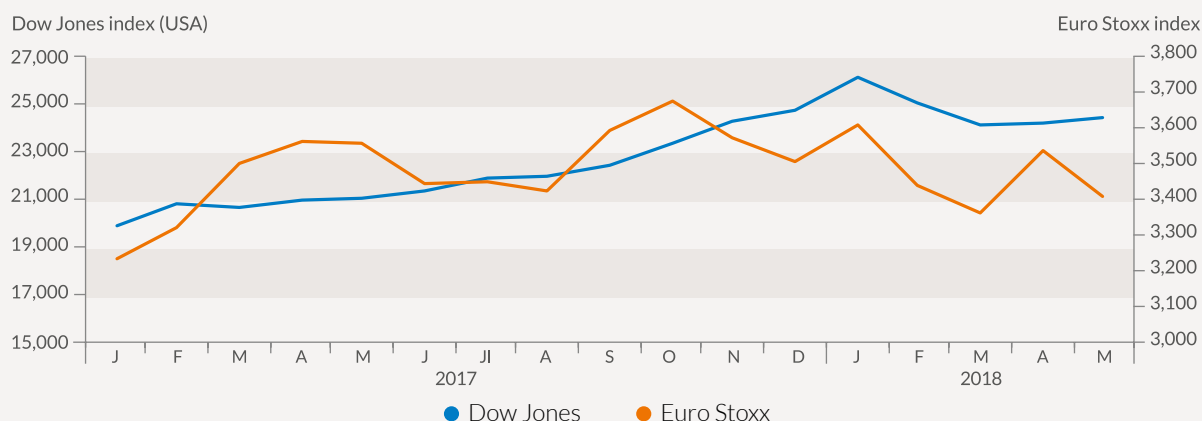
Chart 1.4



Source: Energy Information Administration, of the US Government.

STOCK MARKET INDEX IN THE USA AND EUROZONE

Chart 1.5



Source: ECB and Federal Reserve.

The economic and financial stability experienced throughout 2017 resulted in risk premiums – which measure excess return with the German bond – being low, especially in peripheral countries with a higher risk of public debt (Greece, Italy, Portugal and Spain). The risk premium halved in Greece (from 669 basis points in January 2017 to 327 basis points in January 2018), and also experienced a falling trend in Portugal, which ended the year practically converging with the Italian risk premium (around 140 basis points). In Spain, the risk premium stood below 100 basis points in January 2018. In contrast, in Italy, the political crisis in May 2018 caused the risk premium to rise above 200 basis points.

2017 was characterised by economic and financial stability, with low volatility.

12

IMF ECONOMIC OUTLOOKS FOR THE GLOBAL ECONOMY

Table 1.1

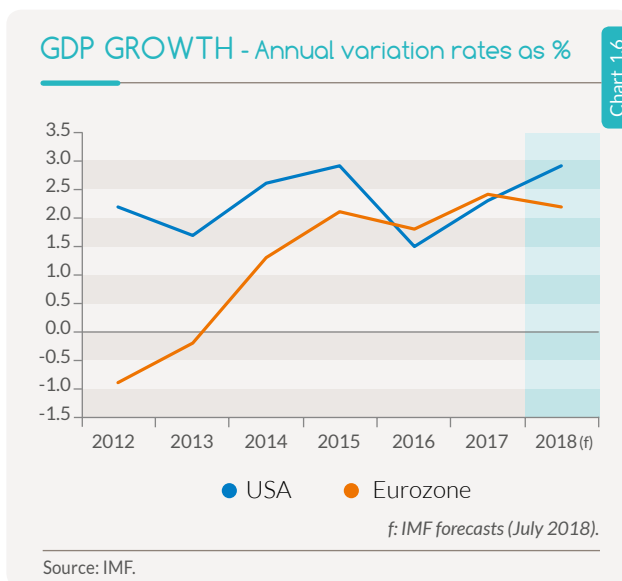
	2016	2017	FORECASTS	
			2018	2019
Global GDP	3.2	3.7	3.9	3.9
Advanced economies	1.7	2.4	2.4	2.2
USA	1.5	2.3	2.9	2.7
Eurozone	1.8	2.4	2.2	1.9
Germany	1.9	2.5	2.2	2.1
France	1.1	2.3	1.8	1.7
Italy	0.9	1.5	1.2	1.0
Spain	3.3	3.1	2.8	2.2
Japan	1.0	1.7	1.0	0.9
United Kingdom	1.8	1.7	1.4	1.5
Canada	1.4	3.0	2.1	2.0
Emerging and developing countries	4.4	4.7	4.9	5.1
Sub-Saharan Africa	1.5	2.8	3.4	3.8
Emerging European economies	3.2	5.9	4.3	3.6
Commonwealth of Independent States	0.4	2.1	2.3	2.2
Russia	-0.2	1.5	1.7	1.5
Developing Asia	6.5	6.5	6.5	6.5
India	7.1	6.7	7.3	7.5
China	6.7	6.9	6.6	6.4
Middle East and North Africa	5.0	2.2	3.5	3.9
Latin America & Caribbean	-0.6	1.3	1.6	2.6
World trade (goods and services)	2.2	5.1	4.8	4.5

Source: IMF, July 2018.

2. Developments in the major advanced countries

2017 was marked by a rising trend in economic growth that was practically generalised in all the major developing countries. This dynamism was driven by the recovery in domestic demand and the upswing in world trade. Within domestic demand, whereas growth in private consumption remained the same as the previous year, investment picked up, to become the GDP component with the most positive trend in 2017. Investment benefitted from both the improvement in economic prospects and the increase in financial wealth and low interest rates.

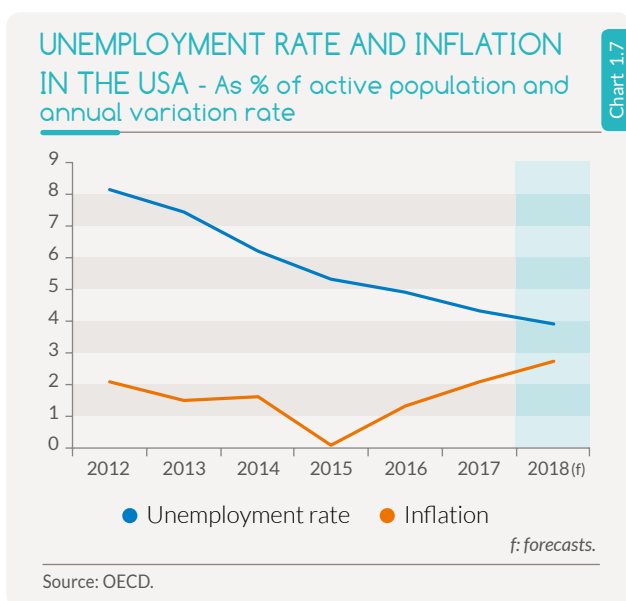
In 2017, the two main economic areas, the USA and Eurozone, saw very similar GDP growth rates (2.3% and 2.4%, respectively). GDP accelerated eight tenths against the previous year in the case of the US economy, and six tenths in the Eurozone. Also notable was the accelerated growth in Canada and Japan, while GDP in the United Kingdom slowed one tenth to 1.7%, as Brexit began to have an impact.



2.1. USA

The US economy is still one of the main forces behind global expansion and therefore belies the doubts about its sustainability. In 2017, growth was 2.3%, based on rising business investment which was due, to a large extent, to the recovery in the energy sector.

The contribution to growth from foreign demand was negative (-0.2 points) and equal to the previous year. Dollar depreciation, which favoured exports, and falling oil imports due to the development of fracking, meant that the foreign trade balance of the US economy did not worsen, despite the economic acceleration. So, in 2017, the deficit in the current account balance remained at 2.4% of GDP, for the third consecutive year.



The favourable trend in the US economy resulted in a continuous improvement in the results of the labour market. The annual rate of growth in employment was 1.3%, putting the unemployment rate at 4.3% in 2017, a historic low that can be considered full employment.

US inflation ends up rising, in a context of full employment.

For its part, inflation followed the trend led by oil prices throughout the year, the first part of the year marked by a downward trend from the maximum reached in February (2.7%), and the second part of the year showing a

slight upward trend to reach 2.1% in December. The wage increase also encouraged inflation, with wages seeing an increase of 1.7% in 2017, compared with 1% in the previous year, in a context of full employment. On yearly average, consumer prices accelerated from 1.3% in 2016 to 2.1%, standing close to the goal of 2%. The increase in inflation favoured the Federal Reserve's monetary policy of gradually raising interest rates.

Finally, the greater dynamism in the US economy boosted the adjustment of the public deficit that had slowed in the previous year. The government accounts balance went from 5% of GDP in 2016 to 3.6% in 2017, an adjustment that contrasts with the increase in deficit that occurred in the previous year.

Box 1.1

THE US TAX REFORM

On 22 December 2017, the US Government signed the *Tax Cuts and Jobs Act*, the law that embodies the tax reform pushed by President Trump. The approved cuts in taxes, with a major cost in terms of revenue, represent the widest-ranging reform of the US tax system since 1986 and are intended to favour growth, job creation and domestic investment, discouraging the delocalisation of activities and the advantage of multinational companies abroad.

The effects of the reform on personal income tax are not as wide-reaching as initially planned, and valid for a limited period until 2025. However, it involves a cut in tax rates and the incorporation of legislative changes in the regulation of exemptions and deductions. The most important changes occur in corporate tax: firstly, a substantial reduction in the tax rates to 21%. This percentage, added to the federal corporate tax applied on average by the different states, results in the average tax for the whole country falling from 40% to 25%. This new tax rate is close to the average rate for OECD countries, which is also 25%, but below that of countries such as Germany or France. The second major change in corporate tax is the adoption of measures to

move towards a system of taxing company profits, applying the territorial principle. According to this new principle, dividends from subsidiaries abroad are exempt of tax and may be repatriated without incurring tax, although a transitional tax has been established for profits accumulated by subsidiaries abroad between 1986 and 2017. This change led to news such as Apple's announcement that it must pay 38,000 million dollars' tax on profits held abroad and that it will repatriate about 200,000 million dollars. Equally, to incentivise national production, a tax incentive for exports was approved, so income from the provision of goods and services to individuals and businesses outside the US will incur a reduced tax rate of 13.12%.

According to the simulation made by the Tax Foundation, the economic impact of the tax reform will be substantial because, in static terms, the drop in revenue will be 1.4 billion dollars over the period 2018-2027, of which 1.3 relate to personal income tax and 373,000 million to corporate tax. Now, the estimated impact of the reform on economic growth will also be notable, with 0.44% in expected GDP growth in 2018 and 2.86% over the next decade.

2.2. Eurozone

In 2017, the dynamism of the Eurozone economy, consisting of 19 member countries, was surprising. Growth accelerated in the central nucleus of countries, especially in Germany and France, and was also notable in the countries that most suffered the recession (Ireland, Spain, Portugal and even Greece, which emerged from recession in 2017).

Surprising dynamism of the Eurozone economy in 2017.

GDP growth was 2.4% for the whole year, according to the IMF and Eurostat, six tenths more than the growth seen in the previous year, and the most positive rate since 2007.

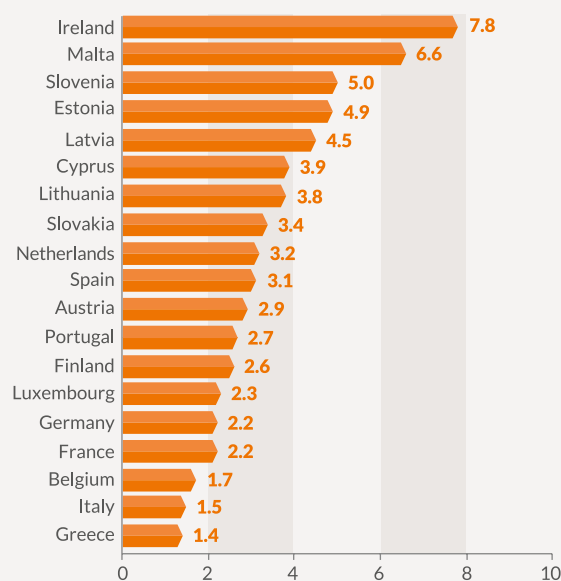
This growth was based on three factors: low interest rates, an easing of the restrictive fiscal policy, and growth in world trade which offset the negative effect of euro appreciation on European exports.

By components, the recovery in the Eurozone was the result of the improvement in foreign demand, as the rate of growth in domestic demand slowed three tenths to 1.7%, especially in private consumption. The increase in public consumption also slowed to 1.2% on annual average. The same occurred with investment which, despite a quite positive result, saw the rate of growth slow from 4.6% to 2.9%. In contrast, foreign demand made a positive, growing contribution to the trend in GDP. This trend was the result of accelerated growth in exports, which grew 5.1%, 1.7 points more than the previous year. Growth in exports, based on the recovery in foreign demand, surpassed the acceleration in imports (4.3%, half a point more than the previous year), favoured by the strength of domestic demand. This helped to stabilise the Eurozone current account surplus at about 4% of GDP in 2017, the highest achieved in recent decades, according to the OECD.

In 2017, the economic recovery helped to increase employment, but the unemployment rate is still high. Specifically, employment rose by an annual 1.6%, surpassing growth in the previous year by two tenths. This enabled a reduction of the unemployment rate from 10% in 2016 to 9.1% in 2017, the lowest since 2008 but still far from the minimum achieved in 2007 (7.6%) which, according to the European Commission's forecasts, could be achieved in 2019. For their part, unit labour costs grew 0.7% as a result of wage increases of 1.6% per worker and an increase in productivity of 0.8%. Now, real labour costs, after discounting the GDP deflator, fell 0.3%, allowing the Eurozone economy to gain competitiveness in 2017.

Despite the upswing in the economy, prices remain at abnormally low levels for the cyclical situation of the economy. The European Commission indicates that it is vital to improve production and wages to encourage inflation. Specifically, prices started the year by reaching a maximum of 2% in February and ended with an increase of 1.4% in December. On annual average, inflation was 1.5%, compared with 0.2% in the previous year. All the Eurozone economies saw positive annual rates of inflation but only six crossed the threshold of 2%. Inflation in the countries forming the European nucleus remained moderate, for example in Germany (1.7%), France (1.2%) and Italy (1.3%). The greatest rises in prices were seen in Eastern European countries, such as Lithuania (3.7%), Estonia (3.7%) and Latvia (2.9%).

GDP GROWTH IN EMU COUNTRIES IN 2017 - Annual variation rates, as %



Source: European Commission.

Prices remain at abnormally low levels for the cyclical situation of the economy.

Chart 18

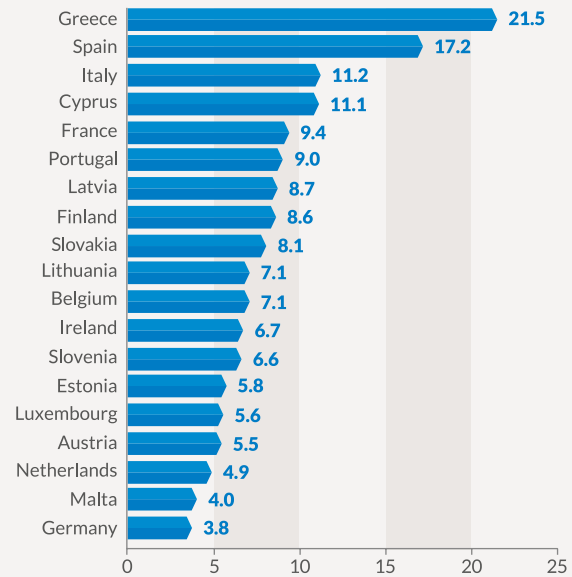
Monetary policy was influenced by the described context of economic recovery and low inflation. So, with the goal of deterring the deflationary risk and boosting the economy, the ECB agreed to extend the bond-buying measure until September 2018 and keep the official interest rate at the minimum of 0.05%, at least until after summer in 2019.

In 2017, the global public deficit of the Eurozone fell to 0.9% of GDP.

Finally, fiscal policy continued to be restrictive but not as contractionary as the previous year. The global public deficit of Eurozone member countries fell from 1.5% of GDP in 2016 to 0.9% in 2017. Yet again, the reduction in the deficit can be explained by the adjustment in spending's share of GDP (47.1%) rather than an increase in revenue, as the latter's share of GDP has remained practically constant (46.2%). The EMU countries with a public accounts surplus are Germany, Cyprus, Lithuania, Malta, Netherlands, Luxembourg and Greece. In contrast, the member countries with the highest public deficits are Spain (-3.1% of GDP), France (-2.6%) and Italy (-2.3%). The public debt-to-GDP ratio maintained its falling trend in 2017 for the whole of the Eurozone, to reach 88.8% of GDP, due both to the increase in GDP and the lower level of deficit and low cost of finance.

UNEMPLOYMENT RATE IN EMU COUNTRIES IN 2017 - As % of active population

Chart 1.9



Source: European Commission.

3. Developments in the major emerging and developing countries

In 2017, emerging and developing economies grew at the strongest rate since 2014, thanks to sustained capital flows towards those countries, favoured by economic optimism and abundant liquidity.

Asian emerging and developing countries are still the region with the highest growth (6.5%), despite deceleration in growth in India (from 7.1% to 6.7%), partly due to the introduction of a tax on consumption. In contrast, the Chinese economy saw 6.9% growth, two tenths more than the previous year, thanks to growth in foreign demand.

In 2017, Latin America emerged from recession with modest growth of 1.3%. Within this region, Brazil's performance was very positive, since it benefitted from an increase in exports and the recovery in domestic demand after eight consecutive quarters of falling GDP. Argentina was also able to emerge from recession thanks to financial and economic stability but, in May 2018, had to face a serious devaluation of its currency due to the rise in interest rates in the US. Mexico, for its part, maintained its moderately positive growth, despite the uncertainty associated with renegotiation of the NAFTA agreement with the USA and Canada. In contrast, Venezuela finds itself in a critical situation from an economic and humanitarian point of view, with hyperinflation and insolvency, despite being the country with most oil reserves in the world.

Argentina, Brazil and Russia emerge from recession in 2017.

In the Middle East and North Africa, the rate of growth was 2.2%, less than half that of the previous year. These economies felt the fall in oil prices that occurred in the first half of the year, and were also affected by the supply restriction agreed by OPEC, and by geopolitical conflicts in the region. However, a better trend is expected in 2018, due to the rise in oil prices in the first few months of the year.

Finally, the group of countries that showed the second highest rate of growth, after the Asian economies, was that of emerging countries of Europe (5.9%). On the European continent, Russia's emergence from economic recession is notable (1.5% in 2017 compared with -0.2% in 2016), benefitting from an increase in general revenue from oil exports and the political conflict in the Middle Eastern region.

4. Prospects

The first few months of 2018 were marked by a slowdown in growth in the Eurozone, an acceleration in oil prices, continuation of the policy of progressive monetary normalisation in the USA and Eurozone, an increase in tension in the Middle Eastern conflict, and episodes of market instability in February and March, especially in the USA.

As for economic activity, the world is in a globally positive moment with outlooks favoured by the impetus from tax cuts in the US, market optimism and financial conditions that remain favourable. However, the risks of a downturn have intensified in the last few months, especially from growing trade tensions and the increase in oil prices. In fact, the IMF July Outlook maintained the prognosis of world growth at 3.9% for 2018 and 2019, but lowered expected growth for Japan, the United Kingdom and the Eurozone, due to weakening activity at the beginning of 2018.

Lower growth forecasts for Japan, the Eurozone and the United Kingdom.

The IMF predicts that advanced economies will grow 2.4% in 2018 (the same as in 2017), a prognosis that is four tenths higher than it made in October 2017, above all from the

direct and contagion effect of US expansionary fiscal policy. These prospects are globally positive, but the IMF also warns that, in most countries, the currently favourable rates of growth will not last beyond 2020.

In 2018, the emerging and developing market economies will maintain their rate of acceleration and grow 4.9%. Although the high rate of growth is mostly due to the uninterrupted economic dynamism of emerging Asian economies, the predicted upturn in growth will also be a consequence of more favourable prospects in countries exporting raw materials, after three years of very weak economic activity.

In the US, forecasts indicate that growth will rise from 2.3% in 2017 to 2.9% in 2018 (0.6 percentage points above the October forecast). The upturn relates to stronger activity than expected in 2017, firmer foreign demand and the macroeconomic effect of the tax reform passed in December 2017, especially the cuts in taxes paid by businesses and the temporary authorisation to account for investment wholly as expenditure, which is expected to stimulate short-term activity. The upturn also takes into account the increase in public spending after the bi-party budget deal agreed in February 2018. It is expected that the changes to fiscal policy will stimulate growth until 2020 but, beyond that date, the increase in the deficit from the tax reform will need a greater budget adjustment, which will offset part of the greatest growth achieved in previous years.

In the first quarter of 2018, the US economy saw positive quarter-on-quarter GDP growth that was similar to the previous quarter (0.5%), enabling annualised growth of 2.2% (2.9% in the previous quarter). Private consumption lost impetus but, in contrast, non-residential investment and exports gained impetus. There was also a slowdown in the rate of import growth, partly due to lower consumption and partly due to greater restrictions on imports.

The unemployment rate in the US reaches 3.9%, a historic low.

In the first four months of 2018, cumulative year-on-year employment grew 1.5% (almost 800,000 new jobs), and the unemployment rate fell to 3.9% in April, the lowest of the

series since the 1960s. This trend favoured an improvement in consumer confidence, which rose above the historical average. Inflation, on the other hand, rose in the first five months. In April, it reached 2.5% due to rising oil prices and also greater wage pressure, due to the low unemployment rate, demonstrated by the increase in underlying inflation (to 2.1% in April). In this context of full employment and rising inflation, the Federal Reserve decided to raise interest rates again in March and June 2018, putting them in the range of 1.75-2%. Moreover, it is expected to make two or three more increases over the year.

In the case of the Eurozone, the IMF predicts that growth will decelerate two tenths to 2.2% in 2018, then reach 1.9% in 2019, due to the weakening of the German, French and Italian economies in the first quarter. Mid-term, Eurozone growth is expected to reach 1.4%, affected by lower productivity in a context of weak reforms and unfavourable demography.

By countries, the European Commission, in its report in April 2018, forecasts an increase in Germany's GDP of 2.3% (2.2% in 2017) and an increase in French GDP of 2% (2.2% in 2017).

The first few months of 2018 were marked by a slowdown in growth in the Eurozone.

For its part, Spain is still one of the economies that will grow most in 2018, although its rate of growth will slow two tenths against the previous year (2.9%). The labour market will continue to recover, which will enable the unemployment rate to fall seven tenths in the Eurozone, to 8.4% in 2018. The easing of the goals for reducing public deficit will also contribute to the economic recovery. The Commission predicts that the public deficit will continue to shrink but the adjustment will slow, reaching 0.7% of GDP in 2018 (0.9% in 2017).

Now, Eurozone growth slowed in the first quarter. The quarterly increase in GDP went from 0.7% in the fourth quarter of 2017 to 0.4% in the first quarter of 2018. This was due to the generalised slowdown that occurred in the main European countries, starting with Germany (which grew 0.4% in the first quarter compared with 0.5% in the previous quarter), followed by France (which grew 0.2% in the first quarter compared with 0.7% in the previous quarter). Outside the Eurozone, the slowdown in growth in the United Kingdom was notable (0.2% in the first quarter compared with 0.4% in the fourth quarter of 2017). In contrast, growth remained strong in Spain in the first quarter (0.7%, the same as the previous two quarters). Various factors could explain the economic slowdown in the Eurozone: the long negotiations to form a government in Germany, which caused a decline in public spending, combined with tensions in the labour market due to a lack of qualified staff; the long period of continued growth which may be adjusted to reach more sustainable levels; the indirect impact of Brexit on the United Kingdom; the protectionist threat from the US which may harm European exports, and lower foreign demand due to a weakening in the global recovery and the delayed effect of euro appreciation.

Eurozone inflation remained moderate in the first four months of the year (1.3% on average), but the forecast is that prices will accelerate in 2018 as a whole, as the impact of rising oil prices transfers to consumer prices.

Oil prices pick up and the euro depreciates in May 2018.

In the first four months of 2018, the tendency for the euro to appreciate slowed, with the dollar/euro exchange rate stabilising, but there was a sudden depreciation of the European currency in May. In 2018, the European Central Bank will continue its announced reductions in the volume of asset-buying from September, but no changes in the benchmark interest rates are expected, currently at 0%.

In Japan, it is expected that GDP growth will slow to 1% in 2018 (after the solid result of 1.7% in 2017, above the trend) before decelerating even more to reach 0.9% in 2019, according to the IMF. The upturn in the growth forecast is the result of the improved prospects in foreign demand, the increase in private investment and the supplementary budget for 2018. However, mid-term prospects for Japan are still weak, above all due to contraction in the labour force. The yen suffered no notable changes and the benchmark interest rates are expected to remain around zero until mid-2019.

In the first quarter of 2018, the Japanese economy weakened. In comparison with the fourth quarter of 2017, GDP contracted 0.2%, after growing at a rate of 0.1% in the three previous months. This meant a year-on-year

contraction in the economy of -0.6% in the first quarter of the year, the first fall in activity since 2015, after a period of eight consecutive expansive quarters, forming the longest continuous period of growth since the end of the 1980s. The fall in activity in Japan in the first quarter of the year reflects the impact of falling domestic demand, with a year-on-year drop of 0.9%, including a fall of 1.2% in private consumption and a drop of 8.2% in private residential investment.

In this context, the Bank of Japan maintained the interest rate policy that was introduced in March 2016, consisting of a three-level system: existing deposits on the date of implementing

Downturn in the Japanese economy in the first quarter for the first time since 2015.

OECD ECONOMIC PROSPECTS FOR THE MAIN DEVELOPED COUNTRIES

Table 1.2

	GDP % annual variation			INFLATION ⁽¹⁾ % annual variation			UNEMPLOYMENT RATE ⁽²⁾ % active population			CURRENT ACCOUNT BALANCE % of GDP			PUBLIC DEFICIT % of GDP		
	2017	2018f	2019f	2017	2018f	2019f	2017	2018f	2019f	2017	2018f	2019f	2017	2018f	2019f
	USA	2.3	2.9	2.8	2.1	2.7	2.3	4.3	3.9	3.6	-2.4	-2.8	-3.1	-3.6	-5.5
Japan	1.7	1.2	1.2	0.5	1.2	1.5	3.7	3.8	3.7	4.0	3.7	4.1	-3.5	-3.0	-2.5
United Kingdom	1.8	1.4	1.3	2.7	2.6	2.2	4.4	4.5	4.6	-4.1	-3.1	-2.5	-1.8	-1.4	-1.3
Eurozone	2.5	2.2	2.1	1.5	1.6	1.8	9.1	8.3	7.8	4.0	4.0	3.9	-0.9	-0.6	-0.4
Germany	2.5	2.1	2.1	1.7	1.7	2.0	3.8	3.4	3.3	8.1	8.3	7.9	1.3	1.5	1.5
France	2.3	1.9	1.9	1.2	1.9	1.5	9.4	8.7	8.3	-0.6	-0.5	-0.4	-2.6	-2.3	-2.5
Spain	3.1	2.8	2.4	2.0	1.6	1.5	17.2	15.5	13.8	1.9	1.7	1.7	-3.1	-2.4	-1.5
OECD	2.5	2.6	2.5	2.0	2.2	2.3	5.8	5.4	5.1	0.4	0.2	0.1	-2.0	-2.6	-2.7

(1) For the OECD, the private consumption deflator has been used.
(2) Unemployment rate calculated with national definitions, not harmonised.
f: forecasts.

Source: OECD, May 2018.

the modification will retain the rate of 0.1%; 0% will be applied to mandatory reserves and specific funds relating to support programmes, and other deposits will bear a negative interest rate of 0.1%.

The economic situation is globally positive but the risks are increasing.

In summary, despite the fact that aggregate economic figures are good and the markets are optimistic, the current impetus is not guaranteed. Risks have increased since the start of the year. Low inflation has enabled the process of gradual withdrawal of stimuli to be gentle, but the new context of rising inflation due to rising oil prices could accelerate the process of raising interest rates and generate tensions in the financial markets and in countries with dollar-denominated debt, as occurred in Argentina. Other risks are the shift toward protectionist policies that could harm international trade; the US trade war with China and the worsening geopolitical tensions in the Middle East after Trump decided to break the nuclear agreement with Iran. The rising trend in oil prices is also a threat, above all to major oil-importing countries, such as Spain. It should be remembered that in May, prices reached an average of 77 dollars/barrel, 50% higher than the price one year before.

The French economy

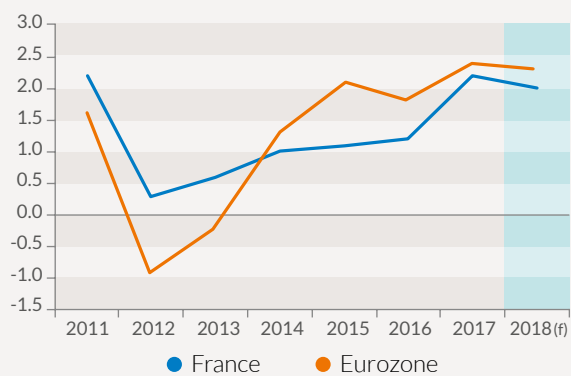
1. The main features of economic development in 2017

The French economy grew in 2017, at the fastest rate in the last six years. According to the French National Institute of Statistics (INSEE), annual GDP expanded 2.2% compared with 1.2% in the previous year. Despite this upswing, the French economy is still growing slower than the Eurozone as a whole (2.4% in 2017). The increase in GDP was basically driven by dynamic investment and the acceleration in exports, although public consumption also made a positive contribution. This varied basis of expansion means that it may be more sustainable in future.

In 2017, the French economy grew at the fastest rate in the last six years.

The driving factors behind the growth of the French economy were the favourable international environment, low interest rates, oil prices - which remained at historically low levels in 2017 - and the increase in economic confidence after the presidential elections in May 2017. The new President of France started a phase of economic reforms and commitment to relaunching the European Union, starting with a historic reform of French labour legislation at the end of the year.

GDP GROWTH IN FRANCE AND THE EUROZONE - Interannual variation rates, as %



Source: European Commission.

Despite the economic acceleration, the level of per capita GDP in 2017, compared with the European average for purchasing power parity (EU=100), fell to 104, compared with 108 achieved in 2013. This indicates that French per capita income is 4% higher than the European average,

but also that it was 8% higher three years earlier. It should be noted that the crisis did not affect the level of real convergence of France with the EU, as it had a very similar index in 2008 to 2014 but, on the other hand, divergence has been occurring since the start of the economic recovery.

Box 2.1

ECONOMIC REFORMS PASSED BY MACRON'S GOVERNMENT IN 2018⁽¹⁾

Measures to increase personal income

- Gradual elimination of the municipal housing tax for 80% of French people by 2020.
- Reduction in social contributions.
- Increase in the minimum retirement pension: the current amount (€803) will increase to €903 by 2020.
- Increase in adult disability benefits (AAH): currently 1.1 million individuals receive €811 under these benefits. It is planned to increase this amount to €860 on 1 November 2018, and to €900 on 1 November 2019.

Measures to effectively reduce unemployment and encourage employment

- Increase in the “activity premium”: this incentive, in the form of benefits, will rise €20/month from 2018 to €80/month by the end of a five-year period. It is intended for people on low incomes.
- Change in focus of employment policy towards professional training: the skills investment plan will unblock finance worth 14 million euros over a period of five years – only 1.5 million euros in 2018.

Measures to improve competitiveness

- Reduction in corporate tax: this currently stands at 33% in France, higher than the 25% European average. This gap will be closed within five years. From 2018, the rate will fall to 28% for all businesses on their first 500,000 euros profit.
- Replacement of the CICE (tax credit for competitiveness and employment) through a permanent reduction in social contributions paid by the employer: the CICE will be retained in 2018, reduced from 7% to 6% before being replaced in 2019 by a permanent reduction in employers' social contributions, directed especially at low wages.

Measures to encourage investment and innovation

- Introduction of a 30% fixed rate (UFP) on investment income in 2018 (dividends, capital gains, interest, etc.).

- Replacement, from 2018, of the solidarity tax on wealth (ISF) by a property tax based on the value of real property (IFI).

Measures to facilitate the ecological transition

- 20,000 million euros of the *Big Investment Plan* will be channelled over the next five years into policies to achieve zero net carbon emissions (renovating buildings to make them more energy-efficient, increasing renewable energy generation, etc.).
- Incentive to buy cleaner vehicles: all owners of petrol-engine vehicles registered before 1997 or diesel engines before 2001 can apply for €1,000 aid to buy a cleaner car, whether new or secondhand.
- Large-scale launch of the “energy coupon” (discount on the price of the energy bill): under trial in 2017, this scheme will be extended nationally on 1 January 2018. 4 million households will benefit, from €48 to €227/year, depending on individual household circumstances, with an average of €150/year.
- Harmonisation of the rates of diesel and petrol tax over 4 years.

Measures to revise housing policy

- Housing benefit reforms: the budget reserved for the personal housing allowance (APL), currently worth 18,000 million euros, will be cut to 17,000 million euros.
- Renewal of the *Pinel* scheme and extension of interest-free loans: the *Pinel* scheme to encourage buy-to-rent investment will be extended 4 more years, specifically in areas where demand exceeds supply.

Measures to support the armed forces, implementation of the law and efforts in security and justice

- Unprecedented increase in the armed forces budget.
- The justice system will have more resources, creating 1,000 more jobs from 2018.

(1) <https://www.gouvernement.fr/en/the-2018-finance-bill>

By components, economic growth in 2017 was led by domestic demand which – excluding stock variation – added 1.8 points to growth, slightly lower than the contribution in the previous year. All components of domestic demand had a positive performance. Nevertheless, while the rate of growth of private consumption decelerated from 2.1% in 2016 to 1% in 2017, public consumption remained around 1.3%. Household consumption points to the effect of the wage slowdown and adjustment in state benefits, despite the creation of jobs. Equally, the GDP component that was a major driving force behind activity in 2017 was investment, which grew 4.5%, compared with 2.8% in the previous year. Business investment benefitted from the improvement in the economic environment and the reforms passed by Macron, especially in the labour market, while family investment in housing was favoured by credit facilities, low interest rates and confidence in the economy.

In contrast, external demand shifted from a negative contribution of five tenths in 2016 to a positive contribution of one tenth in 2017, due to growth in exports of goods and services accelerating from 1.5% in 2016 to 4.5% in 2017, and overtaking imports (3% in 2016 and 4% in 2017). Unlike in previous years, the trend in French exports of goods and services was more positive than in the Eurozone, demonstrating that the loss of competitiveness that had been occurring for several years has slowed. In fact, in the fourth quarter of 2017, the foreign sector started to make a positive contribution to GDP, due to a major acceleration in exports combined with a slower increase in imports.

The reforms passed by Macron's Government begin to influence investment and consumption.

In 2017, the good performance of the trade balance helped to reduce the deficit in the current account balance by two tenths, to -0.6% of GDP, according to the OECD.

As for supply, in 2017, the ten sectoral branches saw a positive trend in gross value added, except for financial activities (-6.8%). The information and communications sector had the most positive trend (5.4%), followed by agriculture (4.8%), scientific and professional activities (4.6%) and commerce, transport and hotels and catering (3.6%). In contrast, industry saw slower growth of 1.5%, and construction was 2.4%. The other three branches of services (real estate, public administration and culture and recreation) saw variations of around 1% or less.

The upswing in the economy has enabled more net employment to be created than in any other year since the start of the recovery.

The upswing in the economy has enabled more net employment to be created than in any other year since the start of the recovery (276,000 more jobs in 2017, compared with 193,000 in 2016). Job growth benefitted from the better economic situation and the reductions in social contributions approved in 2014 and 2015, within the framework of the Responsibility and Solidarity Pact. In variation rates, growth in employment accelerated from 0.6% in 2016 to 1.1% in 2017, while the harmonised unemployment rate fell from 10.1% in 2016 to 9.4% in 2017 on annual average, according to the OECD.

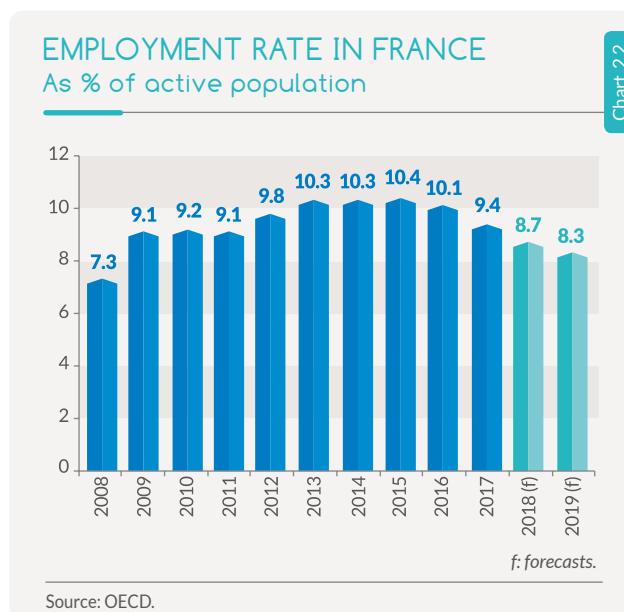


Chart 2.2

The progressive improvement in the labour market and the reduction of the unemployment rate meant that nominal wage increases were higher than in previous years (1.8% in 2017, compared with 1.0% in 2016). For its part, labour activity increased 0.8% and consequently, unit labour costs (ULC) grew 1% in nominal terms. In real terms (after discounting prices) ULCs only increased 0.2%, enabling French businesses to gain competitiveness.

Cuts in social contributions and the labour reform have created a more favourable environment for increasing employment.

The trend in consumer prices fell in the first half of the year and rose in the second half, following the trend in oil prices. On annual average, harmonised inflation was 1.2% in 2017, higher than the 0.3% in the previous year. Underlying inflation, which more closely reflects the trend in core prices because it excludes volatile components (unprocessed food and energy), had a stable trend, staying at 0.6% for the third consecutive year.

In 2017, the public sector continued the policy of fiscal consolidation. The public administration deficit was 59.3 billion euros, a figure that represents 2.6% of GDP, after closing 2016 at 3.4% of GDP. This trend allowed the French economy to exit the excessive deficit procedure set by

Box 2.2

THE LABOUR REFORM PASSED BY MACRON'S GOVERNMENT IN 2017

The labour reform will enable small enterprises to negotiate labour conditions more freely with their workers, with the chance to break away from the sectoral agreements that encompassed all businesses, ignoring the specific situation of each one. For example, until now, if a business underwent losses and falling sales, it could be forced to raise wages if specified in the sectoral agreement.

Firms with less than eleven employees may negotiate conditions directly with their employers, without the need for union representation. However, this type of change is worrying to unions and some workers, who fear that they lack the power and experience to negotiate the working relationship with their employer.

On the other hand, a limit was set on compensation for unfair dismissal. Payment will depend on the time the worker has been with the company, so compensation will rise progressively. For example, unfair dismissal of a worker who has been at a company for two years may entitle him to three months' wages in compensation; on the other hand, someone who has worked for thirty years with a company may receive a maximum of 20 months' wages, this being the limit after the labour reform.

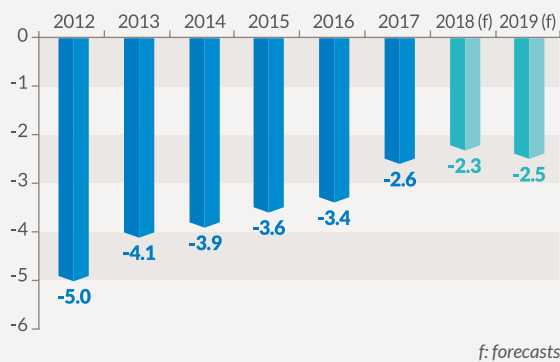
Moreover, new labour legislation allows businesses to cut staff collectively, offering voluntary redundancy through early retirement. In the case of multinationals, this type of policy may be implemented if it can be shown that it is necessary, irrespective of the company's profits outside France.

This series of labour changes tries to make the employment of new workers more attractive as the company can adapt easier if the economic cycle or the company's circumstances change. The decentralisation of collective negotiation within the business will allow for internal adjustments (changes in working hours and wages) without the need for external adjustments or by amount, such as dismissal.

These measures are added to those passed several years ago by the previous French Government, which led to significant cuts in social contributions, with the intention of reducing the gap between business contributions to social security in France and the average for Eurozone countries. Remember that France is one of the member states with the highest labour cost, due to the high tax burden on labour.

FRANCE'S PUBLIC DEFICIT As % of GDP

Chart 2.3



Source: European Commission.

The public sector continues to reduce the deficit thanks to the increase in fiscal revenue.

at the end of 2017 compared with 96.6% at the end of 2016), making the French economy vulnerable to changes in investor sentiment and rises in the interest rate. This level of debt is higher than the average of the 19 Eurozone member states (88.8% of GDP).

the European Commission for countries that cross the public deficit threshold of 3% of GDP. This deficit reduction occurs as a result of a greater increase in GDP of income than expenditure. Specifically, income's share of GDP went from 53.2% to 53.9%, while that of expenditure fell slightly from 56.6% to 56.5%, although France is the Eurozone country with the highest GDP percentages of both public income and expenditure. Among expenditure, the growth in transfers and subsidies is notable, largely due to the return of the 3% tax on dividends. As for fiscal income, income tax and wealth tax increased 5.2%, after rising 0.6% in 2016. Income from social contributions also rose strongly, thanks to the favourable dynamic of employment, and from VAT, due to the increase in the consumption tax bases. Although the public deficit shrank, public debt increased slightly in Maastricht terms (97.0%

2. Prospects

Economic activity is expected to remain dynamic in 2018, despite the weak start to the year. The predictions of the European Commission, IMF and OECD for the whole of 2018 are GDP growth of around 2%. US protectionist policy and an unexpected upswing in oil prices show a slightly less favourable international environment than in the fourth quarter of 2017. Equally, the strong tailwinds that allowed economic activity to accelerate in 2017 (accommodative monetary policy and growing global demand) will continue to support continuous, solid growth in 2018. However, this growth could drop off later (1.7% in 2019 and 1.6% in 2020, according to the Bank of France's predictions), once these external driving factors fade.

Growth in private consumption, which was weak in 2017, is expected to gradually recover as family income increases due to job creation and wage rises. Moreover, tax cuts should provide greater support to purchasing power and consumption, although part of the effect could be diverted towards savings.

Consumption will recover as unemployment falls and wage increases are implemented.

Growth in investment is expected to remain strong in 2018 before dropping off in 2019. Public investment will recover in 2018 after several years of contraction, according to the municipal electoral cycle. In contrast, housing investment is expected to decrease after very high growth in 2017, while business investment will maintain strong growth in 2018, at about 4%, benefitting from the labour reform, favourable financial conditions and the announced reform of business regulations. The negative contribution of foreign trade to GDP growth is also expected to end – for the first time in five years – as a result of the upswing in exports forecast for 2018. Nevertheless, exports will slow down in 2019 due to the delayed effect of euro appreciation and less dynamic global demand.

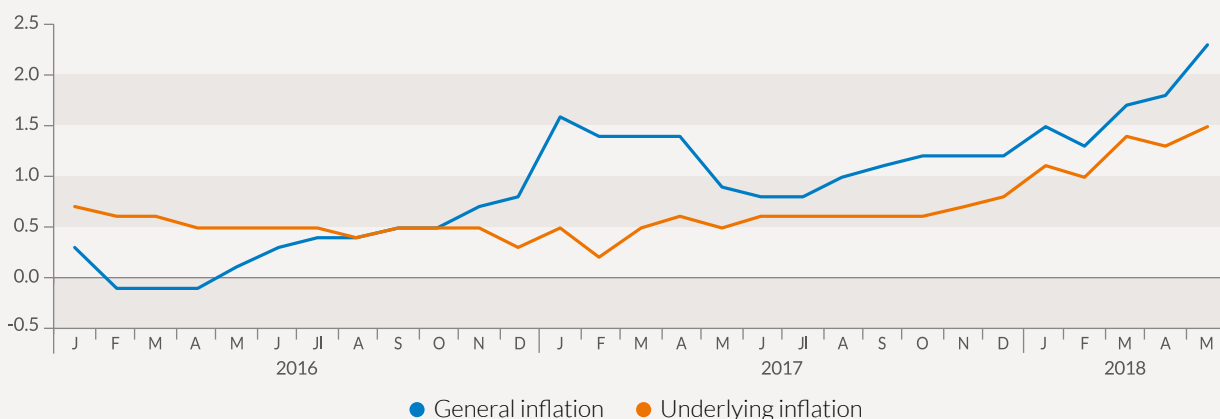
The rate of growth in activity slowed in the first quarter due to capital investment.

In the first quarter of 2018, the pace of economic activity can be seen to slow. GDP growth went from 0.7% in the fourth quarter to 0.3% in the first quarter of 2018. Household consumption expenditure increased at the same rate as the

previous year, while gross fixed capital formation lost impetus. In general, final domestic demand excluding stock variation slowed and contributed less to GDP growth (0.3 points compared with 0.5 points in the previous quarter). Exports also weakened slightly and imports remained stable. Consequently, the foreign sector did not contribute to GDP growth in the first quarter. Equally, the stock variation remained stable and therefore did not contribute to GDP growth either. As for supply, industrial production fell in quarter-on-quarter terms (especially in the transport material sector), but it continued to grow at a sustained rate in services and accelerated in construction.

In this context, the harmonised rate of inflation was 1.6% on average during the first four months of the year, three tenths higher than in the fourth quarter of 2017. Inflation for the whole of 2018 is expected to rise to 1.9%, compared with 1.2% in 2017, driven by the increases in special taxes (tobacco tax) and high oil prices. Nevertheless, underlying inflation in 2018 – excluding energy and food – will only increase marginally.

THE TREND IN CONSUMER PRICES IN FRANCE - Interannual variation rates, as %



Source: Eurostat.

2017 was marked by a significant increase in employment, which could well continue in 2018 despite the reduction in subsidised contracts implemented this year. In variation rates, employment could grow 1.4% and unemployment could fall to 8.7% on annual average in 2018, according to the OECD. Private sector employment will be favoured by the transformation of tax credits for employment, introduced with the competitiveness and employment plan (CICE), through a permanent reduction of business contributions to social security, and the favourable economic trend.

In 2018, the public deficit is predicted to continue to shrink a few tenths to 2.3% of GDP. This will be possible thanks to growth in revenue, which should remain strong due to cyclical development, despite the tax cuts provided in the 2018 budgets – with an estimated impact of 0.3% on GDP. Measures such as housing tax exemption, replacement of the wealth tax by a property tax or the introduction of a fixed rate of tax on investment income will be partially offset by the increase in environmental

The public deficit will decrease in 2018, despite the tax reforms approved for this year.

taxes which will involve about 0.1% of GDP. The forecast also incorporates the impact on spending from the repayment of the 3% tax on dividends (estimated at some 5,500 million euros in 2018).

If policies are not modified, the deficit is expected to rise to 2.5% of GDP in 2019. The forecast takes into account the incremental impact on the deficit of about 0.9% of GDP resulting from the replacement of the CICE (tax credit for competitiveness and employment) by a permanent reduction in social security contributions. If this effect is discounted, the deficit should shrink to 1.9% of GDP, mainly due to positive cyclical conditions. As a result of this trend in the public deficit and GDP, the level of public debt is expected to decrease to 96.4% of GDP in 2018 and to 96% in 2019.

Since the French Government has managed to bring the deficit into line with EU requirements in 2017, it is likely that Macron could reach the goal of fiscal equilibrium in 2022. Once the labour market has become more flexible, the government's priorities are to reform the pension system, eliminate public jobs for life in specific fields and introduce performance-linked variable wages for the civil service.

The French Government also announced that it will undertake a reform of the legislative environment to make business easier and reduce obstacles to setting up businesses. It is notable that, according to the 2018 *Doing Business* report, which evaluates 190 countries around the world, France is at number 31 in terms of "ease of doing business", having fallen three places since the 2017 edition. France excels in matters of trading across borders and enforcing contracts. In contrast, it has a negative bias in registering property, getting credit and paying taxes.

The high level of public debt and the high unemployment rate are the two main risks.

On balance, GDP growth will continue to be strong in 2018, driven mainly by private consumption – which will benefit from increased employment and decreased tax – investment – which will be boosted by the labour measures and measures to encourage competitiveness – and exports – considering the improvement in competitiveness which French businesses may achieve. Nevertheless, with the public debt close to 100% of GDP and unemployment around 9%, the challenges are still significant.

Fulfilment of the prospects for the next few years depends on the upside and downside risks. On the one hand, current and future reforms could increase the potential growth of the French economy. On the other hand, euro appreciation and the uncertainties hanging over global

FRANCE. MAIN MACROECONOMIC AGGREGATES - Interannual variation rates

Table 2.1

	2015	2016	2017
Components of demand			
Private consumption	1.5	2.1	1.0
Public consumption	1.0	1.4	1.3
Gross fixed capital formation	1.0	2.8	4.5
Domestic demand without inventories (a)	1.3	2.1	1.8
Inventories (a)	0.3	-0.4	0.2
Exports of goods & services	4.6	1.5	4.5
Imports of goods & services	5.9	3.0	4.0
Components of supply			
Agriculture	0.1	-12.3	4.8
Industry	0.4	1.1	1.5
Construction	-0.6	-1.4	2.4
Commerce, transport, hotels & catering	2.1	1.2	3.6
Information & communications	3.8	3.9	5.4
Financial activities	0.2	0.5	-6.8
Real estate activities	0.3	0.2	1.2
Scientific activities & prof. services	1.7	3.2	4.6
Public admin., health & social serv.	0.3	1.3	0.9
Cultural, recreational & other activities	-1.1	2.7	0.7
GDP at market prices	1.1	1.2	2.2

(a) Contribution to growth of GDP at market prices.

Source: INSEE (demand) and Eurostat (supply).

demand represent a negative risk to export growth. Although the main negative risks derive from the foreign sector, new domestic risks have appeared. The rail strikes in the second quarter of 2018 could have a negative impact on growth, although the effect is likely to be limited and short-term. Moreover, a prolonged decrease in business sentiment throughout the year could result in a steeper fall in growth in 2019.

Current and future reforms may increase the potential growth of the French economy.

III. The Spanish economy

1. The main features of economic development in 2017

In 2017, the pace of activity in the Spanish economy remained strong, greater than initially predicted. This enabled Spain to regain GDP levels from before the crisis and continue to

For the third consecutive year, GDP growth was higher than 3%.

approach the 2008 employment rate. The upward trend largely exceeded expectations thanks to the favourable behaviour of foreign markets, especially Eurozone economies, which showed strong growth in a context of very favourable financial conditions. So, in 2017, the Spanish economy again saw new records in the figures for exports and foreign tourists, demonstrating the progress that the country has made in opening up and internationalising its economy during the period of crisis. This resulted in greater consumer and business confidence, reflected in the good trend in consumption and investment. Equally, the flow of new credit to households and small and medium-sized enterprises began to grow, but still within an overall context of debt.

Spanish GDP ended the year with annual growth of 3.1%, two tenths lower than the 2016 rate, but with growth above 3% for the third consecutive year, according to data from the National Institute of Statistics. Quarterly growth saw a slight deceleration in the second half of the year, since it grew 0.8% in the first quarter and 0.9% in the second - in line with the rates observed from the start of the recovery - but growth fell to 0.7% in the third and fourth quarter. For its part, the potentially negative impact of political uncertainty in Catalonia seems to have been slight and, to a large extent, offset by the improvement in the external context.

One of the positive aspects of growth in the Spanish economy is that its composition remains balanced for the second consecutive year, as both domestic demand and external demand have made a positive contribution to GDP growth. National demand, driven mostly by the dynamism in investment and private consumption, is proving to be the main driving force behind growth, as it added 2.8 percentage points to the rise in GDP, three tenths more than in 2016. On the other hand, net external demand added 0.3 points to growth, four tenths more than in the previous year, as a result of an acceleration in imports of goods and services that exceeds the acceleration in exports.

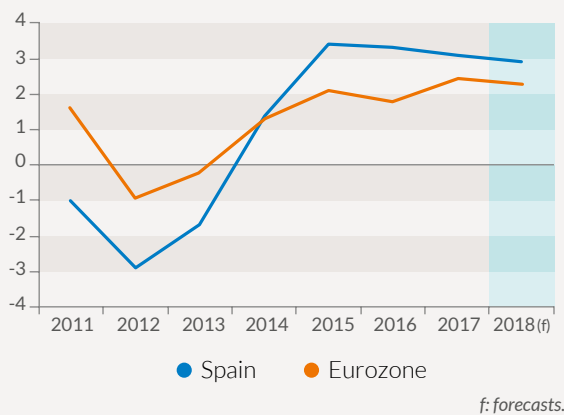
Spain is the major European economy that grew most in 2017.

The Spanish economy grew most among the major developed countries, well above the 2.3% of Eurozone member states as a whole, and was also among those that created most

employment. From the start of the recovery, growth in the Spanish economy has been stronger than for the EU, so Spanish per capita GDP growth measured at purchasing power parity

GDP GROWTH IN SPAIN AND THE EUROZONE - Interannual variation rates as %

Chart 3.1



Source: Eurostat.

f: forecasts.

compared with the EU-28 average (equal to 100) has gradually risen to reach 92 in 2017. However, it is still far from the 103 it reached in 2007, just before the crisis.

Among the components of national demand, the highest rate of growth was in investment in capital goods (6.1%), followed by investment in construction, with an annual rate of 4.6%, two components whose variation rates have also accelerated since the previous year. The key factors in this upswing in investment are low interest rates, increased profits and the improvement in economic prospects. In contrast, growth in household final consumption expenditure decelerated, from 2.9% in 2016 to 2.4% in 2017. Among the factors that may

explain the slowdown in growth in private consumption are wage stagnation and rising inflation. Finally, public consumption grew 1.6%, double the previous year, reflecting a relaxation in the fiscal consolidation effort favoured by the increase in tax revenue due to a very favourable economic trend.

As for external demand, the increased dynamism in both exports and imports compared with the previous year is due to an improvement in world trade flows and the upturn in investment. Real exports of goods and services saw an increase of 5% in 2017, two tenths more than in 2016, while imports accelerated 2 points, to a rate of 4.7%, explaining the fall in the positive contribution from external demand to GDP growth in 2017. The increase in imports was driven, above all, by the upturn in investment in capital goods, which encourages imports.

Unlike previous periods of expansion, GDP growth was accompanied by an external surplus.

The current expansion of the Spanish economy is compatible with maintaining an external surplus, which had not occurred in previous periods of expansion. According to balance of payments data, the financing capacity of the

Spanish economy remained at 2.1% of GDP for the second consecutive year. This external surplus allowed for the volume of foreign debt to continue to fall for the sixth consecutive year.

From the perspective of supply in 2017, growth was seen in the main branches of activity, except in financial activities and insurance, which maintained the negative trend that started in 2009 with the financial crisis. Industry grew at a similar rate to the previous year (3.7%) while construction was the sector with the greatest increase (4.9%), although its contribution to GDP is still small due to the major decrease in share it suffered during the crisis. Within services, the progress in professional activities stands out (6.2%), and in information and communications (5.1%). Dynamic investment in construction was reflected in an increase in the real estate sector, growing in 2017 for the second consecutive year, also noted in the increase in real estate sales and housing prices.

In line with the strong dynamism in economic activity, the labour market continued to recover. Throughout this year, 490,000 full-time equivalent jobs were created, representing growth of 2.8% compared with the previous year. Productivity per employee increased slightly, by 0.2%, and remuneration per employee by 0.1%, so that unit labour costs fell 0.1%, following the overall trend of recent years. The improvement in unit labour costs compared with the Eurozone allowed

for recovery of the loss of competitiveness that accumulated during the period of expansion, a key factor in explaining the dynamism in Spanish exports.

Long-term unemployment and temporary work are the greatest elements of concern in the labour market.

The level of unemployment continued to fall in Spain, but at an ever-lower pace. Specifically, in the fourth quarter of 2017, the total number of unemployed was 3,766,700, 11% less than at the end of the previous year. In absolute terms, the number of unemployed fell 471,100 in one year, the slowest decrease in the last three years. The unemployment rate also fell to 16.5% at the end of 2017, the lowest since the fourth quarter of 2008 but still far from the minimum achieved in 2007 (8.2%). Despite the reduction in the unemployment rate, there are still groups that are greatly affected, such as young people under the age of 25 (the youth unemployment rate is still 38%), immigrants from outside the EU (with an unemployment rate of 26%) and people who have been unemployed for more than two years - 38% of the total. The persistence of a high unemployment rate is one of the reasons for increased income inequality in Spain in recent years.

New to 2017 is the slowdown in growth in temporary employment, compared with the previous three years. This meant that at the end of 2017, the rate of temporary employment reached 26.7%, only 0.2 points above the level at the end of 2016, and far from the levels seen during the crisis (33.8% at the end of 2006). However, the rate of temporary employment in Spain is still much greater than in the Eurozone (16.2% at the end of 2017).

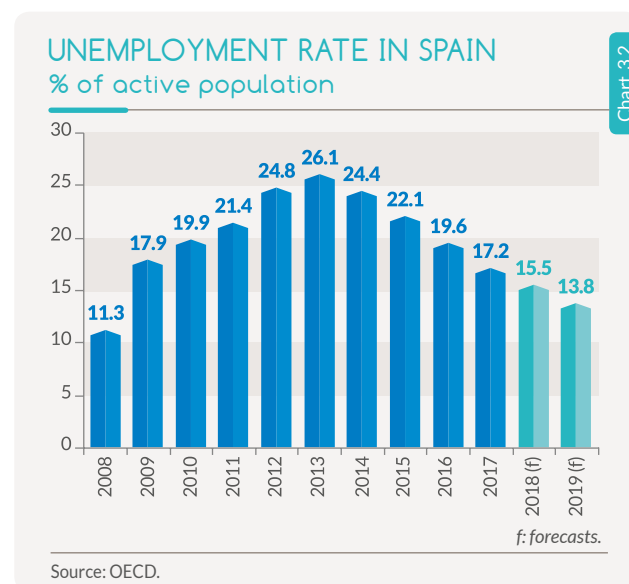
At the beginning of 2017, an 8% rise in the interprofessional minimum wage (SMI) was approved, to which another increase of 4% was added in 2018. This increase, which directly affected just over 3% of employees, may have low aggregate effects on both employment and wages.

The trend in inflation was influenced by the behaviour of energy and oil prices and also the euro/dollar exchange rate. Inflation rose to 3% at the start of 2017 due to rising energy prices, and slowed throughout the year to reach 1.1% in December (1.2% in harmonised terms with the Eurozone), as euro appreciation offset part of the increase in oil prices. Equally, on annual average, prices increased 2%, much more than wages (0.1%), representing a significant loss of purchasing power for families. Underlying inflation, on the other hand, reached about 1% on annual average, one point less than overall inflation, indicating that no inflationary pressures occurred from the point of view of demand. In 2017, there was a new positive inflation differential between Spain and the Eurozone, contrasting with recent years, which can be explained by the fact that the Spanish economy depends more on energy price variations. If this differential is maintained, businesses could suffer a loss in external competitiveness, added to that caused by euro appreciation, which also occurred throughout 2017.

In the field of public finance, in 2017, the Spanish economy met its deficit reduction goal agreed with the European Commission and is already close to 3% GDP, which would enable it to exit

The level of unemployment continued to fall in Spain, but at an ever-lower pace. Specifically, in the fourth quarter of 2017, the total number of unemployed was 3,766,700, 11% less than at the end of the previous year. In absolute terms,

the number of unemployed fell 471,100 in one year, the slowest decrease in the last three years. The unemployment rate also fell to 16.5% at the end of 2017, the lowest since the fourth quarter of 2008 but still far from the minimum achieved in 2007 (8.2%). Despite the reduction in the unemployment rate, there are still groups that are greatly affected, such as young people under the age of 25 (the youth unemployment rate is still 38%), immigrants from outside the EU (with an unemployment rate of 26%) and people who have been unemployed for more than two years - 38% of the total. The persistence of a high unemployment rate is one of the reasons for increased income inequality in Spain in recent years.

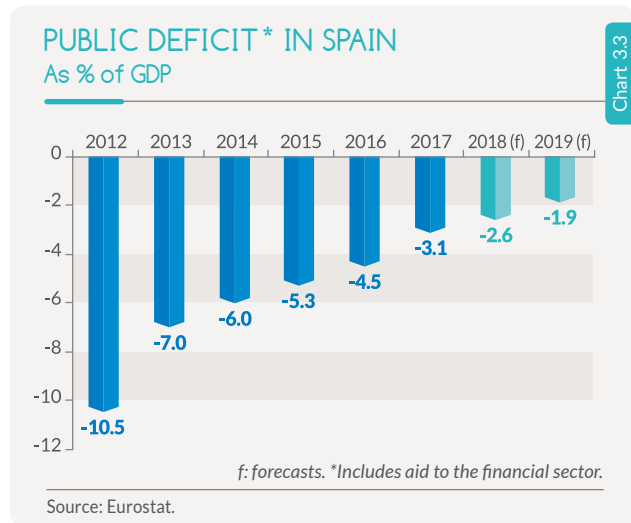


Families lose purchasing power due to rising inflation and stable wages.

the excessive deficit procedure. Specifically, the deficit for the whole of the Spanish public sector reached 3.1% of GDP (-4.3% in 2016), the lowest level in the last 10 years. The drop in the deficit this year can be explained, above all, by the reduction in the deficit of the central government and regional governments. In contrast, the deficit in the Social Security Fund increased and the surplus of local corporations stabilised. For its part, the public debt-to-GDP ratio shrank slightly from 99% to 98.3%, thanks to the increase in nominal GDP and containment of interest rates.

The favourable economic situation that framed the 2017 budgets was reflected in both the increase in public revenue, due to dynamism in tax revenue, and containment of public spending, due to the decrease in entries for unemployment benefit and interest payments and the gentle increase in public sector pensions (0.25%). As for revenue, the main tax forms (VAT, personal income and corporate tax) saw a year-on-year increase in revenue of about 4-5% in both cases, thanks to the raised tax bases for consumption and income, as there were no notable tax reforms in 2017.

Spain reduced its public deficit to close to 3% of GDP.



2. The Catalan economy

The Catalan economy remained sound and continued to grow a little faster than for Spain as a whole, as it has done since the start of the recovery, especially in relation to the labour market.

In 2017, Catalan GDP grew 3.4%, according to the Catalan Institute of Statistics (Idescat), combining four consecutive years of strong growth. The increase in Catalan GDP surpassed that of the Eurozone by more than one point (2.3%). The Catalan economy saw quarter-on-quarter growth in the last quarter of 2017 of 0.8%, only 0.1 percentage points less than the first three quarters of the year, in which the economy grew 0.9%. According to these figures, the forecasts that the political conflict would cause a major slowdown in the economy were not borne out.

Catalonia grows more than Spain, with new records in exports and tourism.

Since the end of 2013, Catalonia has been creating net employment. In 2017, according to the INE, employment grew 2.9%, more than in Spain. Job creation enabled the unemployment

rate to be reduced to 13.4%, much lower than the maximum in 2013 (23%), but this rate is still higher than the average for the Eurozone (9.1%).

Growth comes from the expansion in domestic demand, the strength of industry, the high levels of investment and the export capacity. It should be remembered that Catalonia has a long industrial tradition. Manufacturing's share of total GVA is 17.4%, 1.9 percentage points more than in the EU-28 and 3.9 percentage points more than in Spain. Growth in industry in 2017 was higher than in the economy as a whole, so its share increased, demonstrating the reindustrialisation observed since the start of the economic recovery. The main industrial branches are food, the chemical and pharmaceutical industry, transport materials and machinery, although Catalan industry is a notably diverse sector.

Box 3.1

THE POLITICAL CONFLICT IN CATALONIA

On 1 October 2017, the independence referendum was held in Catalonia despite being suspended by the Constitutional Court, with tension and violent episodes at the polling booths. With the announcement by the President of the Generalitat of Catalonia, Carles Puigdemont, that the result of the referendum would be implemented (Yes to Catalan independence won), the two main financial institutions based in Catalonia, Banc Sabadell and CaixaBank, announced that they would move their headquarters. Other large companies took the same steps over the next few days, drawing along some smaller businesses too.

On 27 October 2017, the Catalan Parliament unilaterally declared independence and suspended it, after an anonymous vote with 70 votes in favour, 2 blanks, 10 against, and the absence of the parties opposing independence. Faced with this, on 27 October 2017, the Spanish Senate authorised the implementation of article 155 of the Spanish Constitution in Catalonia, approving the dismissal of the Generalitat government, dissolution of the Catalan parliament, and calling regional elections in Catalonia for the 21 December 2017. At these elections, with a record participation of over 80%, Ciutadans (a unionist party) received most votes (36

seats of the total of 135 in the Catalan parliament) but the three independence parties again won the absolute majority with a total of 70 members. With part of the former government in exile (including the ex-President Puigdemont) and another part in prison, the post-electoral period was marked by political paralysis. Finally, on 14 May, Quim Torra was chosen President of the Generalitat of Catalonia and, on 1 June, the ministers were formally appointed and government was formed.

Political tension in Catalonia was the main source of economic risk in Spain in 2017, especially in October and November. Economic indicators referring to the last months of the year indicated that the Catalan economy slowed down more than the other large autonomous communities. According to forecasts, political tension would affect certain economic sectors such as tourism (also influenced by the terrorist attack in the Ramblas in Barcelona on 17 August 2017) and property investment, but it appears that these effects were transitory as the Catalan economy grew again in the first quarter of 2018, as much as the Spanish. Mid-term, it needs to be seen whether this situation will affect foreign investment or business dynamism as, far from disappearing, the political conflict has continued.

The scale of foreign trade is also a notable feature of the economy. Catalonia is the leading Spanish community for foreign trade (concentrating 25.6% of exports and 28.1% of imports in 2017). Moreover, it shows a positive external balance with both the rest of the country and overseas, a sign of its competitiveness. Notably, in 2017, there was 7.3% growth in exports to France, the main international destination for Catalan goods. Outside the Eurozone, the most important growth occurred in exports to the USA (21.2%) and China (17.7%), despite euro appreciation.

The dynamism of the international economy and Catalonia's opening up to the world has resulted in a record number of foreign tourists. In 2017, Catalonia received 19 million foreign tourists, meaning a year-on-year increase of 5%. The number of passengers at Barcelona airport reached 47.3 million in 2017, 7.7% more than in the previous year, becoming the seventh most visited airport in Europe and second in the European top 10 for growth this year. Note that in 2017, Barcelona also became the world leader for holding international congresses, even beating Paris, according to the International Congress and Convention Association (ICCA). Barcelona is

Barcelona becomes the world leader for organising international congresses.

also one of the leading cities for scientific conventions and trade fairs linked to strategic activities such as ICT (Mobile World Capital) or the medical sector.

Another characteristic of the Catalan economy is that the public sector has a lower administrative burden than this sector in the Spanish and EU economies. The Generalitat of Catalonia closed 2017 with a public deficit of 0.56% of Catalan GDP, much lower than the -0.92% of the previous year. Between 2010 and 2017, the adjustment in the public deficit surpassed 85%, going from a historic high of 4.48% of GDP (9,100 million euros) to 0.56% of GDP in 2017 (1,243 million euros). Moreover, in 2017, the Generalitat's finances closed with a structural primary surplus, i.e. discounting the effect of the economic cycle on the Generalitat's finances and interest payments.

3. Prospects

The rate of growth in the Spanish economy remained strong in the first quarter of 2018, despite the weakening European context. The Spanish economy saw growth of 0.7%, equal to the previous quarter. This growth reached the year-on-year rate of 3% of GDP, one tenth less than in the fourth quarter. The lower interannual growth in GDP is the result of a contribution from domestic demand of 2.8 points, four tenths lower than in the fourth quarter of 2017, virtually offset by a positive contribution from external demand of 0.2 points, three tenths higher than in the preceding quarter. Household final consumption expenditure saw interannual growth of 2.8%, three tenths higher than in the fourth quarter, as a result of the improvement in the labour market and economic prospects. This growth in consumption was at the cost of a decrease in the level of family savings to a historic low, due to the low increase in family income. On the other hand, growth in investment slowed significantly, especially investment in capital goods. As for external demand, imports continued to grow but growth was slower than in exports, resulting in an increasingly positive contribution to GDP growth from the foreign sector.

GDP growth in Spain remained strong in the first quarter of 2018, despite the slowdown in Europe.

As for the labour market, employment and unemployment figures show that the recovery process in the labour market continued into the first quarter of 2018, but at an ever-slower pace. Employment shows year-on-year growth of 2.4%, two tenths lower than that of the preceding quarter, while the unemployment rate continued to fall in interannual terms to 16.7%.

TREND IN CONSUMER PRICES IN SPAIN - Interannual variation rate, as %

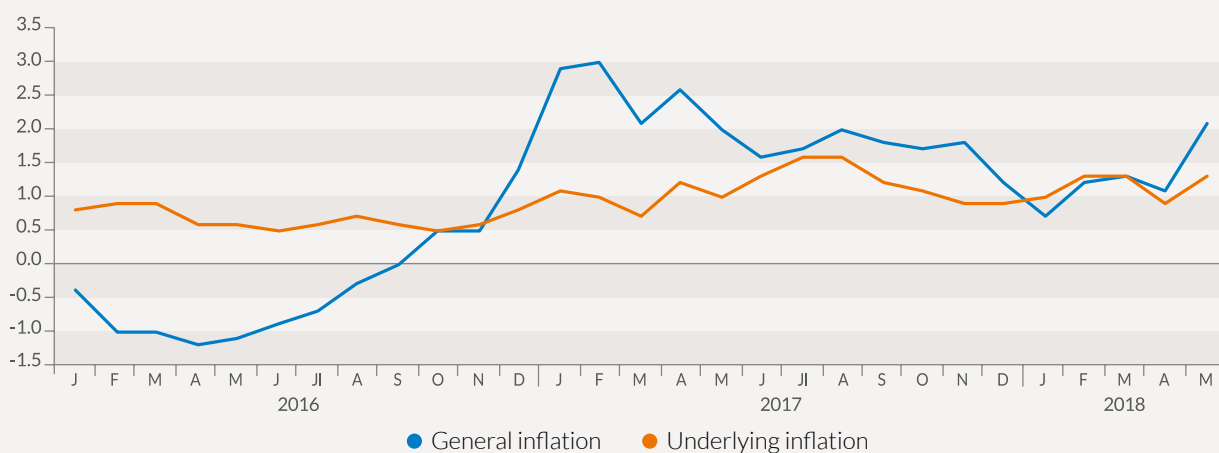


Chart 3.4

Source: Eurostat.

The budgets for 2018 continue to reduce the deficit thanks to the increase in tax revenue.

Consumer prices maintained a stable, moderate trend during the first four months of the year, but this trend broke in May, with an upturn in prices to 2% due to rising energy prices.

In relation to the public accounts, the Spanish Government included a new deficit goal for 2018 in the Stability Plan, equal to 2.2% of GDP, requiring the deficit to be reduced by 0.9 percentage points of GDP against 2017. The national budget plan in 2018 is framed by a favourable macroeconomic environment (2.7% predicted GDP growth), allowing for the entry for social expenditure, public investment, civil service wages and public sector pensions to increase, while the public deficit continues to fall. For its part, the public debt will continue its downward trend to reach 97.6% of GDP in 2018, a lower reduction than desired in the face of a future scenario of rising interest rates, being one of the main vulnerabilities of the Spanish economy.

National and international bodies have revised their forecasts of growth in the Spanish economy upwards for 2018, as both the IMF and the OECD put it at 2.8%. This estimate is mainly based on a more favourable than predicted trend in activity in the first quarter of the year, with a lower economic impact from the political conflict in Catalonia and the return of stability and business confidence from December 2017. On the other hand, there will be a less positive impact from the external driving factors (tailwinds) that drove growth in recent years, especially rising oil prices (which reached 77 dollars a barrel in May 2018) and euro appreciation. As in the previous two years, in 2018, the composition of growth will still be balanced. For the 2019 period, the expansion of the Spanish economy is expected to continue, if at a much slower rate, with real GDP growth of 2.4%, according to the OECD.

In relation to the labour market, the OECD predicts growth in employment of 2.2% in 2018 and 2% in 2019. This growth in employment will lead to additional falls in the unemployment rate, which is predicted to reach 15.5% in 2018 and 13.8% in 2019. Despite this decrease, the unemployment rate in Spain is still the second highest in Europe, after Greece.

Growth will slow down slightly in 2018 due to lower momentum from the tailwinds.

The improvement in potential growth of the Spanish economy requires increased dynamism in productivity, which shows practically zero growth in the current recovery. In this context, investment in human and technological capital is especially important. It should be noted that the crisis increased the gap between Spain and its European partners in relation to R+D as a

SPAIN. MAIN MACROECONOMIC AGGREGATES - Interannual variation rates

Table 3.1

	2015	2016	2017
Components of demand			
Private consumption	3.0	2.9	2.4
Public consumption	2.1	0.8	1.6
Gross fixed capital formation	6.5	3.3	5.0
Domestic demand (a)	4.0	2.5	2.8
Exports of goods and services	4.2	4.8	5.0
Imports of goods and services	5.9	2.7	4.7
Components of supply			
Agriculture, livestock and fishing	-2.4	6.9	3.7
Industry	5.4	3.6	3.7
Construction	2.4	1.9	4.9
Commerce, transport and hotels & catering	4.5	3.8	3.2
Information and communications	3.6	4.9	5.1
Financial and insurance activities	-5.5	-0.8	-1.5
Real estate activities	-0.1	1.5	1.3
Professional activities	5.5	7.0	6.2
Public admin., health and education	2.2	2.0	1.4
Artistic, recreational & other activities	2.1	1.5	1.7
GDP at market prices	3.4	3.3	3.1

(a) Contribution to growth of GDP at market prices.

Source: National Institute of Statistics (INE).

Spain rises in the ranks of Doing Business.

percentage of GDP, both in the public sector and especially in the private sector. To the structural features are added the low ranking in ease of doing business compared with other

developed countries. According to *Doing Business* in 2018, which assesses 190 countries around the world, Spain occupies position number 28 (just before Portugal and three places in front of France), but climbed four places in 2017, after improvements in enforcing contracts (26th place), protecting minority investors (24th), paying taxes (34th) and getting electricity (42nd), as well as maintaining first place in trading across borders, a position it shares with countries such as Austria, Belgium, France and Denmark.

To summarise, forecasts indicate that the Spanish economy will continue growing above the European average, but the rate of increase will slow as external driving factors fade. Although, the economy entered the fourth year of expansion in 2018, no tensions will appear in the external accounts or inflation, beyond those that may occur due to rising oil prices. Altogether, the high level of public debt and the labour market will continue to be the main challenges faced by the Spanish economy over the next few years. For its part, the labour market still suffers two major structural problems: long-term unemployment, which cannot be corrected solely by more economic growth due to the low qualification of most of the unemployed, and the high level of temporary employment, which is a major

The high level of public debt is one of the main risks for the future.

burden on social cohesion. The forecasts assume political stability in the national government and gradual stabilisation of the situation in Catalonia. On June 1, the head of the opposition and leader of the Socialist party, Pedro Sánchez, won the motion of censure against the prime minister of the Spanish government, Mariano Rajoy. Despite the change in government, the new prime minister is committed to maintaining the budgets presented by the previous executive. Apart from this odd episode of political instability, which has not been punished by the financial markets, the main risks come from the external environment. Firstly, the instability in the Middle East may cause oil prices to rise, with seriously negative impacts on the Spanish economy, which is greatly dependent on this energy source. Secondly, the weakening European economy could affect Catalan exports, as it receives 60% of foreign sales.



The Andorran economy: general developments

IV. Population, employment and education

1. Population and migratory flows

Andorra ended 2017 with a registered population of 80,209, representing an increase of 2.5% compared with the previous year (up 1,945) and the highest figure since 2011. This trend shows an acceleration in the rising trend that started in 2014, favoured by an improvement in the economic context after the adjustment due to the crisis and regularisation of the census.

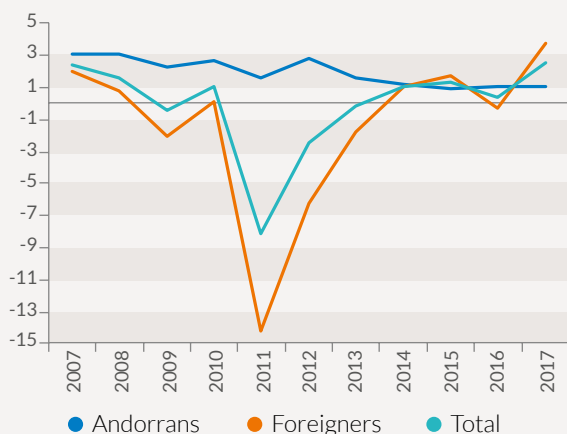
In parallel, the figures for estimated Andorran population published by the Department of Statistics (a different concept from the population registered by the Comú governments, referred to in the previous paragraph), also reflect an increase in population of 2.3% in 2017, with a population of 74,794. These estimated population data are prepared monthly since 2009, thanks to communication and cross-checking of census data between official and parish bodies, and are the reference date used in this report for calculating population indicators. The comparison between both sources still shows a significant difference of more than 5,400 people, making the registered population 7.2% higher than the estimated one. However, the discrepancy between both series has reduced appreciably over time, considering it was 20.9% in 2010.

Andorra ended 2017 with a registered population of 80,209, the highest figure since 2011.

The distribution by nationalities reflects that the rise in population seen in Andorra can be explained, above all, by the increase in the foreign population and, to a lesser extent, Andorrans. This contrasts with the pattern of the previous year where the number of registered foreigners fell

REGISTERED POPULATION
Interannual variation rate (%)

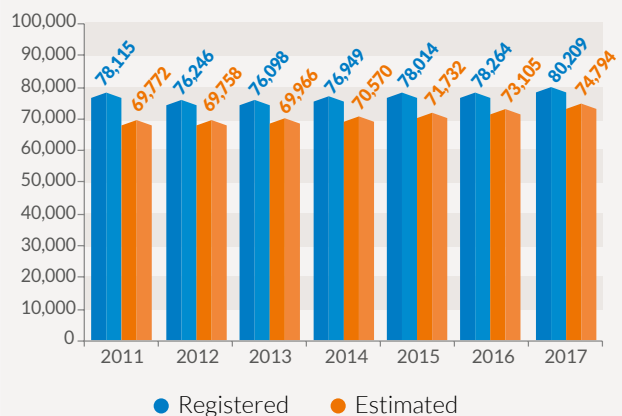
Chart 4.1



Source: Parish censuses of the Comú governments / Department of Statistics.

REGISTERED AND ESTIMATED POPULATION

Chart 4.2



Source: Parish censuses of the Comú governments / Department of Statistics.

and the whole increase in population related to the Andorran population. As a result, in 2017, the foreign population reached the highest figure since 2011.

With the recovery in economic activity, Andorra is again attracting foreign workers.

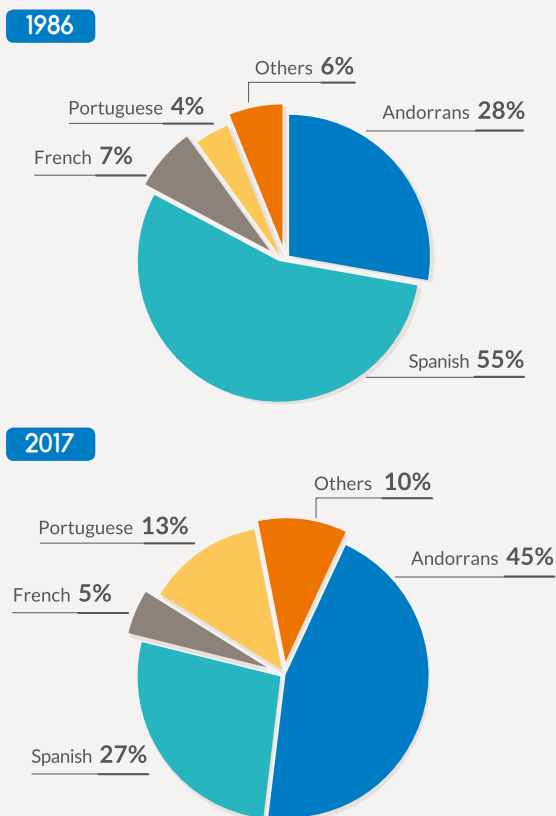
Specifically, the increase in the native population was 1.1%, to 36,526, similar to the rate of increase of the last three years. In parallel, the foreign population increased 3.7%, the highest rise since 2004, putting the total figure at 43,683. This trend confirms that, with the gradual recovery in economic activity, Andorra is again attracting foreign workers.

The increase in foreigners was distributed among the main nationalities present in the country. Specifically, the Spanish, who are the largest group, increased 3.4%, raising their share of the total population two tenths, to 26.6%. The increase in French was stronger (6.4%), and the number of Portuguese also grew slightly, after eight consecutive years of falls. Moreover, foreigners of other nationalities are again the group that grew most (7.7%), cumulating ten years with a better trend than the other three foreign groups. Consequently, their share of the total population rose to 9.7%, the highest level in the available historical series and almost double that of the French, contrasting with the similar share that both groups had in 1999. So, it can be concluded that the source markets of labour continue to diversify.

Altogether, the proportion of foreigners in the total registered population increased six tenths to 54.5%. This is the highest level in the last five years, if still far from the maximum reached in 1986 (72.5%). In contrast, the percentage of the group of Andorrans fell to 45.5% but, even so, the current situation is much more balanced than it had been in the past.

REGISTERED POPULATION BY NATIONALITIES

Chart 4.3

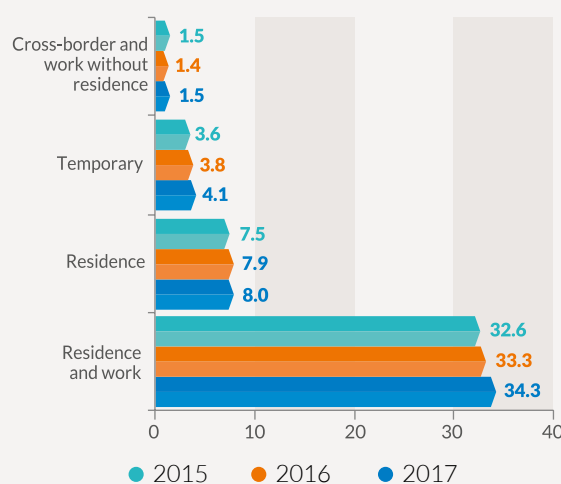


Source: Parish censuses of the Comú governments / Department of Statistics.

The arrival of foreigners to Andorra is reflected in the increased number of valid immigration permits which, on 31 December 2017, totalled 47,878 (including temporary), 3.4% more than in the previous year. Of these, the majority are for residence and work, increasing 3.1% due to the improved trend in the Andorran job market. This factor also drove the increase in

VALID IMMIGRATION PERMITS BY TYPE, AT THE END OF THE YEAR - In thousands

Chart 4.4



Source: Department of Immigration / Department of Statistics.

permits for border workers (5.2%). For their part, plain residence permits increased more slowly (1.3%). In contrast, temporary work permits for foreign companies saw a decline (-1.7%, to 115).

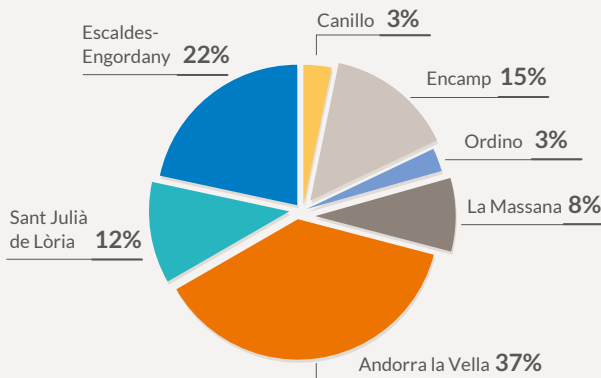
By parish, according to the data on estimated population, the increase in population in 2017 was also generalised, following the pattern that marked the three previous years. Of note are the increase in Canillo (7%), followed at a distance by La Massana (3.3%) and Encamp (3%). The other

four parishes grew under the average, with rates varying between 2.1% in Ordino and 1.5% in Andorra la Vella. However, the latter parish is still by far the most populated, with 29.4% of Andorra's total estimated population (28.1% according to the registered population data), and Canillo is still the least-populated parish (5.3% of the total estimated population and 5.8% of the registered population).

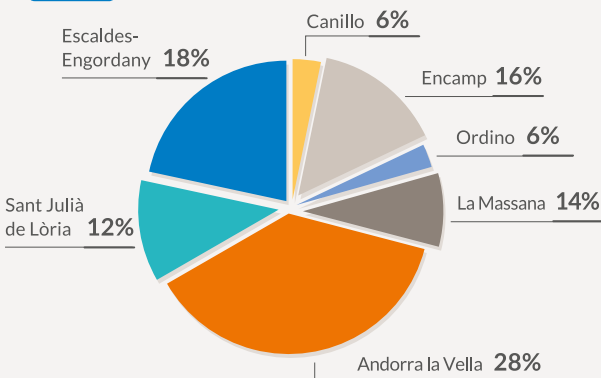
REGISTERED POPULATION BY PARISH

Chart 4.5

1991



2017



Source: Parish censuses of the Comú governments / Department of Statistics.

The population of the high, less-populated parishes grew more than the low parishes for the fourth consecutive year.

Consequently, the population of the high, less-populated parishes grew more than the low parishes for the fourth consecutive year, recovering the trend of gaining percentage that was seen from the start of the nineties until 2011. So, the share of the high parishes increased to 39.5% of estimated population (41.4% of registered), one point more than four years ago, and well above the 29.1% they represented at the start of the nineties (according to registered population). In contrast, the low parishes contain 60.5% of the estimated population, dropping to 58.6% of the registered population.

The recent increase in the foreign population has accentuated the predominance of the male population over the female.

As for the population structure by age and gender, the recent increase in the foreign population accentuated the predominance of the male population over the female. So, according to the data on estimated population, the number of men exceeds the number of women in all working age brackets, except the 35-39 age bracket and the over-75 age bracket. Consequently, the difference

VARIATIONS IN THE ESTIMATED POPULATION

Table 4.1

	2016	2017
Births	634	588
Deaths	310	319
Natural increase	324	269
Birth rate (per thousand)	8.672	7.862
Death rate (per thousand)	4.240	4.265
Rate of natural increase (per thousand)	4.432	3.597
Increase from migration or census regularisation	1,049	1,420
Total population increase*	1,373	1,689
Marriages	295	320

* Natural increase plus migratory increase.

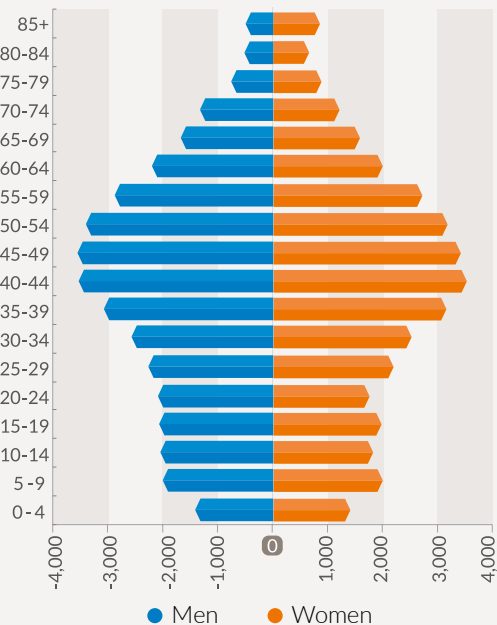
Source: Department of Statistics.

between the percentage of men and women increased 1.7 percentage points. It should be remembered that the greater presence of men can be explained by the size of the foreign workforce which has traditionally been male. So, the presence of foreigners clearly exceeds that of Andorrans, in all age brackets from the age of 30, according to registered population data. In contrast, the proportion of Andorrans is much higher in the age brackets: 0-9 (78.3%), 10-19 (76.7%) and 20-29 (61.2%). In contrast, the presence of Andorrans is limited to 33% in the 65 and over age bracket.

Finally, the distribution by ages in 2017 shows that Andorra is experiencing a progressive aging process, similar to other developed economies. So, the increase in registered population has only been noted from the age of 15 upwards, a pattern that has been repeated since 2014. Now, the population under 14 has fallen 1.2%, and lost half a point in the total, to 13.8%. In contrast, the group of 65 and over grew 5.2%, raising its share of the total by four tenths, to 14.4%, a historic high. In between, the population of working age (15-64) increased 2.7%, raising its share of the total a little, to 71.8%. As a result, the average age of the Andorran population in 2017 rose to 41.4, reaching a new historic high. In any case, it is also important to note the differences between parishes, with ages from 38.4 in Ordino to 42.1 in Andorra la Vella.

STRUCTURE OF THE ESTIMATED POPULATION BY AGE AND GENDER. 2017

Chart 4.6



Source: Parish censuses of the Comú governments / Department of Statistics.

The progressive aging of the population continues, with an average age of 41.4, a historic high.

2. Employment and unemployment

In 2017, the trend in the Andorran labour market was clearly positive, favoured by the context of improvement in the overall economic situation and the support of measures to promote employment. According to data from the Workforce Survey, published for the first time this year,

the working population of Andorra increased for the third consecutive year, at an annual rate of 0.5%, to reach 42,593. Of these, 13.2% are self-employed and the others are employees, divided between the private sector (68.6% of total employed) and the public and semi-public sector (18.2%). As for training, 81.2% of the employed population has at least secondary education, and in relation to the type of working hours, 90.9% are full-time and the other 9.1% are part-time. Full-time workers have an average of 40.9 hours per week and those working part-time an average of 20 hours. The percentage of women working part-time is three times higher than that of men.

In 2017, the Andorran labour market showed a positive trend, with an increase in employment and a reduction in unemployment.

In parallel to the increase in employment, the falling trend in the number of unemployed that started in 2014 continued and accentuated, with a reduction of 24.9%, putting the total figure at 1,029, less than half of the peak reached in 2013.

As a result, the unemployment rate also fell appreciably to reach 2.4%, a much lower level than seen in neighbouring countries. By gender, it is notable that the unemployment rate for men (2.8% in 2017) is higher than for women (2%), which has been consistent over time and differs from what usually occurs in other countries. By age, the bracket most affected by unemployment is 15-24 (7.1% average in 2017), although the youth unemployment rate has fallen drastically over the last five years. This decrease is related to an increase in the inactivity rate in this age bracket throughout the last five years, due to the fact that more young people are taking tertiary studies. In the case of the 25-54 age bracket, the unemployment rate was 1.9% in 2017, while for the oldest (55-64) it reached 3.1%.

EMPLOYED AND UNEMPLOYED POPULATION - In thousands and %



Source: Workforce Survey, Department of Statistics.

To complete the analysis of the unemployed population, it should be noted that 13.1% of the unemployed are long-term, i.e. have been searching for work for more than one year, and are concentrated in the 55-64 age bracket, in which the proportion is four times that of the other age brackets. 86.9% are short-term, and 55.0% of the unemployed have been searching for work for less than three months. Altogether, this demonstrates that the labour context in Andorra presents a quite positive global situation.

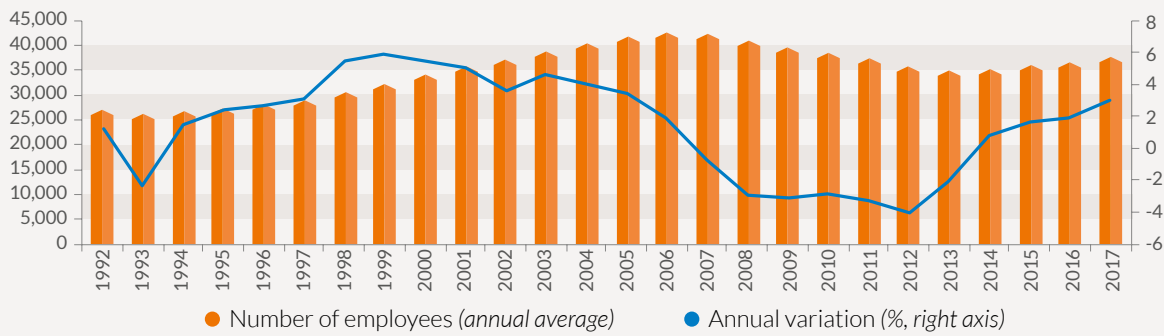
In 2017 the number of employees rose at the strongest pace since 2005.

The favourable trend in the Andorran labour market in 2017 is also reflected in the data of the Andorran Social Security System (CASS), which show that the annual average

number of employees rose 3%, the strongest rate since 2005, to reach 37,705. This increase surpasses that of 2016 (1.9%) and shows consolidation of a period of growth in numbers of employees that started in 2014, after seven consecutive years of falls. So, the total employment stands at 2011 levels, although still far from the more than 42,000 employees in 2006. Along the same line, the average number of jobs in Andorra increased, for the fourth consecutive year, to 45,809, 3.4% more than in 2016.

TREND IN THE NUMBER OF EMPLOYEES

Chart 4.8



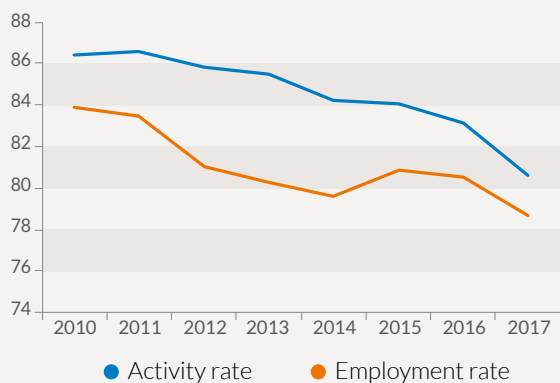
Source: CASS (Andorran Social Security System) / Department of Statistics.

Nevertheless, according to the new Workforce Survey, the employment rate, calculated on the population aged 15-64, fell 1.8 points to 78.7%. This is the lowest level in the available historical series (since 2010), but still easily above the European Union average (67.6%). The activity rate, which fell 2.5 points to reach 80.6%, follows the same pattern, again the lowest level since 2010 (first available data). In this case, Andorra also stands above the community average (73.3%), although the difference has halved in comparison to 2010.

This structurally downward trend in the activity and employment rates can be explained, to a large extent, by two reasons: on the one hand, the progressive aging of the population, which means a relative decrease in the activity rate for the most active age brackets, and, on the other hand, because lower youth participation has been seen in the labour market in recent years, as the improvement in the economic situation allows for an increase in the proportion of young people and other age groups dedicated to studying or continued training.

ACTIVITY RATE AND EMPLOYMENT RATE, AGES 15-64 - As %

Chart 4.9



Source: Workforce Survey, Department of Statistics.

In 2017, Andorra created jobs in services and construction and lost jobs in industry and the primary sector.

jobs in the manufacturing industries (-1.3%), which greatly offset the increased employment in the production and distribution of energy, gas and water (5.2%), while the average number of employees in the extraction industries fell from three to one.

Next to this situation and in parallel with the increase in employment, an increase in the number of businesses was seen, for the ninth consecutive year, of 4.4%, to 8,408 businesses (this concept does not include households employing domestic staff or voluntary declarants without activity). Consequently, in 2017, the average number of employees per business fell to a new historical low of 4.4 (for parity, employees in households employing domestic staff are also excluded).

By sectors, the trend in employment in 2017 showed divergent behaviour, after two years in which the increase was generalised to large sectors. So, on the one hand, jobs were created in services and construction and, on the other hand, were lost in industry and the primary sector. More specifically, employment in industry fell 0.7%, after three years of increasing, basically due to the decrease in

In parallel, the trend in the primary sector also turned around, with a drop in employment of 2.6%, after two years of increases. In any case, the behaviour of this sector has a much lower incidence on the economy, being an activity with a very small impact on the Andorran labour market, with only 167 employees. In contrast, construction has continued to create jobs for the third consecutive year (2.1%), reaching 2,875 employees, although this is far from the almost 6,800 employees there were in the sector in 2006.

Box 4.1

PROGRAMMES TO PROMOTE EMPLOYMENT IN ANDORRA

In 2017, various public programmes to promote employment continued, following the line of work started in 2012, with the following goals: (i) to progressively introduce a system of personalised, integrated schedule of job guidance, aimed at all individuals registered with the Job Service; (ii) to bolster access to work for people with difficulties integrating into the labour market, and (iii) to increase the efficiency of use of public resources assigned to the active employment policy programmes and allocate them according to the needs and socioeconomic context at any one time.

The main changes included in 2017 in the five current programmes focus on the following aspects: young people can join them even if it is not their first job; people with disabilities or in a vulnerable situation are included (allowing for contracts to be below 40 hours a week), and the shortcomings set until now are removed.

So, the programmes announced in 2017 were as follows:

1. Programme to promote permanent contracts in the private sector, giving grants of 250 euros per month, for fifteen months, to businesses that employ unemployed workers who have proven training or have acquired professional experience in specific areas of work, and who form part of the groups of people with labour market integration difficulties, so that their professional profiles remain active without the need for training.

2. Programme to promote employment and training in the private sector, offering a training process in a business environment to unemployed workers forming part of the groups of people with labour

market integration difficulties. This is subsidised, at the first stage, with 550 euros per month (plus a maximum single payment of 300 euros if there is theoretical training) and, at a second stage, if there is a permanent contract, a grant of 250 euros per month, for up to six months.

3. Programme to promote employment in distant geographical areas, awarding financial support and a grant, for up to six months, to individuals who accept job offers from businesses with their premises in areas of Andorra that are distant from the main nucleus of the population, to offset the costs of transport and travel time. The financial support per worker varies according to the distance between the place of residence and the workplace.

4. Programme to improve employment through the public sector, with the aim of promoting temporary contracts for people with market integration difficulties, to carry out work that helps to provide a service for the benefit of the community. Remuneration of those on contract consists of the current minimum wage and payment of the business quota of social security contributions (15.5%) for the duration of the contract, up to nine months.

5. Programme to promote employment and practical training within a business, of young people between the ages of 16 and 20, with a grant of 550 euros per month at the first stage, as long as there is practical training within the business with the specific fixed-term contract of six months of the programme (plus a maximum of 300 euros in a single payment if there is theoretical training) and, at the second stage, in the case of a six-month or permanent contract, a grant of 400 euros per month for up to six months.

Now, the greatest dynamism in employment was seen in the field of services – the sector of Andorra with the highest concentration of employment – where the number of employees increased for the fourth consecutive year, at a rate of 3.3%, the strongest recorded in the last thirteen years. As a result, services' share of total employment rose to 87.7%, a level that sets a new record in the available historical series. In contrast, construction lost another tenth to reach 7.6%, another historical low, and industry and agriculture also shrank to 4.3% and 0.4%, respectively.

NUMBER OF EMPLOYEES

	2017	% var. 17/16	% total 2017
Agriculture, livestock, hunting & forestry	167	-2.6	0.4
Industry	1,603	-0.7	4.3
Extraction industries	1	-63.6	0.0
Manufacturing industries	1,434	-1.3	3.8
Production & distribution of electricity, gas & water	169	5.2	0.4
Construction	2,875	2.1	7.6
Services	33,061	3.3	87.7
Commerce & motor vehicle repairs (etc.)	8,838	1.0	23.4
Hotels & catering	4,957	5.4	13.1
Financial system	1,867	-4.1	5.0
Public administration, defence & mandatory social security	4,377	1.4	11.6
Others	13,022	6.0	34.5
Total	37,705	3.0	100.0

Source: CASS (Andorran Social Security System) / Department of Statistics.

Table 4.2

In greater detail, the distribution of employment between the tertiary activities shows that commerce and motor vehicle repairs are still the most important subsector of services, with 23.4% of total employees in Andorra, although they still lost ground compared with the previous year and achieved the lowest percentage in the available historical series. Real estate activities, rentals and business services (13.2%) were second in the ranking, followed closely by hotels and catering, concentrating 13.1% of employees, three tenths more than in 2016 and a level that had not been achieved since before the crisis (2006). Next come Public administration, defence and mandatory social security, with a drop in percentage for the third consecutive year, to 11.6%, after achieving a historical high in 2014. This is followed by "other social activities and services provided to the community; personal services" – not including health and education – (7.6%), health and veterinary services (5.3%) and the financial sector (5%) – where employment fell most (-4.1%). The other tertiary activities have a much lower percentage of employment.

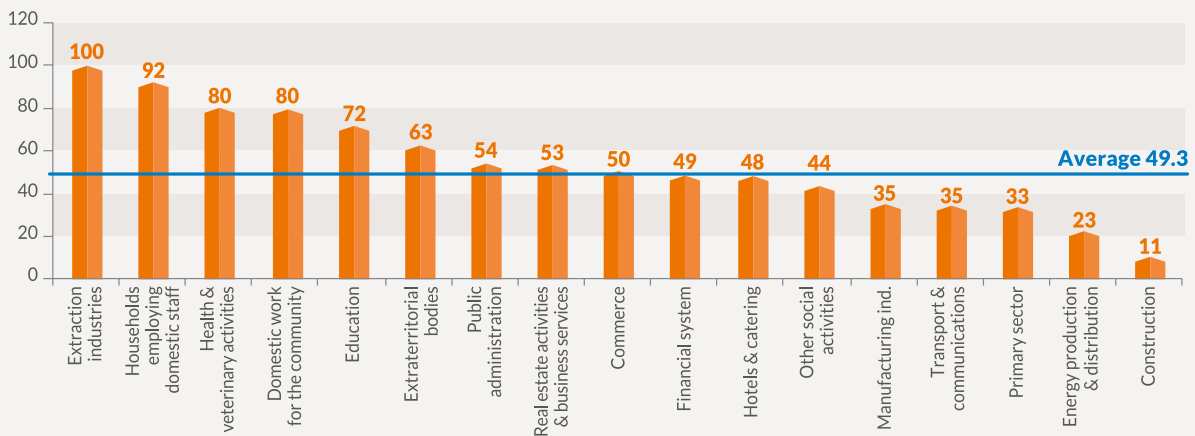
Hotels and catering's share of employment rises to the highest level since 2006.

By gender, the increase in employment in 2017 was higher in the case of men (3.2%) than women (2.8%). This left the distribution of employees at 50.7% and 49.3%, respectively, a situation that, despite everything, is quite balanced. However, the breakdown by sectors reflects very significant differences. So, the sectors with the largest presence of male employees are construction (9 out of 10 employees are men) and energy (8 out of 10 employees). In contrast, the sectors that employ mostly women are households employing domestic staff (9 out of 10); health activities and domestic work for the community (8 out of 10, in both cases), and education (7 out of 10). This distribution pattern of employees by gender in Andorra is similar to those of developed economies.

The job creation seen in 2017 was accompanied by a steep drop in the number of job seekers (-19%) for the fourth consecutive year, reaching a total of 388, the lowest in the last nine years.

PERCENTAGE OF FEMALE EMPLOYMENT BY SECTORS. 2017 - % women among total employees

Chart 4.10



Source: CASS (Andorran Social Security System) / Department of Statistics.

The number of job seekers falls for the fourth consecutive year and the number of workers looking for a better job increases.

So, the percentage of job seekers among total applicants fell to 67.9%, the lowest percentage since 2009. In contrast, the number of applicants looking for a better job saw a significant increase of 44.2%, to 184, which seems to indicate more optimism among the workers towards labour market conditions and the possibility of improving their professional situation.

In parallel, the trend in jobs offered at the Job Service continues to rise, with an increase of 62.7%, to 1,153, the highest figure in the historical series (available since 2007), a trend that indicates an improvement in the employment plans of businesses, in keeping with a more positive economic context. According to these data, the ratio of number of applicants to supply fell from 0.9 to 0.5, implying a much tighter labour situation than only two years earlier and a clear improvement in the job options of the unemployed, although this situation may also imply discrepancies between the characteristics of the unemployed and the requirements of businesses.

The improved trend in the labour market was also reflected in a strong decrease in the number of receivers of unemployment benefit, of 54%, to only 24 individuals, accumulating five years of decreases. Moreover, the coverage rate for job seekers fell 4.6 points to 6.1%, the lowest level since 2009, when the benefits were first offered, and a very low level compared with European neighbours.

The distribution by ages shows that the fall in unemployment favoured all groups, except the youngest (up to 17), among whom job seekers increased from 9 to 12, after reaching the lowest level in the available historical series in 2016. In contrast, a strong reduction was recorded in the other age brackets, led by the age group of 60 and above (-29.3%), contrasting with the increase in 2016 and the greater labour market integration difficulties historically shown by this older group in comparison with the rest.

JOB SEEKERS AND JOBS OFFERED

Chart 4.11



Source: Department of Labour / Department of Statistics.

The decreases were also notable in the age groups of 18-25 (-12.2%), 26-39 (-25.2%) and 40-59 (-16.9%), so all three cases accumulated four years of falls at a double-digit rate.

In effect, the percentage of job seekers in the 60 and above age group fell to 13.3%, although this is four times as much as in 2008, partly explained by the progressive aging of the population. In any case, most job seekers are still clearly concentrated among those aged 40-59 (46.8% of the total), followed by those aged 26-39 (20.7% of the total) and, at a distance, the group aged 18-25 (16.2%). On the other hand, applicants aged up to 17 only represent 3.1% of the total.

The age group 40-59 contains by far the highest concentration of job seekers.

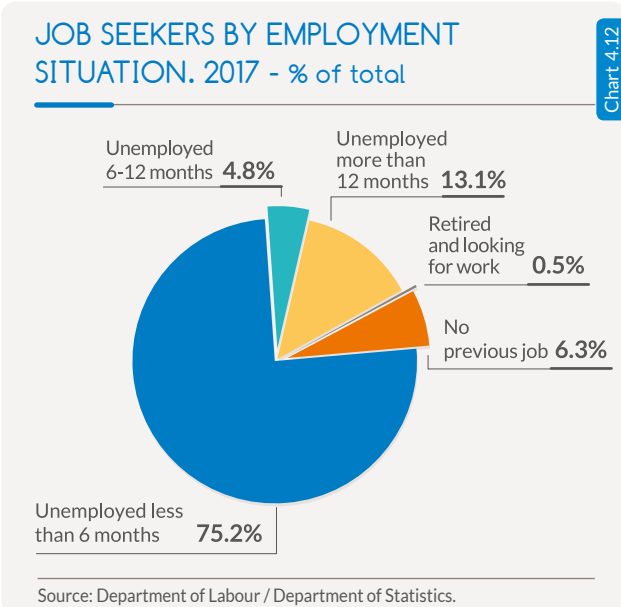
Another notable feature of job seekers in Andorra is that the majority, 75.2%, have been unemployed for less than 6 months, a percentage that rose 3 points against the previous year. For its part, structural unemployment (unemployed for more than one year) stands at relatively low levels (13.1%) in comparison with European neighbours and, moreover, fell in relation to 2016 (15.6%). This can be largely explained by the flexibility of the Andorran labour market. These results are consistent with those of the new Workforce Survey, which also shows structural unemployment at 13.1% in 2017.

Finally, the analysis of job seekers by nationalities shows that the number of foreigners has decreased more than Andorrans, following the same pattern as the three previous years. The group of Portuguese job seekers fell the most (-25.3%), as in the last three years. This limited the

relative importance of this group to 12.6% of the total, the lowest in the available historical series. Also falling more than the average were job seekers encompassed by the group of other nationalities (-23.9%), to represent 11.1% of the total, and the Spanish (-20.8%), although the latter remain the largest group of foreign applicants (125 individuals). The fall in French applicants was also significant (-17.3%) and it remains the smallest (3.5% of the total).

So, the percentage of the total number of foreigners among the total job seekers continued to fall, to 59.3%, the lowest level in the available historical series (since 2007). This percentage is ever closer to that of the total working-age population (58.3%). In contrast, among the job seekers of Andorran nationality there was a decrease of 13.9% and their percentage of the total rose to 40.7%, compared with the 41.7% they represent in the total working-age population. In fact, according to the Workforce Survey, the unemployment rate of Andorrans and foreigners has practically

equalised in 2017 at 2.4% and 2.5%, respectively. It should be stated, however, that this situation was accompanied by significant differences in the inactivity rate between both groups. So, the inactivity rate of Andorrans (27.3%) is more than double that of foreigners (12.8%). This can be explained by the fact that the foreign population returns to their home country when their work in Andorra ends or they reach the age of retirement.



The unemployment rate was similar among Andorrans and foreigners, but the inactivity rate of Andorrans is much higher.

3. Education

In the 2016-2017 academic year, the student population in Andorra, including the school, university and non-university population abroad, was 12,685, 0.3% less than the figure for the previous year, when a record was reached. This downturn can be explained solely by the decline in the non-university population abroad (-20.7%), linking two negative years, and also because the school population stagnated. In contrast, the university population – which includes students in higher vocational education – increased, for the second consecutive year, at a rate of 1.5%.

By country of study, it can be seen that the number of students studying in Andorra increased for the fourth consecutive year (0.2%). In 2017, there were 11,508 students, the highest figure in the available historical series. The percentage of the number of students studying in Andorra in the total student population increased to 90.7%, as the total student population fell. In contrast, the population studying abroad saw a downturn for the second consecutive year (4.9%), which can be explained, above all, by the reduction in the number of non-university students abroad (-20.7%) and also the slight reduction in university students (-0.2%) – the most important group in the population carrying out any kind of studies outside Andorra.

Andorrans studying abroad still do so mostly in Spain, although the trend over the last five years has been for their percentage of the total student population to fall (from 9.1% in 2012 to 6.8% in 2017), which was accentuated in 2017 with a fall of 6.1% (to 865 students). The presence of Andorran students in France was much lower (2.2%) but has remained fairly stable over the last three years although, in 2017, the fall was 0.7%, to 277 students. The distribution by countries of study is completed by 35 students spread between other countries (0.3% of the total), three less than in the 2015-2016 academic year.

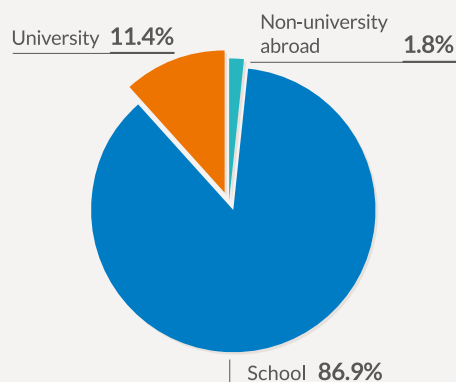
3.1. School population

Over the 2016-2017 academic year, there were 11,018 students at school level, only five more than in the previous year. However, the trend mentioned in the previous section caused an increase in the percentage of the total student population, to 86.9%. Moreover, the schooling rate – calculated as the proportion of school population over the global population at that stage – increased 6.5 points to 50.2%, the highest level in the last three years.

By subgroups, the maternal, primary and secondary levels of education concentrate 86.4% of the school population and the other 13.6% relates to students of baccalaureate and vocational training. As for the trend in the last year, the decrease for the third consecutive year of students at kindergarten (-3.3%) and increase in the other subgroups are notable. The group of vocational students increased the most (4.8%), continuing the rising trend that started in 2013-2014, and contrasting with the slight increase in baccalaureate students (0.1%).

STUDENT POPULATION BY EDUCATIONAL LEVELS. 2017 - As a percentage of the total

Chart 4.13



Source: Ministry of Education and Higher Education / Institute of Andorran Studies.

The Andorran population studying abroad falls, especially in Spain.

STUDENT POPULATION BY LEVELS

Table 4.3

	2016-2017	% variation 16-17/15-16	% 2016-2017
Kindergarten	2,263	-3.3	20.5
Primary education	4,263	0.4	38.7
Secondary education	2,995	1.6	27.2
Baccalaureate	1,058	0.1	9.6
Vocational training	439	4.8	4.0
Total	11,018	0.0	100.0

Source: Ministry of Education and Higher Education.

Analysis of the trend in the school population by type of education shows that the growing uptake of the Andorran educational system stopped in the last two academic years, after obtaining a historical high in 2015. So, the increase in students in this system was almost the same as for the total, maintaining its percentage at 39.3% of the total school student population. In contrast, the number of students in the Spanish educational system saw a decrease of 0.4%, continuing the progressive loss of importance of this system, observed since the start of the nineties. So, its percentage of the total fell one tenth to 28%, setting a new historical low and contrasting with the 52.6% it represented in 1991. To complete the analysis, the number of students in the French educational system increased (0.3%) for the fourth consecutive year, a trend that contrasts with the falling trend that marked the period 2005-2013. Consequently, its share of the total school population reached 32.7%, the highest level since 2008, ever further from that of the Spanish educational system.

3.2. University population

In the 2016-2017 academic year, the university population of Andorra was 1,441 students, 1.5% more than the previous year. By gender, a slight increase in the percentage of women was observed, going from 54.5% in the previous year to 55%, so they remain the majority.

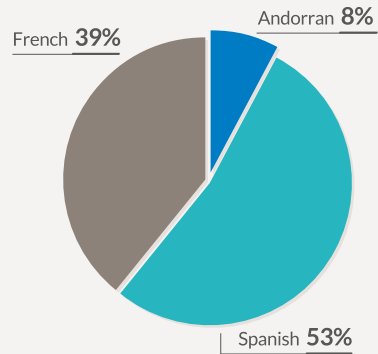
Spain's share of total Andorran university students has been decreasing over six years, but it is still the top destination.

Nevertheless, Spain remains by far the top destination for Andorran university students, with 49.4% of the total (compared with 61% in 2011).

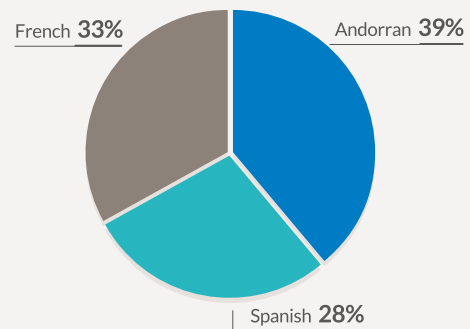
ANDORRAN SCHOOL POPULATION BY TYPE OF EDUCATION

Chart 4.14

1991



2017



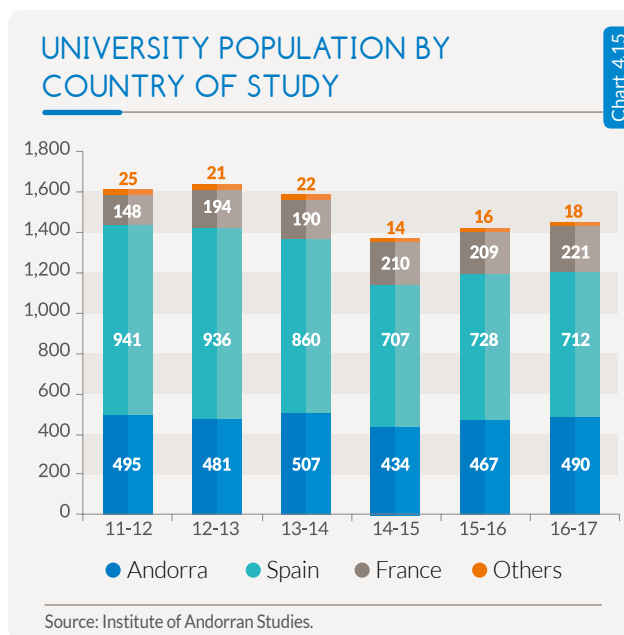
Source: Ministry of Education and Higher Education.

By type of education, the trend for the Andorran system to gain importance stopped in the last two academic years, to the benefit of the French system.

The distribution by countries of study shows that the increase in students was spread over all destinations, with the sole exception of Spain, where it fell 2.2%, with 712 university students. So continues the gradual decrease in Spain's share of the total number of Andorran

university students, which marked the last six years, to the benefit of Andorra and France.

In absolute terms, the greatest increase in university students was seen in Andorra, going from 467 students to 490, an increase of 4.9% and 34% of the total. France's increase was 5.7%, to represent 15.3% of the total, more than double that of eight years earlier. This growing attraction of Andorran students towards France was favoured by the policy of educational aid from the French Government, while the cost of registration with Spanish universities rose. To complete the analysis, 1.2% of the other students – 18 individuals, two more than the previous year – are spread among other countries (United Kingdom, Portugal, Russia, Germany, Argentina, Canada, USA, Italy and Luxembourg).



Finally, the distribution by field of studies reflects that the field with most Andorran university students is still that of social sciences, business studies and law, concentrating 43.5% of total university students. Next are health sciences and social services (15.4%); engineering, industry and construction (12.9%), and arts & humanities (9.4%). With a lower percentage are education, science and services, and agriculture comes last with just 5 students.

V. Activity and demand

1. Developments in economic activity in 2017

The behaviour of the Andorran economy in 2017 was positive, in global terms, with a level of dynamism similar to 2016. Andorra continued to extend the phase of economic growth that started in 2013, allowing it to slowly regain pre-crisis levels of activity. This gradual economic expansion was evident in the favourable trend in the main available indicators of activity, if still at relatively low levels in some cases.

Economic development in Andorra was positive in 2017.

The growing dynamism of the Andorran economy that has been seen in recent years has been largely driven by the good performance in the international context, especially the Eurozone and specifically Spain. This supporting factor has been partly counteracted by the domestic problems suffered in the financial sector over the last three years due to two main factors: on the one hand, Banca Privada d'Andorra was put into administration (the so-called BPA affair) in March 2015, with the subsequent resolution of the entity, culminating mid-2016; on the other hand, an ever more demanding and competitive regulatory environment that required major efforts of transformation and adaptation.

From the perspective of demand, in 2017, a positive trend was seen in the most important indicators relating to consumption and investment, with an especially notable contribution from external demand, as occurred in 2016. From the perspective of supply, Andorran economic growth

continued to be led by services, especially activities linked to tourism which, in turn, depend fundamentally on the good performance in external demand. Also notable was the contribution from construction, which continued its slow path to recovery that started in 2016, after nine years of severe crisis in the sector. In contrast, industry and agriculture showed a weakening pace of activity in comparison with the previous year.

Positive economic development in Andorra can be seen in the upward trend in most indicators of activity and demand. Among the most relevant are notably the increases in imports, numbers of tourists, employment, car registrations, imports of capital goods, government operating costs and public investment, all higher than in 2016. Also significant was the dynamism in the number of businesses and registrations of industrial vehicles. The only indicators that remained negative were energy consumption and credit.

Most indicators of activity and demand displayed a rising trend.

The growth in the Andorran economy was also evident in the labour market dynamics, insofar as this is a lagging indicator of activity. So, in 2017, more jobs were created, if slowly (0.5%), according to the data from the new Workforce Survey. Now, in the case of the group of employees, growth was stronger (3%) and accelerated in comparison with 2016, while the downward rate in the number of unemployed and job seekers intensified, accumulating four consecutive years of decreases. All this, moreover, improves the conditions for residents' consumption.

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

	2016	2017
Activity		
Businesses ⁽¹⁾	5.0	4.4
Establishments ⁽²⁾	5.3	5.9
Employment	1.6	0.5
Employees	1.9	3.0
<i>Industry</i>	1.5	-0.7
Construction	2.1	2.1
Services	1.9	3.3
Unemployment	-17.0	-24.9
Job seekers	-15.7	-19.0
Number of visitors	2.2	1.6
Electricity consumption ⁽³⁾	2.8	-0.4
Imports	4.9	6.6
Demand		
Average wage	4.3	0.0
Car registrations	10.5	19.1
Industrial vehicle registrations	30.0	15.5
Imports of capital goods ⁽⁴⁾	1.9	9.2
Imports of building materials ⁽⁵⁾	-1.6	3.1
Credit from banking entities ⁽⁶⁾	0.3	-5.0
Government operating ⁽⁷⁾	2.0	4.3
Government real investment ⁽⁷⁾	-17.0	19.0

(1) Excluding households employing domestic staff and voluntary declarants (no activity).

(2) Establishments registered with the Registry of Commerce and Industry that carry out a commercial, industrial or service 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) Gross lending to customers.

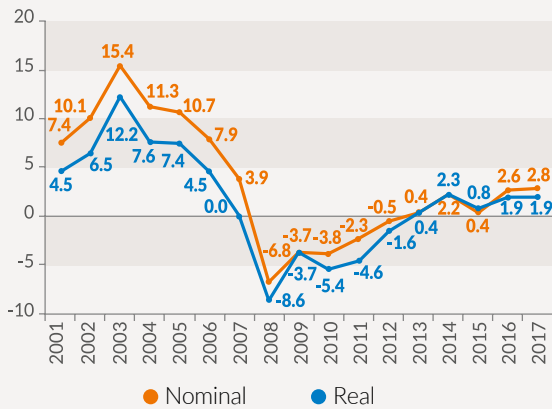
(7) Settled figures, includes Central and Comú governments.

Source: own preparation, according to data provided by the Department of Statistics, Central and Comú governments, FEDA and Andorran Banking.

TREND IN GDP IN ANDORRA

Interannual variation rate (%)

Chart 5.1



Source: Department of Statistics.

In 2017, GDP accumulated five consecutive years of upward trends, with growth of 1.9% in real terms, the same rate as in 2016.

However, in 2017, there were still two notably negative aspects, from the point of view of factors driving demand. On the one hand, the trend in wages, which remained stable in comparison with the previous year, in a context of positive inflation, involving a loss of purchasing power for workers; and, on the other hand, shrinking bank credit. In conclusion, in 2017, the recovery in the Andorran economy continued to progress at a sustained but slow pace.

This trend is reflected in the first estimate of GDP published by the Government, which shows growth of 1.9% in real terms, the same as recorded in 2016. In nominal terms, the rise in GDP over the whole of the year was 2.8%, a percentage that reflects the positive trend in prices in 2017. This increase represents a slight acceleration compared with 2016 (2.6%) and puts the figure for total nominal GDP at 2,674 million euros, the highest value since 2008.

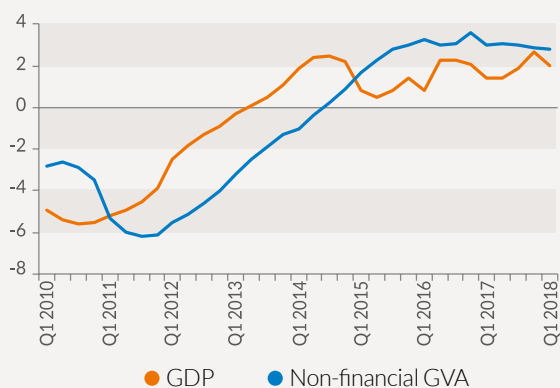
Analysing GDP quarterly throughout the year, it can be seen that the economy improved, with a rate of growth in the first quarter of 1.4%, which accelerated to 1.9% in the third quarter, and ended the year with a year-on-year increase of 2.7%.

So, the economy saw five consecutive years of growth after seven years of crisis and economic losses that still put the value of current real GDP (1,974 million euros) at about the level it was in 2003, and 16% lower than the high it reached in 2007. To be specific, the trend in the Andorran economy over the last three years was affected by a domestic financial crisis, deriving from the BPA affair, plus a more demanding regulatory environment for the financial sector, so, if we exclude this branch from the global trend, the rate of growth in the real economy (non-financial GVA) was much higher (3% in 2017).

QUARTERLY TREND IN GDP AND NON-FINANCIAL GVA IN REAL TERMS

Interannual variation rate (%)

Chart 5.2

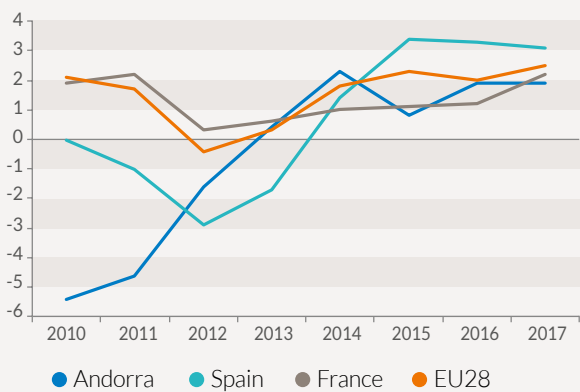


Source: Department of Statistics.

TREND IN ANDORRAN GDP COMPARED WITH NEIGHBOURING ECONOMIES

Interannual variation rate (%)

Chart 5.3



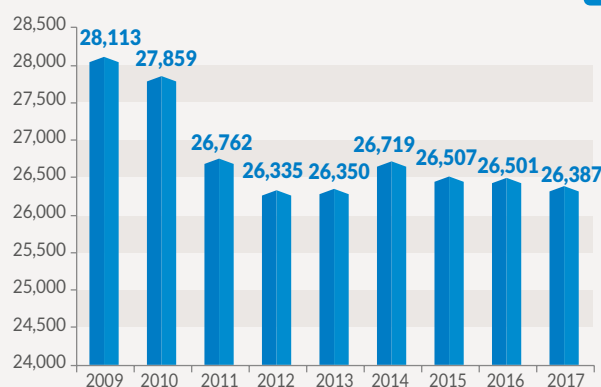
Source: Eurostat and Department of Statistics.

Andorran growth was lower than in Spain, France and the EU as a whole.

From an international perspective, Andorran GDP growth in 2017 remained below both the neighbouring economies of France and Spain, and the EU as a whole. In contrast, the Andorran population continued to grow significantly faster than the European (2.3% and 0.2%, respectively). Consequently, Andorra continued to fall behind neighbouring countries in terms of per capita wealth. According to official figures, Andorran per capita GDP reached 35,747 euros in nominal terms, a similar level to 2014, and 0.5% higher than the previous year. In contrast, in real terms, per capita GDP fell (-0.4%) for the third consecutive year, to 26,387 euros (base year 2000), a similar figure to 2012 and 2013.

PER CAPITA REAL GDP. IN EUROS
(Base year 2000)

Chart 5.4



Source: Department of Statistics.

2. Developments in economic activity by sector

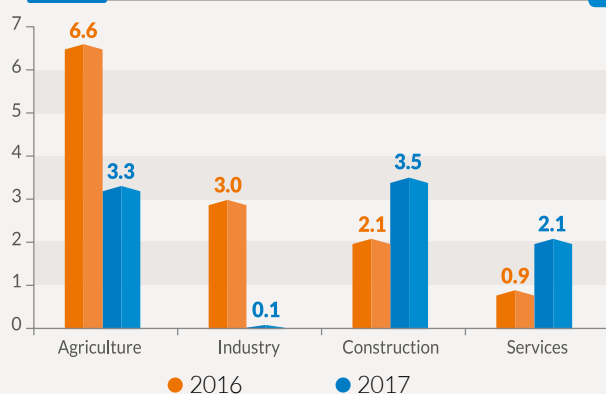
Developments in the major sectors show that Andorran real GDP growth in 2017 was led, as in recent years, by services (2.1%), which represent 88.5% of GVA, so their performance is usually a determining factor in the development of the Andorran economy. In second place, the positive contribution of construction also stands out, since the first clear signs of an upswing appeared in 2016. In contrast, industry held back economic growth with a very weak trend, and agriculture made a minimal contribution, due to its low percentage of GVA and a slowdown in activity compared with the previous year.

Specifically, the construction sector recorded real GVA growth of 3.5%, surpassing growth in 2016 (2.1%). This upswing is significant because it confirms the trend towards recovery that started one year before, after nine years of deep crisis, with major falls in GVA that left it, in 2015, 60% below the 2006 high. As a result, construction currently represents 5.9% of total GVA, compared with 12.6% just before the crisis.

Services continued to lead Andorran economic growth.

TREND IN GVA BY SECTOR
Interannual variation rate in real terms (%)

Chart 5.5



Source: Department of Statistics.

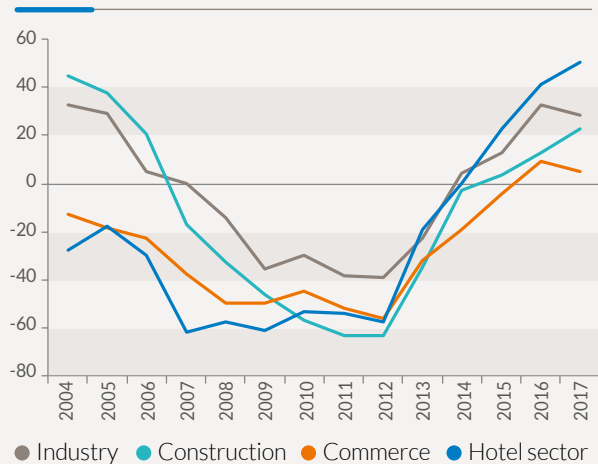
The improvement in construction can also be seen in the trends in most available indicators of activity for the sector. So, in 2017, an increase was seen in the number of employees (2.1%) and establishments (1.7%), similar to those in 2016, and also authorised square metres (62.5%) and imports of building materials (3.1%). Moreover, public investment saw a strong increase (19%), after the steep decline in 2016.

Along the same line, the results of the Chamber's surveys show a gradual recovery in the sector. So, business activities increased, with five consecutive quarters on positive ground,

TREND IN BUSINESS ACTIVITY BY SECTOR

Balance between the percentage of positive and negative replies

Chart 5.6



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

while businesses' replies about developments in contracted and executed works have consolidated the improvement that started in 2016, if at still very low levels. Altogether, this resulted in an upswing in sales figures (7%) and investment (10.7%).

Construction showed a gradual recovery from low levels of activity.

As for the industry and the manufacturing sector, the trend in 2017 was weak, although its impact on growth was limited by its relatively small share (5.1% of total GVA). So, real industrial GVA almost stagnated, compared with the increase of 3% it saw in 2016. It should be remembered that this sector is formed, on the one hand, by basic industry, based mostly on energy production and distribution and, on the other hand, manufacturing, the activity with the highest share - 69% of GVA from secondary activities.

The weakness in the whole of industrial and manufacturing activities that was seen in 2017, was reflected in a reduction in the number of employees (-0.7%) and stagnation in the number of businesses in the sector. However, a trend was also observed towards a gentle improvement in the climate of confidence in the sector, reflected in businesses' responses to the Chamber's surveys. Specifically, the annual average confidence indicator regained a positive balance, which had not been seen since 2002. Moreover, businesses' opinions on business activity remained at positive levels, although they dropped a little in relation to the previous year, as also

BUSINESSES' OPINIONS OF ECONOMIC DEVELOPMENTS IN 2017

Table 5.2

Results of the situation survey in industry

2017 COMPARED WITH 2016 (as % of businesses)

Turnover	Higher	41
	Same	42
	Lower	18
	Average variation (%)	3.1
Volume of investment	Higher	35
	Same	56
	Lower	10
	Average variation (%)	5.5
Number of employees	More	15
	Same	78
	Less	7

PROSPECTS FOR 2018 (as % of businesses)

Trend in turnover	Upward	34
	Stable	64
	Downward	3
Trend in volume of investment	Upward	25
	Stable	64
	Downward	11

Results of situation survey in construction

2017 COMPARED WITH 2016 (as % of businesses)

Turnover	Higher	53
	Same	38
	Lower	10
	Average variation (%)	7.0
Volume of investment	Higher	38
	Same	55
	Lower	8
	Average variation (%)	10.7
Number of employees	More	24
	Same	59
	Less	17

PROSPECTS FOR 2018 (as % of businesses)

Trend in turnover	Upward	32
	Stable	61
	Downward	7
Trend in volume of investment	Upward	27
	Stable	63
	Downward	10

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

Results of the situation survey in retail commerce

2017 COMPARED WITH 2016 (as % of businesses)		Total retail commerce	Food	Clothing & footwear	Household equipment	Health & hygiene	Electronics	Vehicles & accessories	Other commerce	Superm. & dept. stores
Sales figures	Higher	33	26	28	37	42	14	39	31	60
	Same	32	39	25	29	29	29	32	37	20
	Lower	35	35	47	34	29	57	29	32	20
	Average variation (%)	-0.8	0.9	-4.6	0.5	1.6	-8.8	1.4	-0.6	-1.0
Volume of investment	Higher	22	29	6	29	17	21	36	14	50
	Same	63	56	72	62	61	57	50	73	40
	Lower	15	15	22	9	22	21	14	13	10
	Average variation (%)	0.1	4.6	-1.7	0.5	-2.0	-3.2	2.7	-1.1	-0.6
Number of employees	More	15	15	3	12	14	14	39	10	22
	Same	79	79	88	79	73	79	57	85	78
	Less	7	6	9	9	14	7	4	5	0
PROSPECTS FOR 2018 (as % of businesses)										
Trend in sales figures	Upward	34	39	26	29	42	21	43	34	30
	Stable	52	58	55	56	50	29	43	58	30
	Downward	14	3	19	15	8	50	14	8	40
Trend in volume of investment	Upward	21	32	12	14	29	29	29	17	13
	Stable	61	59	56	77	54	57	46	67	38
	Downward	19	9	32	9	17	14	25	17	50

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

occurred with production. In contrast, the trend in the level of productive capacity utilisation continued to improve slowly, to reach a level around 70%, about 13 points higher than the minimum achieved in 2011, but still below the levels prior to the crisis. In this context, industrial companies indicated average increases in turnover (3.1%) and investment (5.5%), similar to 2016.

The dynamism in services was led by activities linked to tourism, in contrast with the weakness seen in commerce.

In 2017, services remained the most dynamic sector of the economy, led by the improvement in activities linked to tourism. This positive trend was still driven by the increasing numbers of tourists (6.5%), although the number of same-day visitors fell slightly. The upward trend in tourism was also evident in the increase in ski days sold (1.3% in the 2016-2017 season and 1.4% in the 2017-2018 season) and the number of total overnight stays (5.3%). In commerce, on the other hand, progress in activity was much slower, if you consider the slight growth seen in most indicators for the sector. Altogether, this resulted in much greater increases in the numbers of employees and establishments in hotels and catering than in commerce.

The growing dynamism in tourism was also reflected in the Chamber's surveys on the hotel sector, with a better evaluation of business activity than in 2016 and at levels that had not been seen for many years. The surveys also indicate increases in sales figures (3.7%) and investment (7.4%), though slower than in the previous year. In contrast, businesses in the commerce sector were less optimistic, with a less favourable opinion of business activity than expressed in 2016, also accompanied by a slight downturn in sales (-0.8%) and stagnation in investment.

BUSINESSES' OPINIONS OF ECONOMIC DEVELOPMENTS IN 2017

Table 5.4

Results of the situation survey in hotel sector

2017 COMPARED WITH 2016 (as % of businesses)

Turnover	Higher	57
	Same	32
	Lower	11
	Average variation (%)	3.7
Volume of investment	Higher	52
	Same	41
	Lower	7
	Average variation (%)	7.4
Number of employees	More	27
	Same	69
	Less	4
Source of clients per sales channel (as %)	Direct client / own web	18.7
	Internet / booking sites	53.7
	TO & travel agencies	24.5
	Others	3.2
Average stay of clients (nights)		2.4

PROSPECTS FOR 2018 (as % of businesses)

Trend in turnover	Upward	67
	Stable	31
	Downward	2
Trend in volume of investment	Upward	37
	Stable	54
	Downward	9

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

Altogether, the real GVA of the subsector Commerce, hotels and catering, transport, information and communications extended three years of quite high growth, by rising 4.4%, compared with 3.1% in 2016. Remember that this subsector's share is 32% of total Andorran GVA, so its development is very important to the whole economy.

The finance subsector was the branch of services that experienced the least favourable trend.

The finance subsector was the branch of services that saw the least favourable development, as occurred in 2015 and 2016. Official GDP figures show a slight increase in GVA in the subsector Financial, real estate, professional and technical activities, which was 0.5% in 2017, although this represents an improvement when compared to the declines seen in the two previous years. In any case, this subsector (which encompasses financial, real estate, professional and technical activities) is still the most important in the economy, with 37% of total GVA.

The weakness of activity was seen in a reduction in gross lending to customers (-5.0%) and deposits (-6.8%), which resulted in a drop in profits in the banking sector, for the fourth consecutive year, of 15.8%, and a cut

in employment in the whole financial and insurance sector (-4.1%). In any case, these figures need to be viewed within the special context that marked the sector from 2015, regarding Banca Privada d'Andorra (BPA) being put into administration by the Andorran National Institute of Finance (INAF), ending with the resolution of the entity.

Analysis of sectoral developments is completed by the primary sector which, in 2017, saw a slowdown in the rate of growth of real GVA, to 3.3%. This deceleration was accompanied by a decrease in the number of employees (-2.6%), in a context where the agricultural usable surface area and the tobacco harvest also declined (-0.9% and -10%, respectively). In contrast, the number of livestock increased (6.8%), after two years of decline. In any case, it should be noted that the size of the primary sector in the economy is very small (0.6%), so its impact on total GDP was very limited.

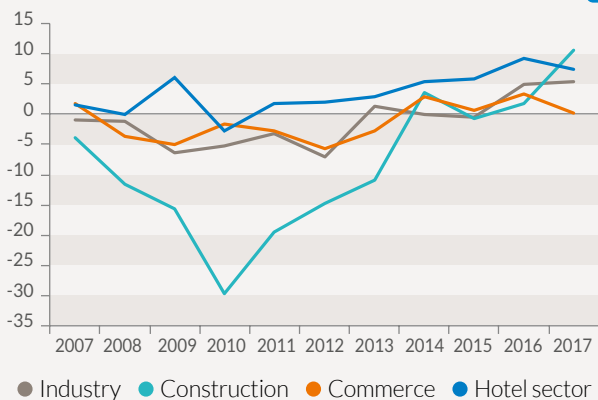
3. Developments in demand by components

By components of demand, available indicators show, in general, that domestic demand saw an upward trend, from levels that are still relatively low. The increase in population and employment generated favourable conditions for growth in residents' private consumption. This situation was

TRENDS IN INVESTMENT BY SECTORS

Interannual variation rate (%)

Chart 5.7



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

The gradual improvements in the economic context and business confidence continued to slowly add momentum to the investment dynamic.

reflected, for example, in an upswing in car registrations (19.1%), 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, the strongly rising trend continued in registrations of lorries and vans (15.5%), plus a recovery in investment in capital goods, as ascertained from the growth in imports of these goods (9.2%). Along the same line, the Chamber's surveys reflect a positive trend in investment in all the major sectors of the economy, except in commerce, where it has tended to stagnate. Accelerated investment in construction stands out, although it should be remembered that this was from very low levels. So, it appears that the gradual improvement in the economic context and in business confidence continues to add momentum to the investment dynamic.

Moreover, the public sector contribution to activity in 2017 was more favourable than the previous year, thanks to implementation of a less restrictive fiscal policy in both central and Comú government. So, both operating costs and real investment showed a more positive trend than in 2016, with increases in the aggregated data of both levels of government, of 4.3% and 19%, respectively. In parallel, fiscal pressure fell seven tenths to 24.5%, after reaching a historic high in 2016. Altogether, this resulted in a decline in the surpluses of both the central and Comú governments (to 0.3% and 1.2% of GDP, respectively). Despite this relaxation of fiscal containment, in 2017, GVA growth slowed in the subsector of Public administration, education, health, social and personal services, from 2.3% to 1.4%, which appears to be explained by the behaviour of the private branch of these activities.

As for the foreign sector, in 2017, there was an increase in imports (6.6%), higher than the previous year. However, this figure is influenced by rising fuel prices in 2017, so if this chapter is excluded, growth in imports was lower (5.4%). In parallel, exports accelerated, seeing an increase of 17% but, considering that the volume of exports is much lower than imports, this increase was not enough to shrink the trade deficit, which expanded to 5.8%. So, in 2017, the traditionally negative contribution from the trade balance to national GDP increased, correlating with the improvement in the economic situation.

In any case, the most significant contribution from the foreign sector to the Andorran economy comes from income from tourism services – the country's most important source of revenue – which continued its 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, the source of most visitors to Andorra.

In 2017, the traditionally negative contribution from the trade balance to GDP increased.

4. Prospects

As for the prospects for the Andorran economy in 2018, the results of the Chamber's surveys indicate continued expansion, at moderate but solid levels. By sectors, it is expected that the positive trend will continue to be led by services, especially those linked to tourism, together with a gradual recovery in construction activity. In contrast, the performance of industry and commerce will remain modest, in line with 2017. So, in all three sectors, positive replies exceed negatives replies about the trend in turnover and investment for 2017, with a notably more favourable gap in the case of hotel activity and a smaller gap in the case of commerce.

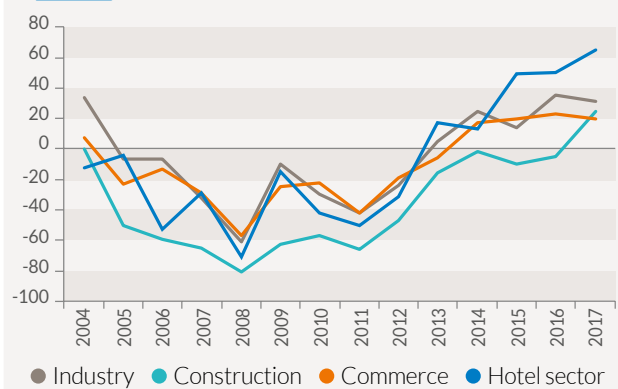
In 2018, the positive trend in the Andorran economy is expected to continue, led by services, especially tourism.

In 2018, the foreign sector can be expected to continue to drive Andorran economic activity, considering the predicted good performance of the Spanish economy and, to a large extent, of Europe as a whole, already confirmed in the first half of the year. In this context, it is expected that the Andorran economy will see an increase in GDP in 2018, for the sixth consecutive year, not far from the rate in 2017.

GDP data for the first quarter of 2018 are consistent with this forecast. So, Andorra saw real year-on-year economic growth of 2%, six tenths higher than one year before, but seven tenths less than the previous quarter. Now, a breakdown by sectors shows significant differences in trend. On the one hand, the strong acceleration seen in construction is notable, contrasting with the intensified decline in industrial GVA. For its part, the rate of growth in services slowed against the previous quarter, but is still on a positive path, as is agriculture. Within services, there was a notable increase in the subsector Commerce, hotels & catering, transport, information and communications (4.8% interannual). In contrast, the branch of Financial, real estate, professional and technical activities slowed, recording very weak growth (0.2%), although better than one year earlier. Finally, it should be noted that the tendency of the subsector Public administration, education, health, social and personal services to lose momentum continued, as in the last quarters, with a slight year-on-year increase of 1%.

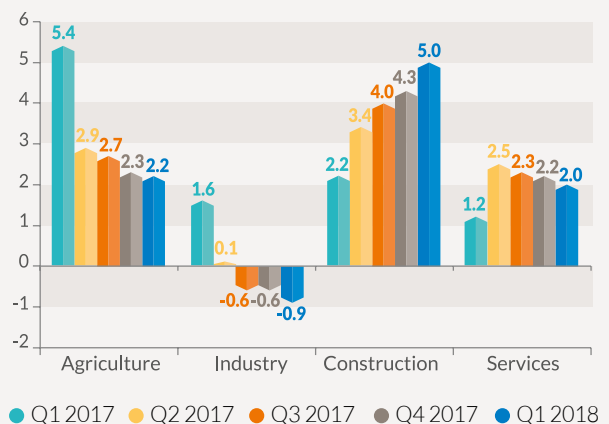
To end, the trend in the main available indicators of activity for the first few months of 2018 also indicate moderate levels of continued economic growth. So, a generalised upward trend can be seen, but in the case of some key indicators this is less intense than in the previous year.

EXPECTED TREND IN TURNOVER FOR THE NEXT YEAR - Balance between the percentage of positive and negative replies



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

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



Source: Department of Statistics.

The main available economic indicators for the first few months of 2018 show moderate levels of continued growth.

Specifically, a slowdown was seen in import growth until June and the number of tourists until May, plus a deceleration in car registrations. In contrast, employment was very dynamic until April, stronger than in the same period of 2017, driven by services, with a notable upturn in the financial sector and construction. Also notable is the strong growth in imports of building materials until June, demonstrating the recovery seen in this sector.

Box 5.1

ECONOMIC FORECASTS FOR ANDORRA FOR THE PERIOD 2018-2021

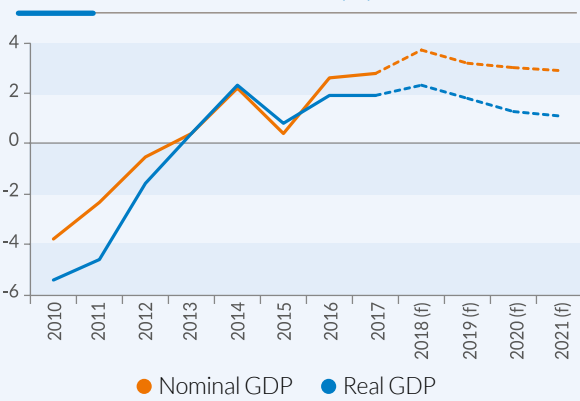
In 2018, the “Macroeconomic forecasts for Andorra” was published for the first time, according to Law 28/2017 of the 2018-2021 Statistics Plan and the Decree of 28.02.2018 approving the corresponding 2018 Annual Statistics Plan. It approaches the 2018-2021 forecast period, matching the timeframe applied to the preparation and updating of the Government’s budget framework. In the case of inflation, the forecast timeframe is limited to the 2018-2019 two-year period, as the reference framework provided by OECD outlooks is limited to the next two years.

The forecasts are based on various methods of statistical modelling and processing of the available historical series and, beyond the specific annual figures for each variable, their main value lies in the trend and order of magnitude they depict.

The scenario appears moderately positive, with a forecast of economic growth for 2018 of 2.3% real and 3.7% nominal, figures that imply a moderate upswing in comparison with 2017. In contrast, from 2019, a trend of gradual acceleration in GDP growth is expected, in line with forecasts for the neighbouring economies of Spain, France and the Eurozone. Accordingly, it should be remembered that the

FORECASTS OF NOMINAL AND REAL GDP IN ANDORRA 2018-2021

Interannual variation rate (%)



Source: Department of Statistics.

estimate of GDP growth in the first quarter was 2%, three tenths less than the forecast for the whole year.

In the case of inflation, forecasts indicate a slowdown towards an annual variation in the CPI of 1.7% in 2018 and 1.4% in 2019, contrasting with the 2.6% at which it ended the year. It should be added that in June 2018, inflation reached 1.9%, only two tenths over the forecast, after recording lower values in the first few months of the year.

SUMMARY OF FORECASTS FOR THE ANDORRAN ECONOMY 2018-2021

Interannual variation rate (%)

Year	GDP		GVA		WAGE BILL	NUMBER OF EMPLOYED	INTERNATIONAL TRADE IN GOODS (NOMINAL)		CONSUMER PRICE INDEX
	Nominal	Real	Nominal	Real	Nominal		Imports	Exports	
2018	3.7	2.3	2.8	1.3	4.0	2.6	1.8	3.6	1.7
2019	3.2	1.8	3.7	2.3	3.1	2.3	4.2	-2.0	1.4
2020	3.0	1.3	3.2	1.4	2.7	2.1	3.1	2.5	-
2021	2.9	1.1	2.9	1.0	2.4	1.8	2.2	2.1	-

Source: Department of Statistics.

In summary, a global view of the first few months leads us to believe that the Andorran economy will continue to grow throughout 2018. This progress will still be driven by the tourism sector, thanks to continued dynamism in the Spanish and European economies, with a growing contribution from construction and a slow recovery in the financial sector.

VI. Prices and costs

1. Consumer prices

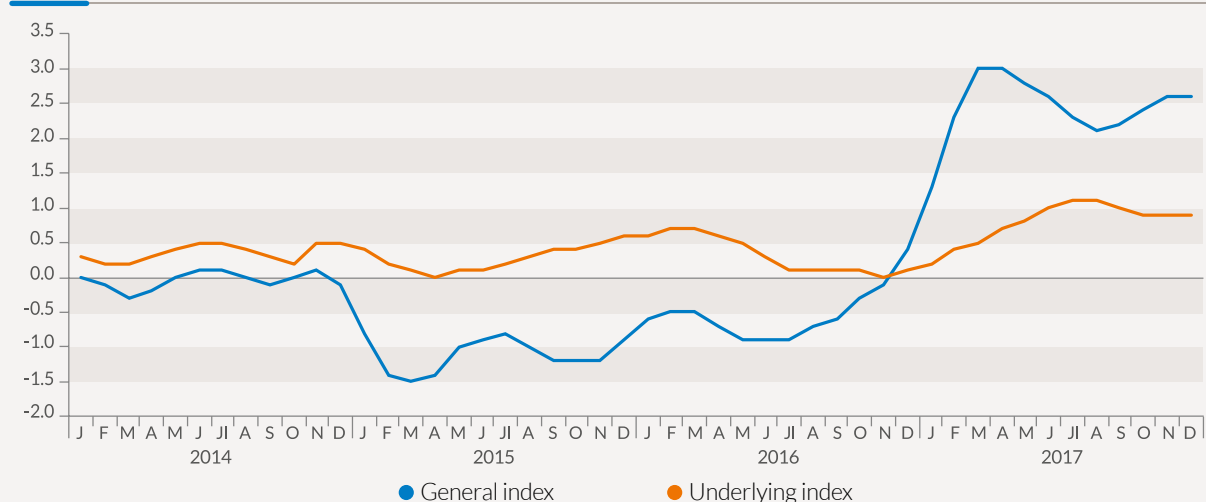
In 2017, the Andorran economy escaped the deflationary pressures that had marked the previous four years, thanks to increasing demand and rising oil prices. This trend matches those of European economies and, especially, Andorra's neighbours and main trading partners, with indices moving upward in comparison with 2016.

The profile of consumer prices was of fast acceleration until April, when inflation reached 3%, then wavered within the range of 2.1%-2.6% until the end of the year. So, the financial year ended with inflation at 2.6%, the highest rate in the last decade and well above the 0.4% of one year ago. Consequently, price acceleration in Andorra was faster than in Spain and France (1.2% harmonised inflation in both cases), the source of most consumer goods, and the Eurozone as a whole (1.4%), undermining the price competitiveness of the Andorran economy.

In Andorra, prices accelerated faster than in Spain and France or the Eurozone as a whole.

By components, the trend in prices varied greatly. Of note are the increases in the components of health, transport, leisure, shows and culture, and food, beverages and tobacco, which saw strong acceleration compared with the previous year. Rising energy prices is one of the main factors explaining the upward trend in the transport component. The increase was much more limited in the case of hotels, cafés and restaurants which, nevertheless, is the only component that has not undergone an annual price decrease since the historical series became available. Inflation in the

CONSUMER PRICE INDEX FOR ANDORRA - Interannual variation rate (%)



Source: Department of Statistics.

Chart 6.1

housing component also rose moderately, due to the impact of energy prices. In this context, electricity prices charged to the final consumer increased by 0.5% on average.

In contrast, there are four components where prices fell, some significantly: first and notably are clothing and footwear, accumulating seven years of reductions within the last eight financial years and reflecting the long-term stagnation that affects demand in commerce. Secondly, the fall in education prices, for the first time since data became available. Goods and services also saw prices fall at the end of 2017, for the sixth consecutive year. Finally, the component of furniture, domestic appliances and household services saw a slight decrease, after several years of very gentle increases.

The behaviour of prices according to special groups shows that the main source of inflationary pressures in 2017 was energy (7.2%), linked to rising oil prices, as occurred, but less intensely, in 2016. Moreover, there was also an upward trend in food prices, with an increase of 3.8%, much stronger than in 2016 (0.6%). In contrast, the prices of services stabilised, a trend that highlights continued low dynamism in demand.

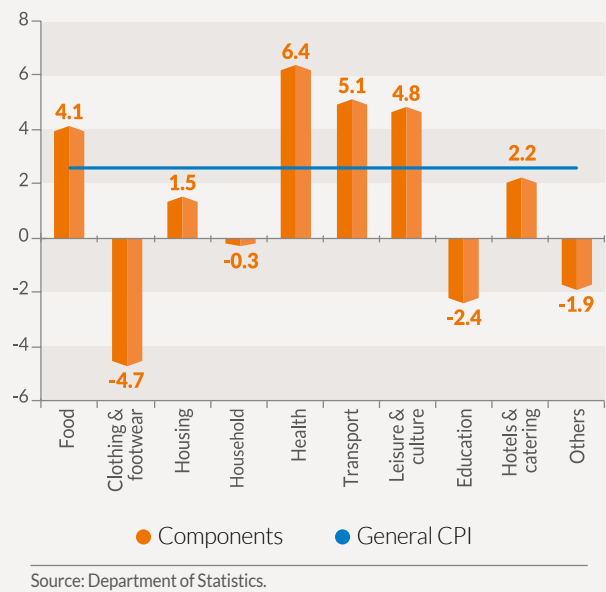
In sum, underlying inflation – which excludes energy and food and measures the trend in core prices – was 0.9%, compared with 0.1% in 2016, well below general inflation for the second consecutive year. It is also notable that this figure aligns with the underlying inflation rate in Spain (0.9%) and France (0.8%), and is even slightly lower than that of the Eurozone as a whole (1.1%), unlike the situation in general inflation. Altogether, this shows that the core components are the most volatile, which explains the inflationary pressures in Andorra in 2017, and also that, in the underlying trend, Andorran prices develop in a controlled manner that is well in line with the main competitors.

2. Wages

In 2017, the average wage in Andorra was 2,076 euros, the same figure as in the previous year. This stabilisation occurs after several years of erratic variations (2014-2016), partly influenced by the introduction of the IRPF (personal income tax) in 2015, which temporarily modified the wage bonus policy of some companies. The fact is that from a historical perspective, the average wage in Andorra has risen slowly, in a context of no inflationary pressures until 2016. In contrast, rising inflation in 2017 led to employees suffering a reduction in purchasing power of 2.6 points, largely counteracting the increase they obtained in 2016 (3.9 points). Nevertheless, in cumulative terms, the average wage has increased 3.9% since 2013, while the cumulative increase in consumer prices for the same period was 1.8%, meaning an

CONSUMER PRICE INDEX. DECEMBER 2017
Interannual variation rate (%)

Chart 6.2



The main source of inflationary pressures in 2017 was energy.

From a historical perspective, the average wage in Andorra has increased slowly, in a context of no inflationary pressures.

increase in purchasing power of 2.1 points in the last four years.

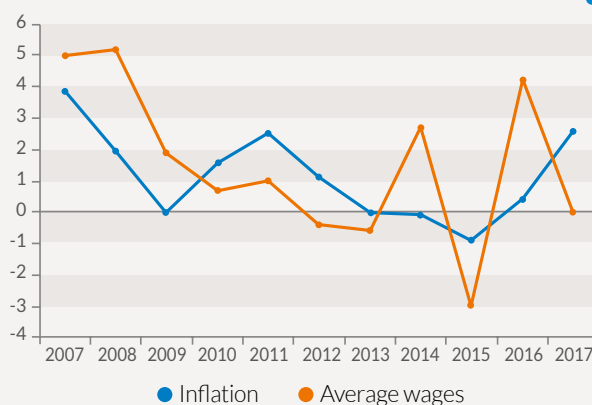
In the case of the minimum interprofessional wage, the trend was more favourable than in the average wage since, last year, the Government announced its commitment to raising it 1.5% per year until the end of its term. The aim is to bring the minimum wage up to half the average wage which, as stated, is around 2,000 euros, following the recommendations of the European Committee of Social Rights. As a result, the minimum hourly wage in 2017 rose to 5.72 euros per hour (for workers aged 18 and above), equalling 991.47 euros per month, for a 40-hour working week.

From a sectoral point of view, the wage stabilisation seen in 2017 is the result of very diverse trends. The negative trend in the financial sector stands out, where the annual average wage fell 5.6%. Other sectors that saw cuts are health activities and domestic work for the community. At the other extreme is construction, with a wage increase of 3.2%, the only one above inflation. The other sectors saw moderate wage increases, notably hotels and catering (2.3%) and commerce (1.7%), due to their high impact on the Andorran economy. Moreover, this positive trend can be seen as a sign that the situation in these sectors is tending to improve, if slowly. As for public administration, the wage increase was 1.1%, a figure that represents a slowdown compared with the previous year. Finally, it should be remembered that the trend in the extraction

AVERAGE WAGES AND INFLATION

Interannual variation rate (%)

Chart 6.3



Source: CASS (Andorran Social Security System) / Department of Statistics.

The average wage in the financial sector fell 5.6%, but was still the highest.

AVERAGE WAGES BY SECTORS (euros)

Table 6.1

	2017	% var. 17/16	Average index in Andorra = 100
Agriculture, livestock, hunting and forestry	1,508.16	3.7	72.6
Extraction industries	1,812.84	-42.3	87.3
Manufacturing industries	2,096.70	1.7	101.0
Production and distribution of electricity, gas and water	3,271.70	1.2	157.6
Construction	1,968.91	3.2	94.8
Commerce and motor vehicle repairs (etc.)	1,765.91	1.7	85.1
Hotels and catering	1,550.56	2.3	74.7
Transport, storage and communications	2,283.25	1.0	110.0
Financial system	4,871.55	-5.6	234.6
Real estate & rental activities; business services	1,924.51	1.0	92.7
Public administration, defence & compulsory social security	2,556.89	1.1	123.1
Education	2,188.28	0.6	105.4
Health & veterinary activities, social services	2,258.88	-0.9	108.8
Other social activities & community services, personal services	1,810.26	1.8	87.2
Households employing domestic staff	1,347.57	1.7	64.9
Extraterritorial bodies	2,321.65	-26.0	111.8
Domestic work for the community	1,356.61	-0.4	65.3
Average	2,076.31	0.0	100.0

Source: CASS (Andorran Social Security System) / Department of Statistics.

industries and extraterritorial bodies must be set aside from the analysis for reasons of statistical representativeness, as they are sectors where very few people work and therefore the variation in one single wage can vary the total dramatically.

The analysis of wage levels demonstrates that, in 2017, the gaps between sectors narrowed after widening in 2016. So, the highest wage is 3.6 times higher than the lowest wage (3.9 in 2016 and 3.3 in 2015). Specifically, the highest wages are in the financial sector, for yet another year, where wages are 2.3 times higher than the average. This contrasts with households employing domestic staff which, with wages 35% below the average, is the lowest-paid sector. The second sector in the wage ranks is that of production and distribution of electricity, gas and water, with wages 58% higher than the average, followed by public administration – which pays 23% more – and extraterritorial bodies – with wages 12% higher than the average. Behind these but above the average are transport, storage and communications; health and veterinary activities and social services; education, and the manufacturing industries.

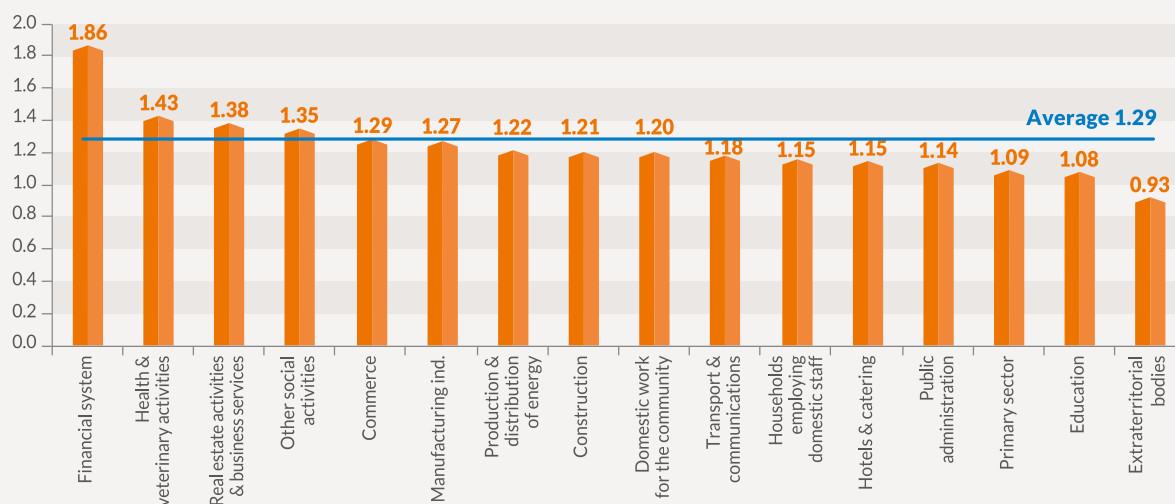
The other branches lie below the average wage level, with percentages that vary between 5% in construction, a sector that is below the average for the eighth consecutive year, whereas before the crisis it had traditionally been above, and the 35% below average for domestic work for the community. Within this group of sectors are notably the cases of commerce and hotels and catering, which employ a large part of the Andorran population (36.6% of total employees), with wages at 15% and 25% below the average, respectively. It should be added that in these two sectors, the gap with the average wage narrowed a little this year but, nevertheless, since 2004, both have cumulatively lost about 5 points against the average.

Men's wages were 29.2% higher than women's, narrowing the gap in comparison with the previous year.

To complete the analysis, it is worth highlighting that wage levels by gender show that in 2017 in Andorra, women's average wages were 1,808.9 euros, compared with 2,336.3 euros for men. Therefore, men's wages are 29.2%

higher than women's. This gap has narrowed against the previous year, when it was 30.3%. This occurs in all sectors, with the sole exception of extraterritorial bodies, where women's wages surpass men's, although this branch is much less significant in Andorran employment.

WAGE QUOTIENT MEN/WOMEN BY SECTORS. 2017



Source: CASS (Andorran Social Security System) / Department of Statistics.

Box 6.1

FACTORS THAT INFLUENCE WAGES IN ANDORRA

The new Workforce Survey, published for the first time this year, provides new data about wages in Andorra that enable greater in-depth analysis of the factors that influence them.

According to this source, the average estimated monthly wage in 2017 is 1,714.15 euros net and the median monthly wage is 1,500 euros net for an average of 40 hours per week. As these amounts are stated in net terms, they are not directly comparable with those published by the CASS (Andorran Social Security System), which are also analysed in this chapter and which are higher.

By gender, women earn on average 1,523 euros net per month and men 1,880 euros net. So, 54.4% of men earn more than 1,950 euros net per month, compared with 38.9% of women. One of the main reasons for these inequalities in the average and the distribution of wages is that women more often work part-time and in less well-paid sectors than men.

By level of education, it can be seen that the higher the level of studies, the higher the wages. This relationship can be seen in both men and women, with a gender gap

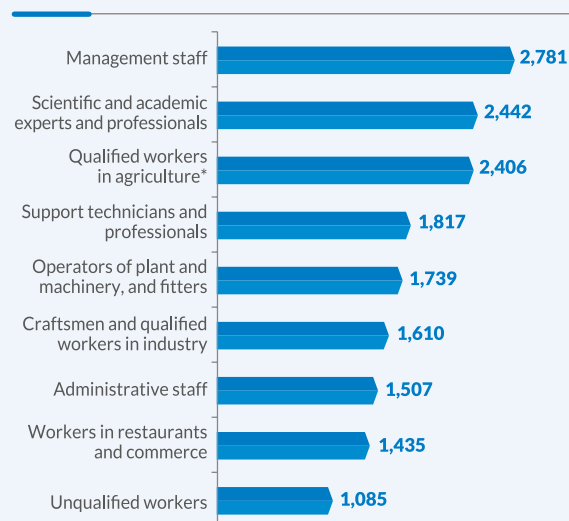
that is quite regular. So, the average wage with tertiary studies is 2,231 euros net, 2.3 times the average wage obtained without studies.

By type of working hours, in 2017 full-time workers obtain an average monthly wage of 1,805 euros net, while part-time workers earn an average of 802 euros net. Again, the gender pay gap is similar, irrespective of the type of working hours.

Regarding the type of contract, seasonal work is lower paid than permanent contracts. 40.1% of employees with temporary contracts earn less than 1,200 euros net per month; in contrast, only 16.7% of permanent employees receive this wage. On the other hand, 43.9% of employees on permanent contracts receive monthly wages above 1,950 euros net, while 28.5% of employees on temporary contracts receive this level of wages.

The average monthly wage also rises on the basis of seniority in the main job and varies between 1,290 euros net in the case of workers who have worked for at least one year and 1,996 euros in the case of workers who have worked for ten years or more.

AVERAGE WAGES BY TYPE OF JOB Euros net/month



(*) Insufficient number of observations.

Source: Workforce Survey. Department of Statistics.

By type of job, the average monthly wage of management staff is the highest, followed by scientific and intellectual experts and professionals, and qualified workers in agriculture. In contrast, the lowest average monthly wages were for unqualified workers and workers in restaurants and commerce.

As for type of employer, the monthly wage is higher in the case of self-employed workers (2,310 euros net on average) than in the case of those working for others. Among the latter, wages in the public and semi-public sector stand at 2,024 euros net, while in the private sector these are estimated at 1,517 euros net.

In conclusion, the factors in Andorra that favour higher average wages are the level of education, the length of the working day and duration of the contract, seniority, the level of professional qualification and self-employment.

Leaving the extraction industries aside, for reasons of statistical representativeness, the greatest gaps are found in the financial sector, where men's average wages are 86% higher than women's; in health and veterinary activities, where they are 43% higher, and in real estate activities and business services, where they are 38% higher. These data demonstrate that in these sectors men occupy most high-level jobs. In contrast, the smallest gaps occur in education, the primary sector and public administration (where men's average wages are 8-14% higher than women's).

VII. The foreign sector

1. Foreign trade flows

The trend in Andorran imports of goods in 2017 was positive, with growth of 6.6%, raising the total figure to 1,307.5 million euros. By chapters, the highest contributions were from motor vehicles (1.9 percentage points) and fuels (1.6 percentage points), while, at the other extreme, the most negative contribution was from the chapter of clocks and watches (-0.3 points).

Imports of tobacco and tobacco substitutes – another important chapter for the Andorran economy – saw an increase, for the second consecutive year, of 3%. This increase was less than that of imports as a whole so, if excluded from the total, growth in imports without tobacco rises a little, to 6.7%. In relation to the degree of sectoral concentration of Andorran imports, a stabilisation in the situation can be seen. So, the percentage of the three largest groups (food, transport material and products of the chemical industries) was 40.3% of the total, one tenth more than they represented in the previous year. Taking the top five (adding machinery and electrical equipment and textiles, in fourth and fifth position in 2017, respectively), the percentage of the total increases to over 60%, highlighting the high level of concentration that is still a feature of Andorran foreign trade.

Exports recorded the highest value since 2011.

Accordingly, the trend in Andorran exports rose in 2017, with growth for the third consecutive year, of 17%, the most positive level since 2011. In absolute terms, the volume of exports was 106.2 million euros, the highest in the last decade. As a result, the rate of coverage rose seven tenths to 8.1%, the highest level in the last eleven years.

The trend by sectoral groups shows that the increase in exports was quite generalised and accompanied by a decrease in concentration. Specifically, the percentage of the three top export groups (machinery and electrical equipment, transport material and optical, photographic and

Motor cars and fuels are the chapters that contributed most to growth in imports in 2017.

FOREIGN TRADE
Interannual variation rate (%)



Source: Department of Tax and Frontiers.

Chart 7.1

TRADE DEFICIT - Millions of euros

Chart 7.2



Source: Department of Tax and Frontiers and own preparation.

precision apparatus) was 62.8% of the total sales, 0.8 points less than in the previous year. Nevertheless, this is a rather high percentage and much higher than that of imports.

It should also be considered that part of Andorran imports are later re-exported. In fact, taking the ten top imports and exports chapters, there are five matches: “motor vehicles”, “electrical machinery and equipment”, “mechanical apparatus”, “articles of apparel and clothing accessories, not knitted or crocheted” and “pearls, precious stones and metals”. This seems to indicate so-called intra-industry trade and/or so-called bidirectional trade (one country is both exporter and importer of one type of product), in which added value that is generated for the national economy or opportunism in commercial trading operations become essential factors and assets.

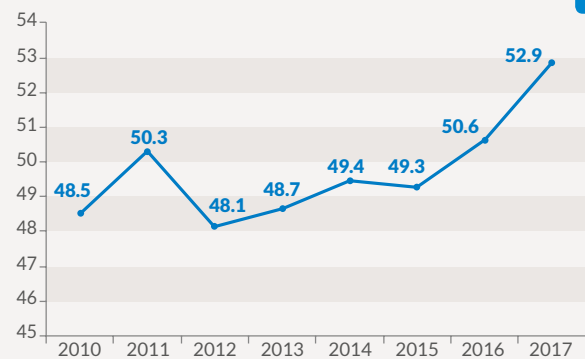
In the case of Andorra, these are products that allow commercial trading operations on an international scale, with significant differences in value between countries which an intermediary can use to his advantage, or the creation of activities linked to coupling with the creation of an added value in Andorra that takes advantage of a market niche.

The trends in both exchange rates and regulatory amendments in international trade are important factors that influence the re-exportation of products. In 2017, the euro exchange rate appreciated, resulting in more favourable conditions for importing products from countries outside the monetary union and then exporting them into the Eurozone.

As for regulation, 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 in chapters 1 to 23 in the harmonised system and, equally, continue to exclude tobacco from the customs union for a transition period of 30 years, to allow for conversion of the sector. This could open up new opportunities for trade between Andorra and the EU, since the EU has been putting increasing legislative obstacles in place in recent years that limited the possibilities of re-exportation by Andorra.

OPENNESS RATE (%)

Chart 7.3



Source: Department of Tax and Frontiers and own preparation.

The trade deficit increased, driven by the improvement in the Andorran economic context.

The combined result of the increase in imports and exports in 2017 was the increase in Andorra's traditionally high trade deficit, slightly surpassing the threshold of 1,200 million euros, the highest figure recorded since 2008.

This trend was motivated by the improvement in the Andorran economic context, which drove the demand in imported consumer products (both domestic and for tourism) and investment.

Finally, this trend also resulted in an increase in the openness rate of the economy (expressed by the value of foreign trade in goods as a percentage of GDP), by more than 2 points, to 52.9%, narrowing the gap with the values of 55% that were achieved before the crisis.

2. Geographical distribution of foreign trade

2.1. Imports

In 2017, imports from Europe, the main geographical source of Andorran imports, concentrated 90.9% of the total, 1.1 points less than the previous year, when this percentage hit a historical high. This trend was the result of a lower increase in imports from the EU (5.7%) than in the total, despite being the largest increase recorded since 2002.

Euro appreciation favoured non-European imports.

The behaviour of imports from other continents was also positive. In relative terms, the role of Africa is notable (118.6%) and America (60%), clearly better than in 2016. Consequently, the

FOREIGN TRADE BY GEOGRAPHICAL AREAS

Table 7.1

	IMPORTS			EXPORTS		
	Meuros 2017	% var. 2017/16	% total 2017	Meuros 2017	% var. 2017/16	% total 2017
Spain	832.3	5.9	63.7	57.1	24.1	53.8
France	180.4	-5.5	13.8	17.9	33.5	16.9
Germany	44.4	24.7	3.4	1.1	-72.1	1.0
Italy	38.0	37.9	2.9	1.7	27.9	1.6
United Kingdom	15.7	-10.2	1.2	0.3	-3.3	0.2
Netherlands	11.9	6.9	0.9	1.3	-1.8	1.2
Portugal	11.4	6.2	0.9	0.2	-18.3	0.2
EU-28	1,167.1	5.7	89.3	81.7	20.8	77.0
Switzerland	16.7	-10.2	1.3	0.6	-10.6	0.6
Europe	1,189.1	5.3	90.9	88.6	20.7	83.4
USA	15.8	98.1	1.2	1.2	20.9	1.2
America	21.2	60.0	1.6	2.7	-34.1	2.6
China	48.3	13.9	3.7	0.6	-66.0	0.6
Vietnam	7.0	6.4	0.5	0.0	-12.1	0.0
Asia	83.0	12.3	6.3	7.1	13.1	6.7
World total	1,307.5	6.6	100.0	106.2	17.0	100.0

Source: Department of Tax and Frontiers.

percentage of both continents increased, to 0.4% and 1.6%, respectively, an importance that had not been achieved in the latter case since 2005. As for Asia, the second largest supplier to Andorra, the trend also rose strongly (12.3%) and accelerated in relation to the previous year, so its share of the total increased three tenths to 6.3%.

Within the EU, purchases from Spain, Andorra's main supplier, increased 5.9%. The percentage of total purchases fell four tenths to 63.7%, after reaching a historical high in 2016. So, in 2017, Spain was the country that contributed most to growth in imports (3.8 points), as occurred in the last few years. In the case of France, the opposite occurred, with a fall of 5.5%, contrasting with the increases seen in the last two years. Consequently, its share of the total shrank to 13.8%, a historic low, much lower than it represented in the nineties, above 30%. However, France remains the second largest supplier to Andorra, well above the third.

As for the other EU countries, Germany consolidates third place in the ranking of suppliers to Andorra, with an increase of 24.7%, raising its percentage to 3.4%. Next comes Italy, also with a strong increase in imports (37.9%) to represent 2.9% of the total. In contrast, purchases from the United Kingdom fell 10.2%, so its percentage fell two tenths to 1.2%.

The other EU countries have a very small share, of less than 1%, so their contribution to total growth is not very important. Outside the European Union, the major contraction in imports from Switzerland stands out (-10.2%) for the third consecutive year, with the second most negative contribution to import growth from a European country, after France. As a result, its percentage of the total fell two tenths to 1.3%, returning to values that are more in line with historical levels, after an exceptionally high level in 2014.

Imports from the USA and Japan practically doubled in 2017.

In relation to imports from countries in the rest of the world, generally only imports from the USA and some Asian countries have any relevance. It is true that in certain years, one

or other country would join them, but this was not the case in 2017. The trend in purchases from the USA was very positive, as it practically doubled those of the previous year, combining four consecutive years of rises and putting its percentage of the total at 1.2%, the same as the United Kingdom.

Along the same line, purchases from Asian countries saw an increase of 12.3%, stronger than the previous year. Of note is the increase from China (13.9%), which raised its share of the total by two tenths, to 3.7%, remaining the largest Asian supplier to Andorra and third in the global ranking, only behind Spain and France. Finally, the strong increase in imports from Japan is notable, almost doubling and putting its share of the total at 0.4%. Equally, this figure is far from what it represented in the nineties and before the last economic crisis, related to the loss of attractiveness of the Andorran electronics trade over the last few years.

In summary, in 2017, the trend towards an increasing concentration of imports from Spain slowed, to the benefit of other European countries, such as Germany and Italy, and non-European countries, such as the USA and Japan. In parallel, France continued to lose importance as a supplier, in line with the background trend observed over the last twenty-five years, while the importance of China and the Asian continent to Andorran imports grew, in line with this region's ever more important role in world trade.

France continued to lose importance as a supplier to Andorra, while the Asian continent's importance to Andorran imports grew.

2.2. Exports

The dynamism in Andorran exports in 2017 (17%) can be explained, basically, by the good performance of sales in Europe. So, the rate of growth in exports to the EU – the main destination of Andorran exports – accelerated to 20.8%, combining three years of upward trends, favoured by the good performance of the European economy. As a result, the EU percentage of total exports increased 2.4 points to 77%, after reaching a historical low in 2016 (74.6%).

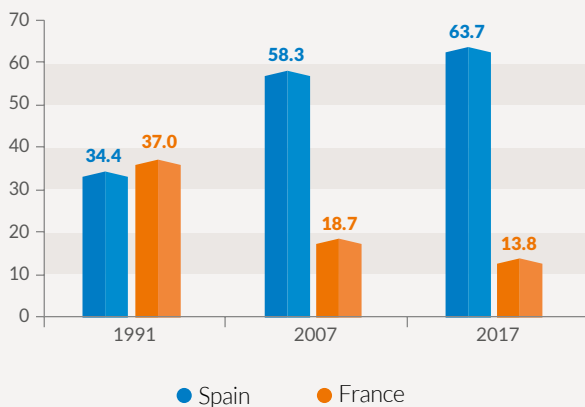
In 2017, exports to Spain and France grew strongly.

By countries, in 2017, Spain, the main consumer of products from Andorra, recovered some of the ground lost in the last two years, with an increase in exports of 24.1% and a contribution to growth of 12.2 points, raising its share of the total to 53.8%. France's progress was even stronger, with an increase of 33.5% and a contribution to growth of 5 points, raising its share of the total to 16.9%. Nevertheless, the balance between Andorra's two main partners is still very unequal, favouring Spain, unlike the similar shares both countries had at the beginning of the nineties.

By countries, in 2017, Spain, the main consumer of products from Andorra, recovered some of the ground lost in the last two years, with an increase in exports of 24.1% and a contribution

IMPORTS FROM ANDORRA'S NEIGHBOURING COUNTRIES - Percentage of total (%)

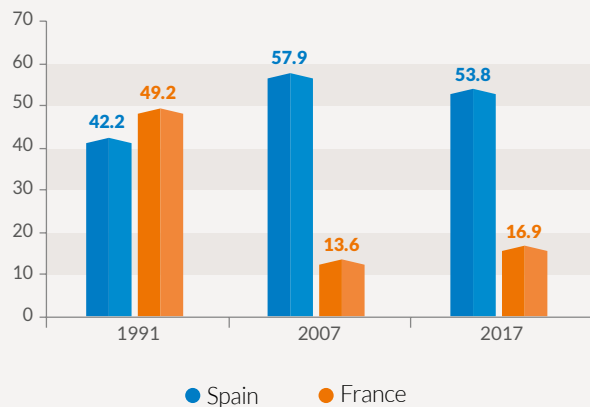
Chart 7.4



Source: Department of Tax and Frontiers.

EXPORTS TO ANDORRA'S NEIGHBOURING COUNTRIES - Percentage of total (%)

Chart 7.5



Source: Department of Tax and Frontiers.

As for the other EU-28 countries, the trend was uneven. The Belgian market stands out, where exports more than tripled, raising its share 1 point to 1.5% and making it the eighth destination in Andorra's export ranking. Exports to Italy also rose significantly (27.9%), raising its share one tenth to 1.6% and its position in the ranking to seventh. In contrast, there was a strong decline in sales to Germany (-72.1%) and, to a lesser extent, to the Netherlands (-1.8%), reducing their share to 1% and 1.2%, respectively. In this way, Germany went from being the fourth destination for Andorran foreign sales to eleventh. The other EU-28 countries have a share of less than 1%, so their contribution is insignificant.

Outside the EU, sales to the rest of Europe also rose strongly (19.7%), for the second consecutive year. As a result, their percentage of the total increased one tenth to 6.4%. Specifically, the contribution from Norway was notable, as exports to that destination grew 24.4%, strengthening its position as third in Andorra's export ranking, after Spain and France, with a share of 5.5%. In contrast, the contribution from Switzerland was negative, with a drop in sales to that country (-10.6%), lowering its share to only 0.6%, compared with the 4.6% it represented in 2010.

The rest of the world's share of total Andorran sales fell 2.5 points, to 16.6%, a trend that was largely influenced by euro appreciation, making sales outside the area less competitive.

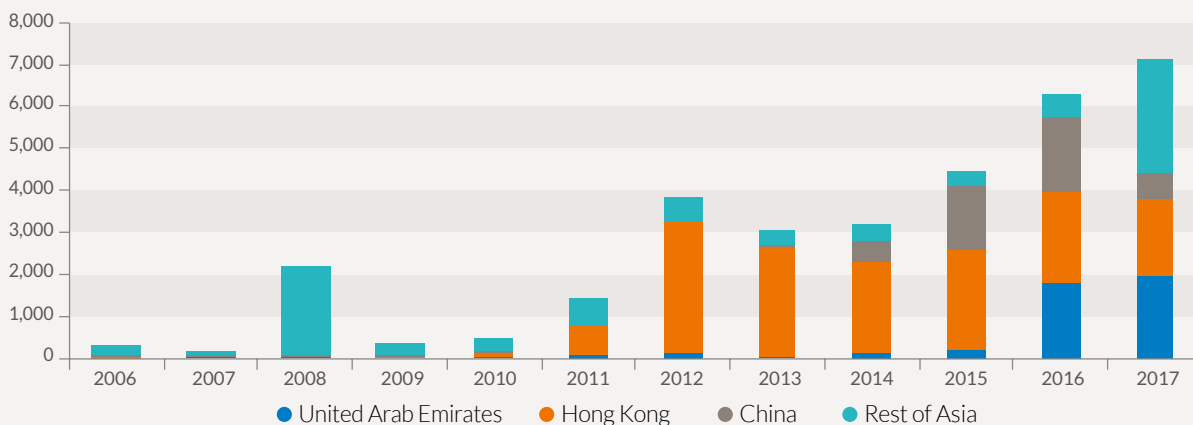
Euro appreciation slowed Andorran exports to the rest of the world.

Accordingly, the decline in exports to the American continent is notable (-34.1%), breaking three years of strong growth, so that its share shrank 2 points to 2.6% of the total. This trend can be explained by the steep fall in sales to markets such as Chile, Mexico and Colombia; on the other hand, sales to the USA showed significant dynamism (20.9%), raising its share to 1.2%.

In contrast, in 2017, the contribution from the Asian continent was positive, growing 13.1%, adding 0.9 points to the total growth. Now, this growth can be explained almost exclusively by the specific contribution from Kuwait, a market that had no significance in the past but which, in 2017, was the destination of 1.6% of Andorran exports. In contrast, the more traditional Asian markets, such as Hong Kong and China, saw major declines that limited their share of the total to 1.7% and 0.6%. Among the Asian markets, the United Arab Emirates also stands out, as Andorran exports there increased 10.1% and represented 1.8% of the total. As a whole, the share of the Asian continent fell two tenths to 6.7%, though in absolute terms it achieved a historical high. Finally, the decline in exports to Africa should be mentioned (-80.6%), leaving its share at only 0.2%.

In summary, Andorran exports still focus on neighbouring economies. Developments outside these economies are inconsistent and influenced by specific transactions and the incidence of the euro exchange rate on the relation between competitiveness and price. On a positive note, there is a notable background trend for the Asian continent to gain importance as a market of destination, led by certain specific countries. This trend is consistent with the growing participation of this region in international trade which, as said, is also reflected in the trend in imports.

ANDORRAN EXPORTS TO ASIA - Thousands of euros



Source: Department of Tax and Frontiers.

3. Sectoral composition of foreign trade

3.1. Imports

The positive trend in Andorran imports that has been seen since 2017 was the result of increases in most sectoral groups. The highest contributions were from transport material (2.3 percentage points) and mineral products (1.6 percentage points). Other groups that also made positive - if limited - contributions are machinery and electrical equipment (1.1 percentage points), food

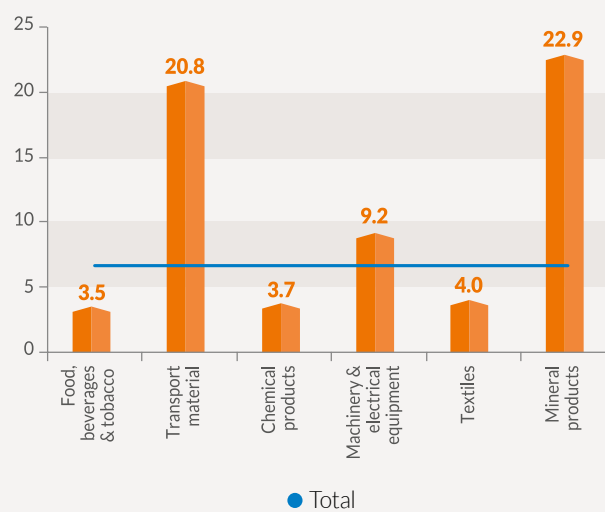
products, beverages and tobacco (0.6 percentage points) and products of the chemical industries (0.5 percentage points). At the opposite extreme, the group that detracted most from import growth is Optical, photographic and precision apparatus (-0.4 percentage points) and pearls, precious stones and metals (-0.2 percentage points), contrasting with 2016, when it made the most positive contribution.

Growth in imports of food, beverages and tobacco, the group with the highest share, slowed to 3.5%.

A more detailed analysis highlights that fact that, in 2017, growth in imports of food, beverages and tobacco, the group with the highest share, slowed to 3.5%. As a result, its share of the total fell half a point to 15.4%, but is still, nevertheless, at the top of the ranking for the eighth consecutive year. The most important chapter in this group is beverages, alcoholic liquids and vinegars, with a share of 6.1% of total Andorran imports, after seeing growth of 2.9% in 2017. The second most important chapter is tobacco, which saw similar growth (3%) but whose share continued to fall (2.1% of total foreign purchases), in the context of a decline in the tobacco harvest in Andorra.

ANDORRA'S MAIN IMPORT SECTORS.
2017 - Interannual variation rate (%)

Chart 7.7



Source: Department of Tax and Frontiers.

Among the import groups with notable trends in 2017 was transport material, with growth of 20.8%, continuing the strong upward trend started in 2013. So, this group made the most positive contribution to growth (2.3 percentage points), even improving the level of the previous year, in which it already contributed 1.6 percentage points. Consequently, its share of the total increased 1.5 points, to 12.6%, the highest level in the historical series and a figure that lifted it two places, to second place in the import ranking. The explanation for this progress can be found in the intense growth of imports of the chapter of motor vehicles, tractors, motorcycles and bicycles (16.9%) – the most important in the group, with 12% of total imports – consistent with vehicle registrations in the Andorran market and also the increase in re-exports of those vehicles.

Imports of transport materials grew strongly, driven by the dynamism in vehicle registrations and re-exports.

The progress of the group of chemical products was slower, with growth in imports of 3.7%, compared with 6.3% in 2016. This performance caused its share to drop four tenths to 12.2%, relegating it to third place in the ranking. The chapters that most explain this trend are perfumery – the most important chapter in the group, with a share of 7.7% of total imports – which grew 4.6%, and pharmaceutical products – second in importance, with a share of 2.3% – which increased 0.8%.

The trend in imports of machinery and electrical equipment was more positive, with an increase of 9.2%, much higher than the 1.9% in 2016, bringing 1.1 percentage points to total growth, the group with the third most positive contribution. This performance increased its share of the total by three tenths, to 12%, falling one place to fourth in the ranking of foreign purchases.

The increase in imports from this group can be explained by the growth in electrical machinery and equipment (11%) and, to a lesser extent, in mechanical apparatus (6.7%) which could partly be related to the increase in re-exports also seen in those two chapters. Another factor favouring this trend is the improvement seen in investment and the consumer electronics trade in Andorra.

As for textiles, imports saw an increase of 4%, cutting its share of the total by three tenths, to 8.3%, although it remains in fifth place in the imports ranking. This increase means an improvement from the stagnation seen in 2016, but is still too weak to be able to speak of an improved trend in clothing sales. In fact, the results of the Chamber's surveys indicate that it was quite weak in 2017.

Mineral products are the group with the highest growth in imports (22.9%) and second largest contribution (1.6 percentage points) to the good performance of foreign purchases in 2017. As a result, the group's share of the total

Mineral products are the group that saw the highest growth in imports, thanks largely to rising oil prices.

rose one point to 8.1%, putting it in sixth place in the imports ranking. The reason for this strong progress is the high increase in imports of fuel, oils and mineral wax (23.9%), the most important chapter in the group – with a share of 7.7% of total imports. This increase, in turn, can be explained by the rise in average prices of fuel purchases associated with the increase in oil prices,

FOREIGN TRADE BY SECTOR

Table 7.2

	IMPORTS			EXPORTS		
	Meuros 2017	% var. 2017/16	% total 2017	Meuros 2017	% var. 2017/16	% total 2017
Live animals & animal products	65.4	4.6	5.0	0.1	9.2	0.1
Vegetable products	27.3	3.1	2.1	0.0	271.4	0.0
Fats & oils	5.7	-1.8	0.4	0.1	14.6	0.1
Food products, beverages & tobacco	201.2	3.5	15.4	0.5	2.4	0.4
Mineral products	106.3	22.9	8.1	0.2	39.2	0.2
Products of the chemical industries	159.9	3.7	12.2	1.7	75.6	1.6
Plastics, rubber & articles thereof	27.7	6.0	2.1	0.9	-49.8	0.8
Fur, leather & articles thereof	15.6	5.0	1.2	1.0	18.9	0.9
Wood, cork & articles thereof	9.8	2.2	0.7	1.1	2.9	1.0
Paper & graphic arts	28.3	-0.9	2.2	5.7	26.8	5.4
Textiles	109.0	4.0	8.3	6.8	5.2	6.4
Footwear, headgear, umbrellas, etc.	36.6	0.7	2.8	1.9	13.7	1.8
Stone, cement & ceramic articles	13.3	-2.6	1.0	0.3	28.8	0.3
Pearls, precious stones & metals	35.9	-7.3	2.7	10.7	41.3	10.1
Base metals & articles thereof	33.8	1.8	2.6	5.1	32.2	4.8
Machinery & electrical equipment	156.9	9.2	12.0	31.4	19.0	29.6
Transport material	165.2	20.8	12.6	21.0	16.0	19.8
Optical, photographic, precision app.	47.5	-9.0	3.6	14.3	7.7	13.4
Arms & ammunition	0.9	-9.7	0.1	0.1	71.9	0.1
Miscellaneous manufactured articles	55.6	3.4	4.3	2.5	-2.1	2.4
Works of art, antiques	5.4	92.5	0.4	0.8	18.4	0.8
Total	1,307.5	6.6	100.0	106.2	17.0	100.0

Source: Department of Tax and Frontiers.

easily offsetting the reduction in imported litres (-0.2%). So, if this chapter is discounted from total imports, it appears that the increase in imports in 2017 was lower (5.4%) and decelerated against the previous year (7.5%). In the case of purchases of salt, sulphur, earths and stone, plastering materials, lime and cement, the second most important chapter in the group, the increase was more modest (6.5%) but much better than the previous year (-14.3%), in line with the beginning of the recovery in the construction industry.

Far behind mineral products come imports of live animals and animal products which, in 2017, saw an increase of 4.6%, stronger than in the previous year (2.7%), but below average, so their share of the total fell one tenth to 5%. This trend can mostly be explained by the increase in imports of meats and edible offal, and milk and dairy produce (4.7% in each case).

Finally, the trend in groups of products with a share of less than 5% of foreign purchases was varied. The increase in works of art and antiques is notable (92.5%), but in the other cases, variations from the previous year were much slighter. With a negative trend, the reductions in optical and photographic imports (-9%) and pearls, precious stones and metals (-7.3%), appear to indicate unfavourable behaviour in the trade in these types of products.

3.2. Exports

In 2017, Andorran exports continued and accelerated the rising trend started in 2015, with significant growth of 17%, higher than the 12.6% recorded in the previous year. This trend can largely be explained by the positive contributions of the groups of machinery and electrical equipment (5.5 percentage points); pearls, precious stones and metals (3.5 percentage points), and transport materials (3.2 percentage points). In contrast is notably the negative contribution from plastics, rubber and articles thereof (-1 percentage points) which, together with miscellaneous manufactured articles, were the only export groups that have worsened since 2016.

The largest export group in 2017 is still, as it has been since 2003, machinery and electrical equipment, which saw a significant increase of 19%. This makes three consecutive years of increases, bringing its share of the total to a notable 29.6%. By chapters, this progress can be mainly explained by the increase in electrical machinery and equipment (16.5%), the most important chapter in the group and in all exports – with 24.1% of total foreign sales. Sales of mechanical apparatus also developed positively (30.9%), exceeding the increase in imports of those products.

Foreign sales of machinery and electrical equipment grew for the third consecutive year and consolidate their position as the largest export group.

Transport material is still in second place in the exports ranking, with an increase of 16%, well in line with the figure in 2016. So, transport material's share of total foreign sales remained practically stable at 19.8%. The chapter that determines this behaviour is motor vehicles, which represents 99% of the group and saw an increase for the fifth consecutive year, of 19.6%.

The trend in foreign sales of optical, photographic and precision apparatus, the third largest export group, was more moderate, with a rise of 7.7%, contrasting with the declines seen in the previous two years. As a result, its share of the total fell to 13.4% and its contribution to the variation in exports was 1.1 percentage points. By chapter, the trend was divergent, with a strong increase in exports of optical and photographic products (15.6%), the most important chapter in the group (10.1% of total exports), contrasting with the fall in sales of clocks and watches (-19.9%).

In fourth place in the ranking by volume of exports was the group pearls, precious stones and metals, among those that grew most in 2017 (41.3%), following the strongly rising trend of the previous two years, so it almost tripled its share of the total since 2014, to reach 10.1%, a historic high. This trend contrasts with the reduction in imports of those products in 2017, raising the coverage of this group to 29.8%, the second highest after optical, photographic and precision apparatus.

The group of pearls, precious stones and metals has practically tripled its share of total exports since 2014.

After the group pearls, precious stones and metals comes the group textiles, which saw much lower growth, with an increase of 5.2% which, nevertheless, is an improvement on the decline it saw in 2016. So, its share of the total fell six tenths to 6.4% and its contribution to total growth was quite small (0.4 percentage points). Within this group are notably the contributions from the chapter articles of apparel and clothing accessories, not knitted or crocheted – the most important chapter in the group, with 3.6% of total exports – which grew 6.4%, and articles of apparel and clothing accessories, knitted or crocheted (11.3%), putting the share of the total at 0.9%.

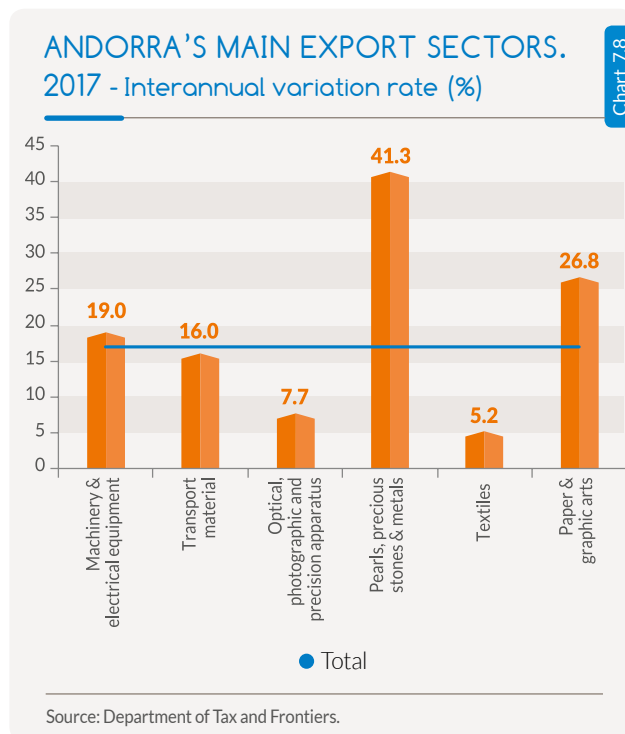
The trend in the group paper and graphic arts was much more favourable, with export growth of 26.8%. As a result, its share of the total rose to 5.4%, making a contribution to total growth in exports of 1.3 percentage points, divided almost equally between the chapter of paper and cardboard and products of the printing or graphic industries.

The other groups represent a share of less than 5% of total exports and mostly showed a positive trend, notably products of the chemical industries (75.6%) and the group footwear, headwear, umbrellas, etc. (13.7%), which contributed 0.8 and 0.3 percentage points, respectively, to export growth. In contrast was the negative contribution from plastics, rubber and articles thereof (-1 percentage points), the result of a decline of 49.8%. This was the only group where exports fell in 2017, together with miscellaneous manufactured articles (-2.1%).

4. Foreign investment flows

To complete the analysis of the foreign sector, it should be noted that Andorra continues to establish itself as an attractive destination for foreign investment. So, in 2017, 774 investment applications were received, in line with the average in the last two years, representing a total volume of formalised investment of 83 million euros. This figure is around 3% of GDP, eight tenths less than the volume in 2016 but still a significant figure.

The geographical distribution of formalised investment shows that Spain is still by far the largest investor country (52%), followed at a distance by France (23%). The rest is divided among various geographical locations. This year, it is interesting to see the increase in investment from more



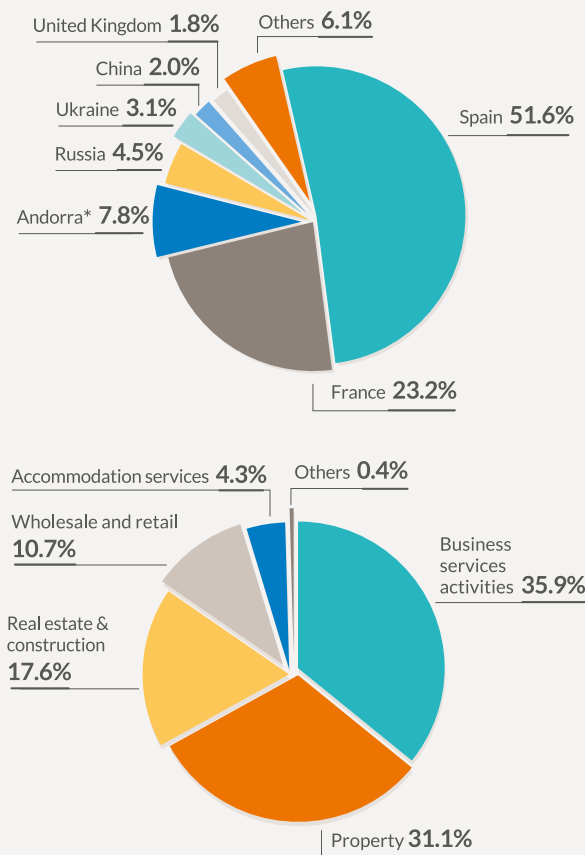
distant countries which, to date, had little investment in Andorra, such as Russia, Ukraine, China and the United Kingdom.

Globally, since 2012, when the current foreign investment law came into force, Spain has concentrated 52% of formalised investment in Andorra, and France, 19%. The rest is spread among many countries, including notably Switzerland (3.8%), Belgium and Luxembourg (3.7% in both cases). Moreover, it is calculated that this investment has had a cumulative impact on the Andorran labour market of about 1,600 jobs in the period 2012-2016 (2017 data not yet available), including jobs created in new businesses and those created through the acquisition of already existing businesses.

By sectors, in 2017, formalised investment was notable in the field of business services activities (36% of the total), followed by property and real estate and construction. Globally, since 2012, the leading sectors have been property (32%), business services activities (26%), wholesale and retail (20%) and real estate and construction (15%). Other sectors that received foreign investment over the last few years, but at much lower levels, are accommodation services; portfolio investment; projects, design or research activities, and manufacturing.

FOREIGN INVESTMENT BY COUNTRIES AND SECTORS. 2017 - As % of total

Chart 7.9



(* Andorran businesses with foreign capital (>50%) that invest in new businesses.

Source: Ministry of the Economy, Competitiveness and Innovation.

VIII. The public sector

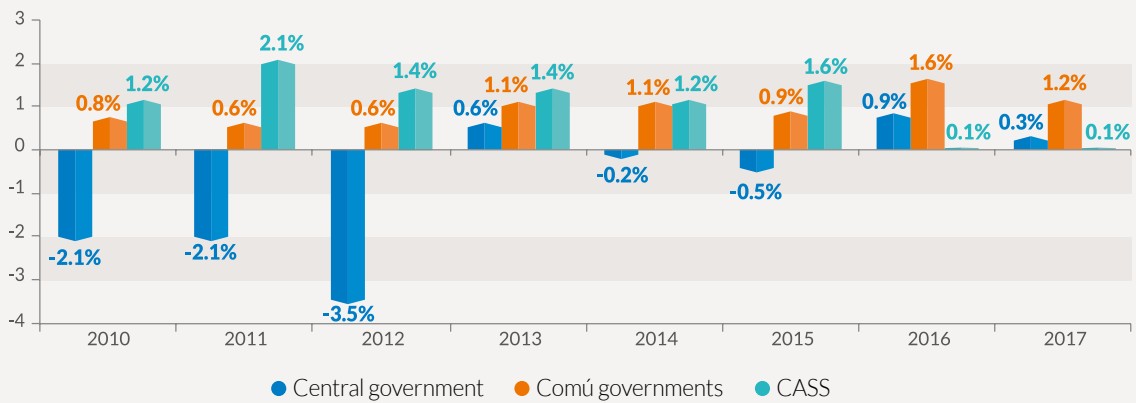
The performance of the Andorran public sector in 2017 was marked by the recurrence of budgetary surpluses at all three levels of public administration (the central Government, local Comú governments, and the Andorran Social Security System - CASS), based on an already consolidated tax model. This helped to diversify and bolster sources of public finance. However, the surpluses obtained in 2017 were lower than one year earlier, partly due to increased Comú expenditure on investment and a notable rise in operating costs.

Specifically, the Government surplus shrank to one third of the 2016 figure, to 0.3% of GDP, while that of the Comú governments fell four tenths, to 1.2% of GDP, having risen significantly in the previous year. The CASS also obtained a surplus, but similar to the previous year (0.1% of GDP). As official statistics do not currently publish the consolidated budgetary balance of all the administrative bodies, we cannot confirm the net economic effect of the performance of the whole Andorran public sector, although it would appear to be expansionary.

In 2017, the budgetary surpluses of the central and local governments shrank, while remaining low in social security.

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

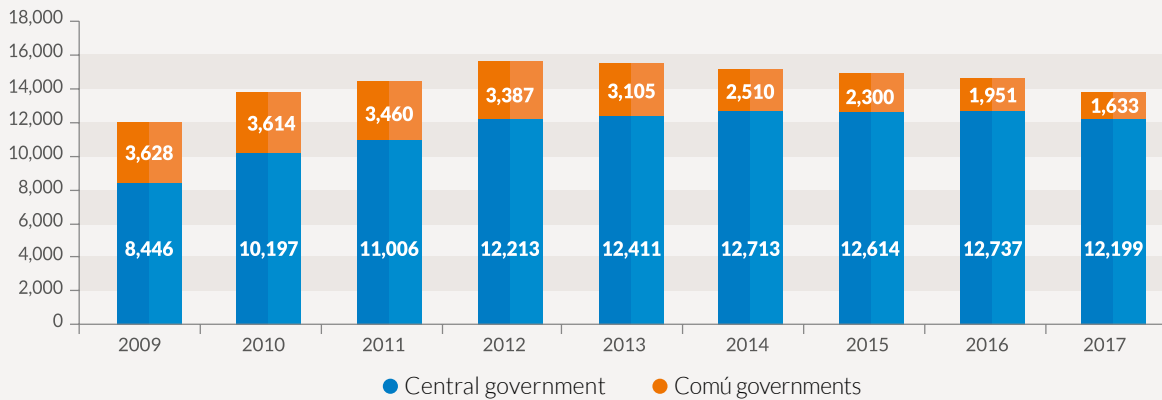
Chart 8.1



Source: Ministry of Finance, Comú governments, CASS, Department of Statistics of the Government and own preparation.

PER CAPITA DEBT (€/person)

Chart 8.2



Note: data published by the Comú governments for 2017 and data reviewed by the Court of Accounts for the other years. Calculated by taking the estimated population as the base.

Source: Ministry of Finance, Comú governments, Court of Accounts and own preparation.

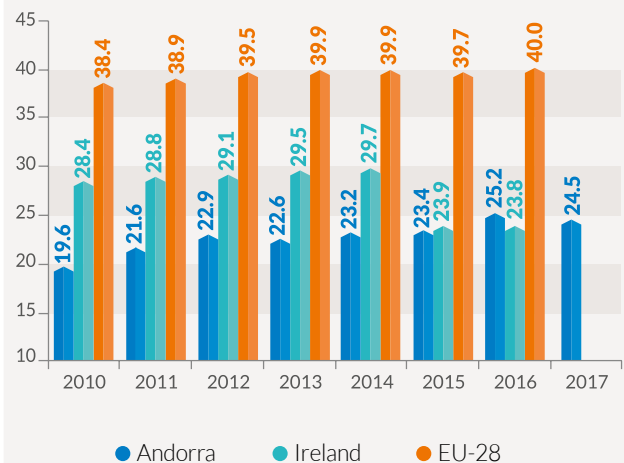
Levels of public sector debt continued to fall.

The achievement of surpluses made it possible to continue the path of lowering levels of public debt, started in 2013 after a historic high in 2012. So, the total debt of Andorra (central and Comú governments) was 1,034 million euros, equal to 38.7% of GDP, a percentage that is below the 50% limit set by the Law on public finance sustainability. So, per capita debt (calculated from the estimated population) reached 13,831 euros, 5.8% less than in 2016, the fifth consecutive annual reduction.

In this context, it is estimated that Andorra's tax burden, according to the accrual principle,

ANDORRA'S TAX BURDEN IN THE EUROPEAN CONTEXT (as % of GDP)

Chart 8.3



Source: Department of Statistics.

fell seven tenths to 24.5%, after reaching a historic high in 2016. This figure contrasts with that of 18% in 2009, but is much lower than the European average of 40% (according to 2016 data) or the level of our closest European neighbours: France (47.6%) and Spain (34.1%), a value that makes Andorra a tax-friendly country. In fact, in the context of the EU-28, the only country with a similar tax burden to Andorra is Ireland.

Andorra's tax burden fell seven tenths to 24.5%, after reaching a historic high in 2016.

Box 8.1

FINANCIAL SUSTAINABILITY TARGETS AND BUDGETARY AND FISCAL STABILITY FOR 2018

According to the provisions of chapter three of Law 32/2014 on financial sustainability and budgetary and fiscal stability, the preparation and approval of the annual budgets of the central and Comú governments must be adjusted to the general budgetary framework that covers the term of mandate. It is also stipulated that the Court of Accounts must annually publish the financial sustainability and budgetary and fiscal stability targets for the central and Comú governments, to be considered when preparing and monitoring their budgetary framework.

The targets set for 2018 are detailed below:

DEBT TARGETS 2018

(as % of GDP)

Debt target for Andorra	43.3%
Debt target for central Government	36.9%

DEBT TARGETS OF COMÚ GOVERNMENTS 2018

(as % of average settled total revenue in the three, immediately-preceding calendar years)

Canillo debt target	180.0%
Encamp debt target	99.7%
Ordino debt target	170.0%
La Massana debt target	138.5%
Andorra la Vella debt target	110.0%
Sant Julià de Lòria debt target	171.0%
Escaldes-Engordany debt target	114.0%

PERMITTED EXPENDITURE TARGET 2018

Central Government permitted expenditure target	€ 450,919,283
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CURRENT OR OPERATING EXPENDITURE TARGET 2018

(growth rate)

Central government current expenditure target	3.3%
Canillo current expenditure target	6.0%
Encamp current expenditure target	2.5%
Ordino current expenditure target	1.3%
La Massana current expenditure target	2.4%
Andorra la Vella current expenditure target	3.0%
Sant Julià de Lòria current expenditure target	1.0%
Escaldes-Engordany current expenditure target	1.3%

DIRECT TAX TARGET PERCENTAGE 2018

Target percentage of direct tax in total direct and indirect taxes of central government	35.6%
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Compared with the situation in 2017, it is evident that the public authorities have a margin of manoeuvre to increase expenditure and debt. It should be noted that:

the debt targets set for 2018 are much higher than the levels seen in 2017.

the permitted expenditure target for the central Government also exceeds the settled totals in 2017.

Altogether, with the favourable economic context expected to continue, this indicates that it should be feasible for the authorities to stay within the targets set for 2018. However, it is notable that the central Government budgets for 2018 already predict an increase in current expenditure of 3.4%, exceeding the set target of 3.3% by one tenth.

Next, we analyse the performance of the public sector in 2017 at each level of government.

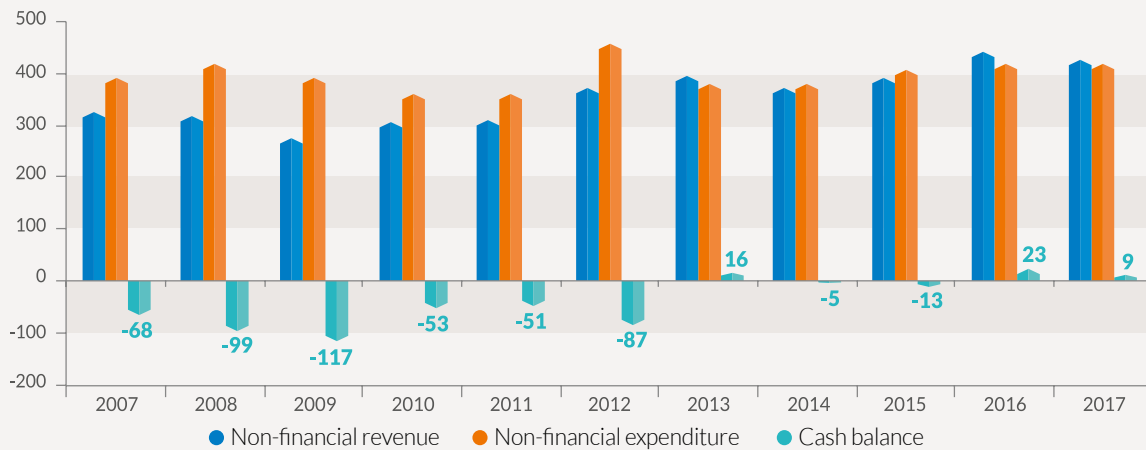
1. Central Government

According to the provisional settlement data for the 2017 budget, the Andorran Government's accounts closed with a non-financial cash surplus of 9.08 million euros, for the second consecutive year, representing 0.3% of GDP. However, this balance is much lower than that of 2016, due to a reduction in revenue (-3.5%) which was only partly offset by slight containment of expenditure (-0.5%).

The reduction in Government revenue was partially offset by containment of expenditure.

In any case, it should be noted that, in 2016, the surplus reached a record figure of 22.6 million euros (0.9% of GDP), breaking the Andorran Government's historical trend of settling budget settlements with deficits. So, over the period of seventeen years between 1998 and 2015, the Government had always registered a deficit, with the sole exception of 2013, when the surplus it obtained was the result of a special entry for revenue from the distribution of profits from Andorra Telecom, rather than the annual results.

GOVERNMENT BUDGET EXECUTION - Millions of euros



Source: Ministry of Finance.

Now, if the financial transactions carried out over the year are added to this non-financial surplus for 2017, a negative budget result is obtained, of 5.1 million euros, contrasting with the very positive result in 2016 (the highest in twenty-six years). Looking at the detail of these financial transactions, the most notable movements relate to various debt transactions intended to renew issuances that matured in 2017 (for a total of 460 million euros) and to substitute a loan policy with debt (for the amount of 60 million euros). In parallel and as a consequence of that issuance, the available balance of the loan policies was reduced from 124 to 50 million euros.

The global debt of the Government shrank for the first time since 2001.

So, the global debt of the central Government shrank for the first time since 2001, to 912 million euros, 2% less than in 2016, when it hit a historic record. Within the debt structure

is notably the increase in the outstanding balance of public debt, to 770 million euros (the rest are loans and policies), triple that of eight years ago. In proportion to GDP, this debt volume represents 34.1%, 1.7 points less than in 2016, a reduction that distances it from the 40% limit established for the central government by the law on public finance sustainability, holding it well below the level of the great majority of European governments. It should also be noted that the term structure of the debt is 75.8% long-term and 24.2% short-term debt, compared with

the 43%-57% division in 2016, meaning that, together with the surplus obtained in 2017, the conditions of the Government's public finance sustainability have improved.

1.1. Revenue

In 2017, settled non-financial revenue was 423.4 million euros, 3.5% less than the previous year, with a budget execution rate of 102%. This decline can mostly be explained by two reasons: on the one hand, a significant decrease in revenue from direct taxes, after six years of strong increases associated with the gradual introduction of new tax forms, a process that culminated in 2015 with the entry into force of personal income tax (IRPF) and, on the other hand, falling investment income.

In 2017, revenue from direct taxes fell, after six years of strong increases.

GOVERNMENT NON-FINANCIAL REVENUE
Thousands of euros

Chart 8.5



Source: Ministry of Finance.

In contrast, income from indirect tax and other taxes and revenue increased, but not enough to offset the decline in the other entries. Other revenue was also obtained from current transfers and the sale of investments, although they have minimal relevance in absolute terms.

Detailed analysis shows that income from direct taxes fell 14.1%, interrupting six years of strong growth and cutting total revenue to 71 million euros. The budget execution rate for this revenue was 96% and this chapter's share of total non-financial revenue fell 2.1 points, to represent 16.8%. Consequently, it still only represents 19.6% of total direct and indirect taxes, well below the limit of 40% set by the Law on public finance sustainability, passed in 2014.

The fall in revenue from direct taxes was basically motivated by the decline in corporate tax (-35.1%), with revenue of 26.4 million euros,

as more negative budgetary settlements were made for tax refunds. In relation to tax liability deductions, there are two factors that help to explain this result: first, deductions for employing staff increased as there are more workers in the labour market and, secondly, deductions for investment also increased due to the growing tendency of the Andorran business network to capitalise fixed assets. To this must be added that the profits in some economic sectors, such as banking, were lower than the previous year, resulting, logically, in lower revenue.

Along the same line, income from economic activities declined 18.5% although, in this case, revenue has become insignificant since personal income tax (IRPF) came into force in 2015, as income from economic activities was then taxed by the IRPF instead of the tax on economic activities.

The other direct tax forms have developed positively in 2017. In particular, the IRPF brought 29.9 million euros into the public coffers, as a result of an increase of 4.9%, showing positive behaviour in family income. Consequently, the IRPF became the main source of revenue from

In the field of direct tax, the IRPF has become the main source of revenue, surpassing corporate tax.

direct taxes, surpassing corporate tax. Equally, revenue from the capital gains tax on property saw a steep increase (42.2%), to 2.8 million euros, which can be explained by an increase in the number of transactions in the Andorran property market.

The analysis of direct tax is completed by the income tax on non-residents (IRNR), which saw an increase of 3.7%, to 12.1 million euros in revenue, contrasting with the steep decline in the previous year. It should be noted that this tax has been affected by the signing of various double taxation agreements, those with Spain and France being especially relevant, being the origin of most businesses offering services to Andorra. So, the change in trend seen in 2017, after the first year

Indirect taxes are still by far the most important source of finance for the Government, with the IGI being the main form.

of application of the agreements, is indicative of regularisation of the situation and another sign of improvement in economic activity.

In relation to indirect taxes, revenue in 2017 grew 0.8%, to 293 million euros, a figure that exceeds the budgetary provisions (104%), but

represents deceleration since the previous year. In any case, this entry is still by far the most important source of finance for the Government, with a total share of non-financial revenue of 69.2%, almost 3 points more than in 2016.

Within this type of revenue, the top tax form by volume of income is the indirect general tax (IGI), a tax on consumption that has been in force since 2013. The trend in this tax in 2017 has been positive, with an increase in net settled revenue of 3.3%, to 132 million euros, representing an execution rate of 107% and indicating a progressive improvement in Andorra's economic activity.

In second place, a moderate increase was also seen in revenue from taxes on foreign trade, of 0.9%, to 108 million euros. This trend occurred in a context where the general rate of tax on tobacco consumption increased on 2 March 2017. The most important concept within this section is the consumption tax, a custom duty on agricultural products imported into Andorra (import chapters 1-24), with a notable percentage in beverage and tobacco imports and providing almost 100% of revenue from foreign trade.

Along the same line, special taxes, the third largest tax form in volume of revenue, generated almost 46 million euros, with an increase of 1.2%. These taxes are applied to imports and manufactures of certain products, such as alcohol, tobacco and fuels, so the slightly rising trend in 2017 is linked to the gentle increase in imports of those products, especially beverages and tobacco.

The other indirect taxes, with a lower share of total revenue, showed diverse trends. On the one hand, revenue from property transfer tax (ITP) increased 7.2%, to 2.5 million euros, boosted by a greater volume of property transactions carried out in Andorra. On the other hand, declines were seen in revenue from the gambling tax (-5.8%) and the ISI service tax (-53.2%). In the latter case, it should be remembered that the banking and financial sector ISI is no longer applicable (since the IGI came into force in 2013) and the decline in 2017 is due to special regularisation that took place in the third quarter of 2016, so it does not reflect any trend in the sector. So, taking into account the sole ISI in force, on insurance, revenue in 2017 was 3.4% higher than the previous year.

In parallel, revenue from other taxes and revenue saw growth of 9.1%, to 26.9 million euros, interrupting three years of falls. This increase surpassed the budgetary provisions, with an execution rate of 107%, raising its share of total settled revenue by seven tenths, to 6.4%. More detailed analysis by entries shows that the increase was well distributed. In first place is notably the rise in revenue from duties (10.5%), an entry that is closely linked to the general trend in the

EXECUTION OF THE GOVERNMENT BUDGET ⁽¹⁾ (Million euros)

Table 8.1

	Settlement 2017	% variation 2017/2016	% execution 2017 ⁽²⁾
Direct taxes	71.3	-14.1	96
On capital gains on property	2.8	42.2	157
On personal income (IRPF)	29.9	4.9	120
On companies / economic activities	26.5	-35.1	70
On non-residents' income	12.1	3.7	121
Indirect taxes	292.9	0.8	104
On property transfers	2.5	7.2	139
On consumption of goods (IGI)	132.0	3.3	107
On consumption of services (ISI)	3.1	-53.2	99
Special taxes	45.6	1.2	102
On foreign trade	108.5	0.9	101
On gambling	1.3	-5.8	102
Other taxes and revenue	26.9	9.1	107
Current transfers	0.1	-15.7	-
Investment income	32.0	-20.7	91
Real investment sales	0.2	1,087.3	-
Non-financial revenue	423.4	-3.5	102
Current expenditure	368.3	0.6	98
Personnel costs	110.8	4.9	100
Consumption of goods and services	45.0	2.3	92
Financial expenditure	13.8	-15.0	94
Current transfers	198.7	-0.7	98
Capital expenditure	46.0	-8.5	61
Real investments	39.9	-10.5	61
Capital transfers	6.1	6.9	67
Non-financial expenditure	414.3	-0.5	92

(1) Settlement of 2017 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 postponed to the following financial year, and the modifications and increases in budgetary credit. In 2017, these modifications represented an increase of 2.5% on the initial budget for non-financial expenditure.

Source: Ministry of Finance.

economy. There was also growth in revenue from service provision (6.3%), sales of goods (6.7%), drawbacks (53.2%) and, to a lesser extent, the entry for other revenue (4.4%).

In the field of service provision, we would mention, on the one hand, "registrations", which grew 10% due to an increasing volume of services carried out at the Vehicle Registry, and, on the other hand, the concept "other services", which grew 7.4%, the result of a combination of various factors. On the positive side is notably the special contribution from the Congress of the International Commission for Alpine Rescue, organised in Andorra in 2017, and on the negative side, the lower revenue from withholding tax on savings income, affected by the context of extraordinarily low interest rates in recent years. On the last point, it should be remembered that Andorra carries out these retentions to implement Law 11/2005, of 13 June, adapting the Agreement between the Principality of Andorra and the European Community relating to the establishment of measures similar to those provided in Council Directive 2003/48/EC on tax on savings income in the form of interest payments. Equally, this retention will no longer apply in 2018, due to the Tax Transparency Agreement signed by Andorra with the EU.

Finally, in the case of the entry for other revenue, the strong increase in the sections of incidentals and surcharges is notable. On the other hand, a decline was seen in revenue from penalties associated with amounts confiscated on behalf of the Andorran state in the execution of Criminal Court (Tribunal de Corts) rulings, which relate to money laundering operations and are generally unpredictable.

As for investment income in 2017, this fell 20.7% to 32 million euros, a total that remained below budget (91%) and lowered its share of total non-financial revenue by 1.6 points, to 7.6%. This trend is mostly associated with the settled amount for the distribution of dividends from Andorra Telecom (-20%) and from marketing euros to stamp-collectors and other collectors (-53.2%). In contrast, revenue from dividends from the Andorran electricity company *Forces Elèctriques d'Andorra* (FEDA) increased significantly (30.7%), directly related to an increase in its profits. Accordingly, it should be noted that the routine for distributing dividends consists of 30% of FEDA's profits and 100% of Andorra Telecom's profits, with the exception of the distribution of reserve funds from Andorra Telecom that was carried out in 2013, as mentioned.

To complete the analysis of revenue, it should be added that the contributions obtained from current transfers and the sale of real investments were insignificant, and that there was no income from capital transfers.

1.2. Expenditure

The volume of settled non-financial expenditure in 2017 was 414 million euros, 0.5% less than the previous year. This trend is the result of a decrease in capital expenditure, largely offset by the increase in current expenditure. So, the rate of execution of non-financial expenditure planned in the final budget (the initial budget plus any changes and increases approved over the year) was 92%, below the percentage of revenue execution. Altogether, this means that the fiscal policy applied by the central Government this year was more restrictive than in the previous two years.

The value of settled capital expenditure was only 46 million euros, 8.5% less than the previous year, a figure that continues the policy of contained investment that defined budgets in recent years. As a result, its percentage of the total fell 1 point to 11.1%, while the rate of budget execution remained at 61%, a much lower rate than in current expenditure (98%), as usual. By chapters, the decrease in capital expenditure can be explained by the cut in real investment (-10.5%), which reached 40 million euros, the lowest level in the last four years.

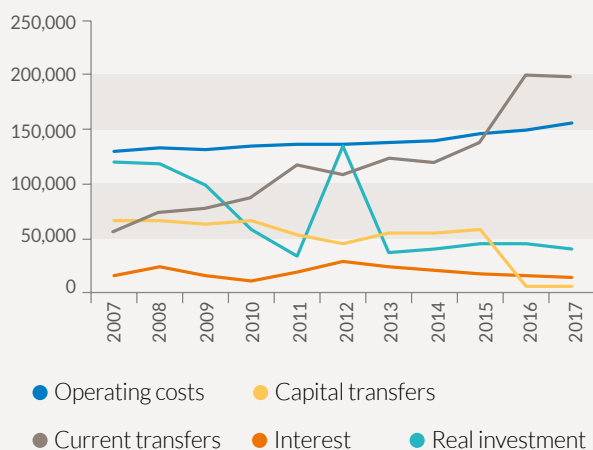
The Government has maintained a policy of contained investment, with a reduction in capital expenditure.

The value of settled capital expenditure was only 46 million euros, 8.5% less than the previous year, a figure that continues the policy of contained investment that defined budgets in recent years. As a result, its percentage of the total fell 1 point to 11.1%, while the rate of budget execution remained at 61%, a much lower rate than in current expenditure (98%), as usual. By chapters, the decrease in capital expenditure can be explained by the cut in real investment (-10.5%), which reached 40 million euros, the lowest level in the last four years.

This drop in investment was partly offset by an increase in capital transfers of 6.9%, although

GOVERNMENT NON-FINANCIAL EXPENDITURE - Thousands of euros

Chart 8.6



Note: In 2016, transfers to the Comú governments were no longer considered as capital transfers (according to previous legislation, it was considered that the bulk of the transfers had to be allocated to investment by the Comú governments) and became current transfers (Comú governments may allocate these transfers to both current expenditure and capital expenditure and to reducing debt).

Source: Ministry of Finance.

Box 8.2

THE NEW MODEL OF TRANSFERS TO THE COMÚ GOVERNMENTS

In April 2014, the central and Comú governments made an institutional agreement, covering a series of necessary actions regarding Comú competences and setting a maximum global amount of transfers at 54.6 million euros in 2015 and 2016.

After long negotiations, a new model of allocating Comú resources was established in 2017, at the same time as redefining competences, with the aim of guaranteeing the sustainability of state finances and the provision of services to citizens and to fulfil the constitutional mandate relating to the principle of Comú self-government. This new model was defined by the approval of two laws: qualified Law 18/2017 on transfers to the Comú governments and qualified Law 19/2017 on amendment of the qualified Law delimiting Comú competences.

So, the annual amount of the transfers from the central Government to the Comú governments was fixed at 55 million euros in 2018, to be increased or reduced annually according to the variation rate in annual GDP growth related to the annual amount set for the previous year.

The newly-established criteria for allocating transfers divides the resources between those for general allocation (80% of the total, equal to 44 million euros) and those considered for sustainable redistribution (the other 20%):

- Among the **resources for general allocation** are those already expressly provided by the Constitution – such as the entry in equal shares for all parishes (31% of total resources for general allocation), the variable entry based on population (26%) and the variable entry based on territory (20%) – and also two new entries: one based on demographic criteria, taking into account the child and senior populations registered in each parish (16%), and one based on overnight stays by tourists (7%).

- **Resources for sustainable redistribution** have the purpose of encouraging the Comú governments to make sustainable investments from an environmental, social and economic point of view (one third of the total), and also comply with acquired commitments regarding water separation and preparation of the land registry (one third). These resources also include an entry for solidarity and Comú specificities (the other third of the resources).

The change of model for deciding the amount of transfers provides for transfers for 2017 to be made according to the legislation currently in force, while those for 2018 and beyond will be made according to the new legislation. Consequently, the new regulations entered into force on 1 January 2018. Moreover, the Law establishes a review of the model every five years, as in the previous Law.

Equally, in March 2018, the Constitutional Court partially accepted the claim of unconstitutionality against this Law, brought by part of the opposition ministers, who considered that some of the included precepts do not comply with the Constitution. Specifically, the Court establishes that the sustainable investment policies and level of compliance for water separation and preparation of the land registry do not respect the requirements of proportionality and objectivity set by the Constitution. Moreover, it also voids the third additional provision because it considers that the investment criteria for environmental, social and economic sustainability should be defined in the Law and cannot be set by later regulations, as that undermines the principle of Comú self-government. It is estimated that this decision affects 4.4 million of the total 55 million established by the Law.

Consequently, in April 2018, the Government entered a new Bill of qualified law amending the qualified law on transfers to the Comú governments, which is currently going through Parliament.

its much lower absolute value (6 million euros) has a very limited impact on the Government's investment effort. Accordingly, it should be remembered that, since 2016, transfers to the Comú governments have no longer been considered as capital transfers (according to previous legislation, it was considered that the bulk of the transfers had to be allocated to investment by the Comú governments) and have become current transfers (Comú governments may allocate these transfers to both current expenditure and capital expenditure and to reducing debt).

As for current expenditure, the increase was led by personnel costs, which grew 4.9%, slightly less than the previous year (5.5%), to over 110 million euros. This trend can be explained by the increase in entries for pay, social security contributions and social benefits. As a result, this chapter's share of total non-financial expenditure was 26.7%, a figure that sets a historic high and maintains this chapter as the second largest expenditure after current transfers.

Another chapter of current expenditure that increased was consumption of basic goods and services, though more slowly (2.3%), having fallen 3% in 2016. So, its share of total non-financial expenditure rose three tenths to 10.9%.

In contrast, current transfers saw a fall of 0.7%, to 199 million euros. The most important cut in comparison to the previous year can be found in the section of transfers to semi-public entities (56 million euros of settled expenditure), including the Andorran Healthcare Service (SAAS), the Social Security System (CASS) and the National Agency for the Resolution of Banking Institutions (AREB). Specifically, in 2017, there was a reduction in the nominative transfer to the CASS, which was partially offset by the increase in the nominative transfer to the SAAS and the transfer to the AREB. As a result, the percentage of current transfers in total non-financial expenditure fell

one tenth to 48%, with which it remains by far the largest chapter in budgetary expenditure.

The financial expenditure chapter fell most in relative terms, due to the context of minimal interest rates.

To end, the financial expenditure chapter fell most in relative terms (-15%), continuing the steep downward trend started in 2013,

favoured by the ECB's policy of monetary easing, which brought interest rates to minimal levels. So, its share of total non-financial expenditure fell six tenths to 3.3%, the lowest level since 2010.

2. Comú governments

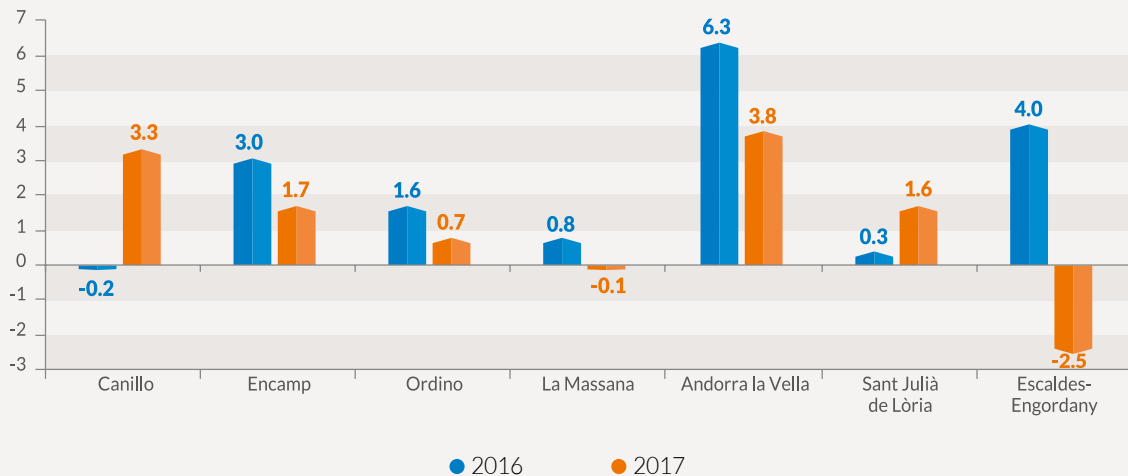
According to the budget settlements of the Comú governments in 2017, including financial assets and liabilities, the total volume of Comú revenue reached the figure of 146.6 million euros, higher than the 138.1 million euros of settled expenditure. Consequently, the balance of the Comú governments as a whole was positive for the tenth consecutive year, by 8.5 million euros, although it fell 46.9% against the previous year, contrasting with the strong increase in that year. The trend in 2017 can be explained by the fact that growth in expenditure was greater than in total revenue. If analysis is limited to non-financial expenditure, it can be seen that the total volume was 146.6 and 115.2 million euros, respectively, meaning a non-financial cash surplus of 31.4 million euros, 1.2% of GDP, part of which was allocated to reducing the debt.

More detailed analysis shows that two Comú governments recorded public deficits (La Massana and Escaldes-Engordany) meaning a deterioration in the situation compared with the positive balances obtained in 2016. In contrast, the other Comú governments settled their budgets with surpluses. Specifically, Canillo goes

The balance of the Comú governments as a whole was positive for the tenth consecutive year.

SETTLED BUDGETARY BALANCE OF THE COMÚ GOVERNMENTS - Millions of euros

Chart 8.7



Source: Comú governments / Department of Statistics.

from deficit to surplus, Sant Julià de Lòria increases it, and the other three (Encamp, Ordino and Andorra la Vella) reduced it in comparison with the previous year. Andorra la Vella still has the highest surplus (3.8 million euros), followed closely by Canillo, while Escaldes-Engordany ended 2017 with the most negative balance (-2.5 million euros).

In parallel, the analysis of debt data shows that 2017 closed with a cumulative consolidated Comú debt of 122.1 million euros, according to the data published by the corporations, which are still provisional while pending review by the Court of Accounts. This figure represents a reduction compared with the 2016 data, already reviewed by the Court of Accounts (except Sant Julià de Lòria), of 14.4%, continuing the downward trend started in 2010, enabled by the fiscal surplus obtained. If these still provisional data are taken as the base, it can be stated that, for the fourth consecutive year, all the Comú governments are clearly below the debt level set by the Law (200% of average settled income in the last three financial years). Of special note is the reduction in the debt made by La Massana, going from a level equal to 337% of revenue in 2012 to 78% in 2017.

All the Comú governments were clearly below the debt level set by the Law, for the fourth consecutive year.

The Comú governments represent 11.8% of the total public debt (central plus Comú government debt), 1.5 points lower than in 2016 and 26 points lower than ten years before. This is less than their share of non-

financial public expenditure (21.8%), representing 4.6% of Andorran GDP. Altogether, this means that in relative terms they are much less in debt than the central Government, a situation that has reversed since 2013, thanks to fiscal consolidation efforts and an improvement in their financing system.

The distribution by parishes shows that all Comú governments reduced their debt in 2017. It is notable that Andorra la Vella still has the largest share of debt (26.5% of the Comú governments' total), consistent with its higher economic importance, but it also reduced its debt the most in 2017, in absolute terms. At the other extreme, Canillo had the lowest volume of public debt (4.2% of the total), and is among those that have made the greatest effort to reduce debt in recent years.

2.1. Revenue

The Comú governments increased their settled revenue for the fifth consecutive year, at a rate of 5.1% in 2017, to reach a figure of 146.6 million euros, the highest level in the last eight years. Settled revenue surpassed the budgeted figure (103%), putting its share of total Andorran public sector revenue (central plus Comú governments) at 13.3%, 2.7 points higher than in 2016, when it reached a historic low (10%). Nevertheless, it should be said that those very low levels were distorted by the central Government's volume of financial liabilities, due to their borrowing requirements which, from 2009, greatly raised their total revenue, artificially reducing the Comú governments' share of the total. In fact, if we only consider non-financial revenue, the Comú governments' share rises to 25.7%, a higher percentage than they represent in total non-financial expenditure (21.8%).

The progress by chapters shows that the increase in revenue can be mainly explained by the increase in current income (6.7%). Within this, the increase by chapters was quite generalised. Other taxes and revenue, the most important entry in volume, increased 8.5%. Also notable were the increases in indirect taxes (9.5%) and direct taxes (6.2%) and investment income (9.1%); in contrast, the increase in current transfers was lower (1.5%).

In this way, other taxes and revenue consolidated its position as the most important current income entry for the Comú governments, with a 27.9% share of the total, followed by direct taxes, which rose to reach 18.1%, and current transfers (13.3%). In contrast, capital revenue increased only 0.9%, due to the slight increase in capital transfers (0.4%), the second most important chapter in revenue, with a share of 26.1%. Revenue from transfers of real investments increased significantly (32.2%), but this low share means that the contribution to the total is insignificant. Finally, note that there was no revenue for financial transactions, for the second consecutive year.

Other taxes and revenue consolidated its position as the most important current income entry for the Comú governments.

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By parishes, it can be seen that only Sant Julià de Lòria saw a drop in revenue (-2%). At the other extreme, Canillo increased its revenue most (12.5%), followed by Escaldes-Engordany (8.1%) and Encamp (7.2%). The other Comú governments increased revenue more modestly, below the total. In this context, Andorra la Vella retains first place in the Comú ranking for volume of total revenue, with 39.1 million (26.7% of the total), while Ordino is still the Comú with the lowest revenue, with 7.9% of the total, equal to 11.5 million euros.

2.2. Expenditure

In 2017, the Comú governments' settled expenditure increased 11.8%, to reach the figure of 138.1 million euros, the highest since 2009. This trend contrasts with the decline of 1.7% in 2016. Non-financial expenditure progressed at a still higher rate of 19.2%, compared with the decrease of 11.8% in 2016. Now, financial transactions fell 14.6%, partly because the volume of debt repayment slowed. This put the rate of execution of total budgetary expenditure at 96.6%.

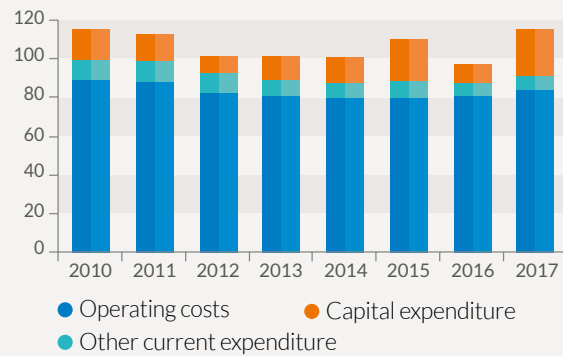
Consequently, the Comú share of total Andorran public sector expenditure (central plus Comú governments) rose to 12.6%, a percentage that still remains below their share of revenue. It should be added that, if only non-financial expenditure is considered, the Comú share of total public expenditure rises to 21.8%, which is also lower than non-financial revenue.

By chapters, the growth in Comú expenditure can basically be explained by the steeply rising trend in capital expenditure (156%), growing strongly after being halved in 2016, so the investment effort rises to 24.1 million euros, the highest figure in the last eight years. The growth in capital expenditure was concentrated in real investment, while falling in capital transfers.

Comú governments made their greatest investment effort in the last eight years.

COMÚ GOVERNMENTS' NON-FINANCIAL EXPENDITURE - Millions of euros

Chart 8.8



Source: Comú governments / Department of Statistics.

As for current expenditure, this rose 4.4%, contrasting with the decline in the previous year. This rising trend can be explained by the increase in consumption of goods and services (13%) and current transfers (4.7%). In contrast, a reduction can be seen for the seventh consecutive year in personnel costs (-0.8%) – still the most important chapter, with a share of 34.4% of total expenditure. This trend demonstrates the continual efforts of Comú governments towards fiscal containment. Equally, the most notable decrease was in financial expenditure (-18.7%), already accumulating six financial years of containment which, in turn, can be explained by the reduction in the volume of debt and interest rates, which also benefitted the central Government.

Finally, the trend in expenditure by parishes shows that it fell in Canillo and Sant Julià de Lòria (-13.1% and -12.1%, respectively), helping to explain the improvement in their fiscal balance in 2017. In contrast, the other Comú governments increased expenditure, especially Escaldes-Engordany (42.1%), the result of a major increase in investment effort, which explains the fiscal deficit. The increase in expenditure was also significant – double digit – in the other Comú governments. So, Andorra la Vella is still at the top of the Comú ranking for volume of expenditure, with a share of 25.6%, while Ordino has the lowest absolute level of expenditure (7.8% of the total).

SETTLEMENT OF THE COMÚ BUDGETS (thousands of euros)

Table 8.2

	REVENUE			EXPENDITURE		
	2017	% var. 17/16	% 2017	2017	% var. 17/16	% 2017
Canillo	15,174	12.5	10.3	11,880	-13.1	8.6
Encamp	27,246	7.2	18.6	25,582	14.2	18.5
Ordino	11,530	1.5	7.9	10,809	11.2	7.8
La Massana	14,291	3.9	9.7	14,420	11.1	10.4
Andorra la Vella	39,112	3.2	26.7	35,301	11.8	25.6
Sant Julià de Lòria	13,056	-2.0	8.9	11,412	-12.1	8.3
Escaldes-Engordany	26,198	8.1	17.9	28,746	42.1	20.8
Total	146,607	5.1	100.0	138,150	11.8	100.0

Source: Comú governments / Department of Statistics.

3. The Andorran Social Security System (CASS)

Settlement of the CASS budgets in 2017, including financial assets and liabilities, resulted in a total volume of revenue of 294 million euros, a slightly higher figure than the 292 million euros of settled expenditure. As a result, the CASS budgetary balance was 2 million euros, 24.5% more

than in 2016. If non-financial revenue and expenditure are taken into account, the CASS non-financial cash surplus rises to 2.3 million euros, 37.1% more than the previous year, thanks to slightly higher growth in revenue than in expenditure.

The CASS increased its budgetary surplus in 2017, although the surplus only represents 0.1% of GDP.

This surplus only represents 0.1% of GDP, the same as in 2016 and much lower than the values of about 1%-2% that it represented in recent years (2010-2015). In any case, any contribution surpluses are in the pension branch

and put into the pension reserve fund, as in previous years, to bolster the available reserves to meet future spending commitments.

Box 8.3

THE ANDORRAN SOCIAL SECURITY SYSTEM

The andorran social security system, managed by the CASS, consists of two branches:

1. The general branch, covering medical reimbursements and benefits for temporary disability, maternity, paternity, pregnancy risk, permanent disability, bereavement payments and orphan's pensions.

2. The pension branch, covering financial benefits for paying pension rights and consisting of the retirement pension and the temporary and life widow's pensions.

Each branch has its own sources of finance and funds cannot be transferred between the branches. Current contributions are 22% of wages: 10% to finance the general branch and 12% towards the pension branch. The contribution is shared by the company and the employee in the proportion of 15.5 points paid by the company and 6.5 points paid by the employee. Self-employed workers contribute the same percentage based on the average wage in the previous year, with the possibility of deductions based on specific parameters.

The general branch is financed mostly by the contributions, and the Government finances any deficit. In 2017, the budgetary finance requirements presented to the Government were 32.7 million euros.

The pension branch differentiates between contributory and non-contributory benefits. Benefits that are considered contributory are financed by the revenue from contributions. In 2017, contributory pensions amounted to 80 million euros. Non-contributory pensions are financed by transfers from the Government. The total transferred amount for this concept in 2017 was 4.7 million euros.

Any surplus from contributions generated by the pension branch of the CASS are transferred into the pension reserve fund, created in 2015 for management and financial efficiency, with the sole purpose of covering the future pensions of persons who have contributed to the CASS. At the end of 2017, the fund's resources were 1,247 million euros, 6.8% more than the previous year. This increase can be explained by a transfer from the CASS of 47.3 million euros, slightly less than in 2016, and a return of 31.7 million, much higher than in the previous year (24.3 million euros).

3.1. Revenue

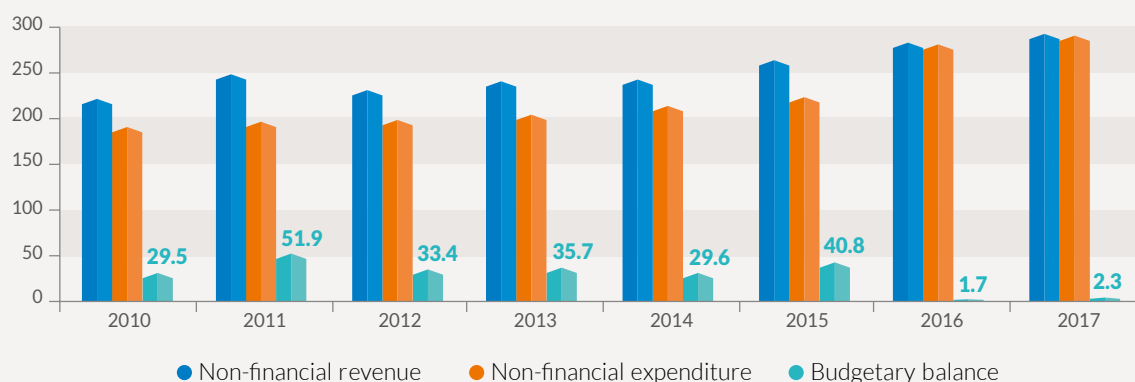
In 2017, the settled non-financial revenue of the CASS reached the figure of 292 million euros, 3.7% more than the previous year. This growth represents a slowdown in relation to one year earlier (7%), putting the execution rate at 103%.

By chapters, the most important source of revenue of the CASS are social contributions, which amount to 250 million euros and represent 85.7% of total revenue. In 2017, they saw an increase, for the fourth consecutive year, of 7%, due to the increases in the number of registered employees in 2017 (3%), the wage bill (3.8%) and the number of self-employed (6.5%). It should be stated that the figure of 250 million euros includes employers' contributions, employees' contributions, self-employed contributions and settled contributions attributable to CASS financial benefits (retirement and widow's life pensions, permanent and temporary disability benefits).

Revenue from social contributions grew in 2017, for the fourth consecutive year.

The second most important chapter in CASS revenue is current transfers from the central Government, reaching 38 million euros, 13% of the total, after falling 16.4% in 2017. Non-financial revenue of the CASS is completed by a small contribution from other taxes and revenue, which rose 62.9% in 2017, and investment income, which fell 10.1%, coming to represent 1.3% and 0.01% of the total, respectively. Finally, it should be added that revenue from financial transactions fell 1.2%, to 2.4 million euros in 2017.

CASS BUDGET SETTLEMENT - Millions of euros



Source: CASS / Department of Statistics.

3.2. Expenditure

Non-financial expenditure settled by the CASS in 2017 reached the amount of 289 million euros, a figure that represents an increase of 3.5%, much more moderate than in the previous year (26%). So, expenditure grew slightly below revenue, with a budget execution rate of 102%. Moreover, expenditure on financial transactions increased 7.6%, to 2.7 million euros, an amount that, nevertheless, is still well below the values before 2016.

In 2017, benefits grew less than contributions.

The distribution by chapters shows that revenue is concentrated, as is logical, in current transfers, where benefits are accounted for, with a volume of 235 million euros, 5% more than the previous year, and a share of the total of 81.2%. This increase is lower than that of contributions, which was a determining factor in the increase in the surplus in 2017.

It should be specified included within this entry are the non-contributory benefits financed by the Government through current transfers, and contributory expenditure paid by the CASS for authorised financial benefits.

The other expenditure is divided between personnel costs, which increased 2.8% and represent 1.7% of the total, and consumption of basic goods and services, which increased 5.9% and represents 0.6% of the total. Expenditure on real investment is insignificant, as is financial expenditure, as the CASS has no debt.

3.3. General branch of the CASS

The distribution of revenue and expenditure of the CASS by branches shows that, in the case of the general branch, revenue from contributions increased 11.3%, to 118.5 million euros, as a result of various factors. Firstly, the improvement in the labour market, which resulted in an increase in the number of employees and self-employed. Secondly, from a basis of comparison effect, as contributions were increased by 2% in 2016, coming into force in April 2016. Thirdly, the major revenue from extemporary contributions up to the legal limitation period of 5 years, on concepts of payment in kind, the result of various checks that were carried out.

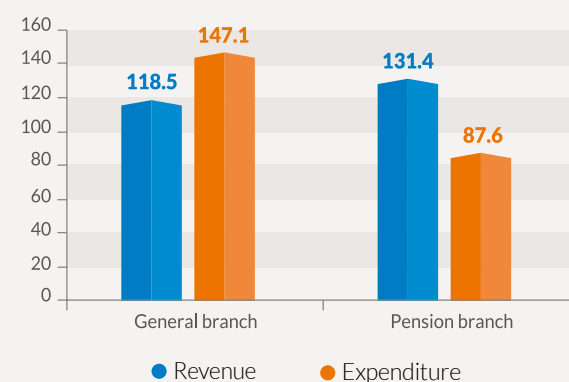
The increase in expenditure on benefits in the general branch was slower, at 5.1%, to 147.1 million euros. This trend was favoured by the fall in the numbers of pensioners covered by this branch in 2017, by 1.2% to 2,564 individuals.

In any case, expenditure easily exceeded revenue in this branch. It should be remembered that the imbalance between revenue and expenditure in the general branch is a problem that started in 2007 and worsened during the years of economic crisis to reach a high in 2015.

Equally, the trend in 2017 was marked by a reduction in the deficit (30.8 million euros) in comparison with 2016. This imbalance is financed by contributions from the Government budget, a situation that has been repeated since 2012, after the cumulative reserves in this branch were depleted in 2011 and according to the provisions of article 86.3 of Law 17/2008. In future, the prospects of a gradually aging population and the growth in chronic diseases would indicate that health costs will continue to rise, making it difficult to restore financial equilibrium, if the current conditions for contributions and coverage are maintained.

In 2017, the deficit in the general branch decreased, favoured by increased contributions and a fall in the numbers of pensioners.

REVENUE AND EXPENDITURE OF THE CASS BY BRANCHES. 2017 (Millions of euros)



Note: Data relating to revenue from contributions and expenditure on benefits.

Source: CASS.

3.4. Pension branch of the CASS

As for the pension branch, revenue from contributions grew 3.5% to 131.4 million euros, an amount that still exceeds expenditure. Specifically, in 2017, total expenditure on benefits in the pensions branch was 87.6 million euros, with growth of 4.7% against the previous year, higher than that of revenue.

This rising trend can partly be explained by a 2% increase in the numbers of pensioners in 2017, reaching a figure of 12,200 individuals in December. Nevertheless, the dependency ratio improved 1.5% to reach 3.87 active insured per pensioner in December 2017, a trend that was favoured by the increase in the active population.

However, in future the analyses made by CASS itself warn that the rate of expenditure will accelerate due to the gradual incorporation into the group of pensioners of sizeable generations with quite high pensions in relation to the contributions made. This situation will therefore require measures to guarantee the long-term financial equilibrium of the system.

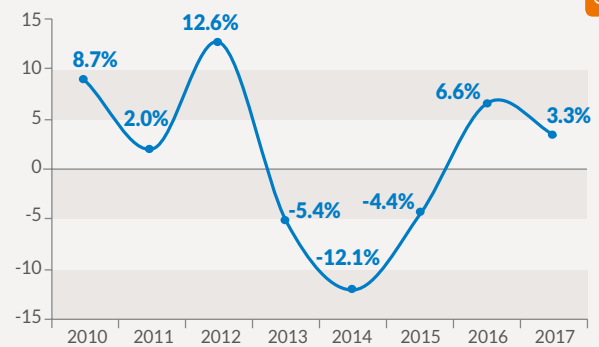


The Andorran economy: developments in the main sectors

IX. The primary sector

The primary sector is the smallest sector of activity in the Andorran economy. It only represents 0.6% of Andorran GVA, so changes in this sector do not significantly affect the total GDP of the economy. The trend in GVA for the agricultural sector was contractionary over the 2013-2015 period, then switched in 2016 to regain a positive rate of 6.6% in real terms. In 2017, it continued to rise but slowed to 3.3%. The long economic crisis and strong external competition pushed crop and livestock farmers to make efforts to introduce improvements in the production process, to obtain seals of quality and gradually integrate into the European customs union.

PRIMARY SECTOR GVA
Variation rate in real terms (%)



Source: Department of Statistics.

Chart 9.1

Despite this positive trend in activity, employment and the business network shrank in 2017. On the one hand, the number of workers fell from 171 in 2016 to 167 in 2017, representing a decline of 2.6%, whereas average monthly wages in the sector rose in 2017, for the second consecutive year, more than 3.5%. Specifically, in 2017, the average wage was 1,508.2 euros, 3.7% higher than the previous year. On the other hand, at the end of 2017, there were 228 businesses dedicated to the primary sector, four less than one year before. The primary sector business network has been contracting since 2013, when it reached the highest number, with 245 businesses. The business structure is based on micro-businesses, as 96% of businesses in this sector have between 1 and 5 workers, and only 10 businesses have 6 or more workers.

FARMS AND UTILISED AGRICULTURAL AREA (SAU) BY PARISH. 2017

	Farms	SAU (m ²)	% total SAU
Canillo	48	3,433,032	17.0
Encamp	46	2,327,906	11.5
Ordino	34	2,705,470	13.4
La Massana	55	3,060,576	15.2
Andorra la Vella	36	717,735	3.6
Sant Julià de Lòria	65	7,425,031	36.8
Escaldes-Engordany	28	509,136	2.5
Total	312	20,178,886	100

SAU: utilised agricultural area.

Source: Department of Agriculture.

In 2017, agricultural GVA continued to rise but slowed to 3.3% in real terms.

In 2017, the number of crop farms also decreased. Specifically, 312 farms were registered, three less than one year before, with a cultivated area of 21 km². The parish with most activity is still Sant Julià de Lòria, with 65 farms, while Escaldes-Engordany closes the ranks with only 28 farms. There has been a gradual decline in the number of

A gradual decline in the number of crop farms has been occurring since 2012.

20 km² utilised agricultural area (SAU), meaning that the average size of farms is becoming progressively larger.

By type of crop, 60.8% of the total farmed area is used for pasture; 25.9% for hay, and 7.2% for tobacco. Over the last five years, the area left fallow and for growing potatoes, vines, forage and aromatic and medicinal plants has fallen significantly. In contrast, the area used for market gardening and, to a lesser extent, hay and pasture has increased. Strong growth is especially noted in the use of agricultural area for various trees, e.g. fruit trees, raspberries and beet, rising from 9,500 m² in 2012 to 30,500 m² in 2017.

In 2017, vineyards occupied 86,379 m², the same area as in the previous year. In 2017, the seal of quality for Andorran wines was introduced. Moreover, the Government started to offer subsidies to vineyards to adopt it, for the extra effort involved in the quality control, the first step towards obtaining the Protected Geographical Indication (PGI) awarded by the EU.

farms over the last five years: in 2012 there were 366 farms and in 2017, there were 312. In contrast, the total cultivated area remained almost constant in the same period, about

AGRICULTURAL AREA BY TYPE OF CROP (in m²). Developments over the last five years.

	2012	2017	% variation 2012/2017	% total 2017
Pasture	12,605,792	12,763,794	1.3	60.8
Hay	5,210,147	5,442,330	4.5	25.9
Tobacco	1,503,335	1,517,116	0.9	7.2
Fallow	501,455	428,719	-14.5	2.0
Market gardening	124,471	168,538	35.4	0.8
Potatoes	243,456	148,557	-39.0	0.7
Vines	109,875	86,379	-21.4	0.4
Miscellaneous ⁽³⁾	9,514	30,549	221.1	0.1
Forage ⁽²⁾	26,965	21,622	-19.8	0.1
Others	418,154	401,393	-4.0	1.9
PAM ⁽¹⁾	40,683	-	-	-
Total	20,793,847	21,008,998	1.0	100
Utilised Agricultural Area (SAU) - in m²	19,874,237	20,178,886	1.5	

(1) Aromatic and medicinal plants / (2) Forage for grazing / (3) Fruit trees, raspberries, beet.
SAU: utilised agricultural area.

Source: Department of Agriculture.

2017 was a rather complicated year for growing tobacco due to the weather, unlike 2016, which was a positive year. Although the declaration of tobacco quotas remained stable in relation to previous years, heavy summer hailstorms affected all the parishes in an almost generalised manner. On average, the percentage of damage to Andorra's harvest was 70% and, after the inspection for real damage, the percentage was 58% (total of the different levels of damage).

2017 was a negative year for tobacco cultivation due to the heavy summer hailstorms.

As a result of this situation, the tobacco harvest saw a decline of 10% compared with the previous year, so 2017 was the worst year since 2007, when production fell 22.5%. This downturn in the 2017 harvest was general to all parishes except Sant Julià de Lòria (the largest,

TOBACCO HARVEST BY PARISHES (Kilos)

Table 9.3

	2016	2017	% var. 17/16	% total 2017
Canillo	15,933.4	14,561.5	-8.6	6.6
Encamp	29,461.5	10,271.7	-65.1	4.7
Ordino	31,652.8	31,499.7	-0.5	14.3
La Massana	45,512.6	44,797.4	-1.6	20.4
Andorra la Vella	30,078.7	27,688.6	-7.9	12.6
Sant Julià de Lòria	80,075.1	80,510.7	0.5	36.7
Escaldes-Engordany	11,369.6	10,233.6	-10.0	4.7
Total	244,083.7	219,563.2	-10.0	100

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

The EU agrees to extend the preferential agreement on tobacco to 30 years in the process of customs integration.

with 36.7% of national production), where the harvest stayed at almost the same levels as the previous year. The biggest falls in the tobacco harvest occurred in Encamp (-65.1%), Escaldes-Engordany (-10%), Canillo (-8.6%) and Andorra la Vella (-7.9%). In total, the volume produced, after adjusting the quotas allocated to the harvesters, was 219,563 kg, about 24,520 kg less than in 2016.

All this is happening at a crucial moment, due to negotiations with the EU for a concrete proposal about which agricultural products must be integrated in the customs union now, and which will be left out for a period to enable gradual incorporation.

In December 2017, the European Union agreed to extend the preferential agreement on tobacco to 30 years in the process of customs integration, although, from the seventh year, Andorra will have to start waiving its current customs duties and start adopting the European Acquis in order to reach the goal of zero customs duties. In return, Andorra must demonstrate that it is diversifying its economy to reduce economic dependency on tobacco. It must also show its commitment to combatting fraud and smuggling. Equally, the Government has made the commitment with the EU to lower the price differential with surrounding countries (currently 30% with Spain), put an identifying label on packets of tobacco and ban advertising of it.

Another item of news about tobacco in 2017 is the increase in consumption tax. The Government raised tobacco tax 10%, a measure that entered into force in March 2017. The price of a packet of cigarettes rose fifteen cents on average, or an average of 4.5% in percentage terms. This tax increase is estimated to represent an increase in state revenue of 10 million euros.

In 2017, the number of livestock increased 6.8% - with 5,564 registered heads - breaking the negative trend of the previous two years (in 2016, total livestock fell 5% and in 2015, 7.5%). This upward trend was solely the result

of sheep breeding and farming, which grew 17.2%, increasing from 2,727 heads in 2016 to 3,196 in 2017. This spectacular increase in sheep breeding offset the decline in other types of livestock. So, the number of horses fell 11%; goats 2.5%, and cattle 2.4%. It should be remembered that, after sheep - representing 57% of the total - the most important are cattle, at 28%, and horses, at 10.5%. Goats only represent 4.2% of total livestock.

In 2017, increased sheep breeding offset falling numbers in other types of livestock.

LIVESTOCK (adult heads)

Table 9.4

	2016	2017	% var. 17/16	% total 2017
Total cattle (bulls, cows)	1,585	1,547	-2.4	27.8
Total horses (workhorses, studs, mares)	657	585	-11.0	10.5
Total sheep (rams, ewes)	2,727	3,196	17.2	57.4
Total goats (bucks, does)	242	236	-2.5	4.2
Total livestock	5,211	5,564	6.8	100

Source: Department of Agriculture.

In 2013, a marketing process for Andorran veal was begun under the quality control and assurance label *Carn de qualitat controlada d'Andorra* and the Protected Geographical Indication *Carn d'Andorra IGP*, but it seems that the positive effect on bovine livestock numbers is running out. So, the livestock farmers' association *Ramaders d'Andorra, SA* has started to work with four research centres and two companies from Spain and France on the project DietaPYR2, within the Poctefa Plan. This is a European project for innovation and the introduction of new technologies into the production chain of native Pyrenean cattle, to label quality meat associated with a traditional production system in the area. The initiative has a global budget of 2.3 million euros and will be carried out over three years.

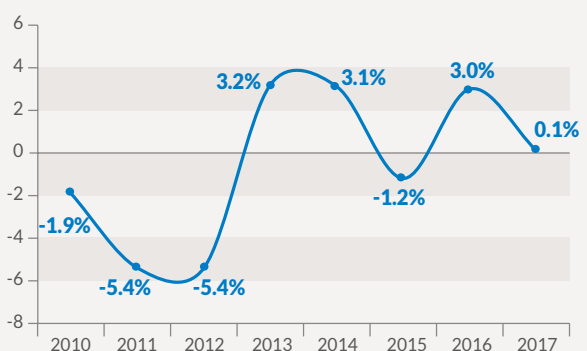
In relation to horsemeat, since 2015, *Ramaders d'Andorra SA* has been marketing horsemeat under the quality control and assurance label. The certification processes by the Government or contracted businesses ensure that the animals, born in Andorra, are suckled by their mother for six months in open pastures (valley floors, woodland slopes and mountains), fattened with food concentrates specially formulated for Andorran breeding conditions, and then slaughtered at the National Slaughterhouse. Marketing is carried out both in the Principality of Andorra, to supply the national market, and by export to other countries.

X. Industry

In 2017, the industry and manufacturing sector saw almost zero growth, after the 3% increase in the previous year and the decrease seen in 2015. One of the main driving forces in this sector is energy production and distribution, a production branch with a more volatile component than other economic sectors. The whole of the industry and manufacturing sector represents a small share of the Andorran economy in comparison with neighbouring countries, as it only represented 5.1% of GVA in 2017. The quarterly trend shows that the sector has shrunk. In the first quarter of 2017, industrial GVA grew 1.6% year-on-year, but it stagnated in the second quarter, and saw identical negative variations in the third and fourth quarters (-0.6%).

GVA IN THE INDUSTRY AND MANUFACTURING SECTOR
Variation rate in real terms (%)

Chart 10.1



Source: Department of Statistics.

This stagnation in industrial activity is also seen in business indicators and the labour market. Specifically, the number of businesses in the secondary sector, 303 in December 2017, was the same as in 2016. The average size of Andorran industries is small, as only 12 of existing businesses have more than 25 workers. Employment in the sector has not grown either. Specifically, the number of employees in the industrial sector is 1,603, slightly lower than in the previous year (1,615 employees). This moderate decline of 0.7% in employment in the industrial sector in 2017 contrasts with the increases seen in the previous two years (2% in 2015 and 1.5% in 2016). Finally, average wages in the sector have started to recover and for once exceed 2,200 euros, with an increase of 1.9% in comparison with the previous year, the most important increase since 2009. It should be remembered that between 2010 and 2016, wages practically stagnated on annual average.

The industrial and manufacturing sector stagnates in 2017.

NUMBER OF EMPLOYEES IN THE INDUSTRIAL SECTOR

	2007	2016	2017	% var. 17/16	% total 2017
Extraction industries	6	3	1	-63.6	0.1
Manufacturing industries	1,788	1,452	1,434	-1.3	89.4
Food and beverages	230	236	235	-0.1	14.7
Tobacco industries	254	239	239	0.1	14.9
Textiles	58	36	35	-4.1	2.2
Clothing and leather articles	1	1	2	61.5	0.1
Wood and cork, basketwork and esparto	270	118	120	1.0	7.5
Printing, graphic arts and reproduction of recorded media	292	200	201	0.8	12.5
Chemical industries	83	117	109	-7.1	6.8
Rubber and plastic articles	2	15	13	-16.0	0.8
Other non-metal mineral articles	63	34	42	25.1	2.6
Articles of metal, except machinery and equipment	148	119	128	7.7	8.0
Machinery and mechanical equipment	154	126	131	3.5	8.1
Office machinery and computer equipment	-	2	1	-52.0	0.1
Machinery and electrical equipment	21	7	7	-2.2	0.5
Medico-surgical, precision, optical and clockmaking equipment and instruments	139	161	131	-18.8	8.2
Motor vehicles, trailers and semi-trailers	-	2	2	0.0	0.1
Furniture; other manufacturing industries	60	25	25	0.0	1.5
Recycling	13	13	14	8.2	0.9
Production and distribution of electricity, gas and water	147	160	169	5.2	10.5
TOTAL	1,940	1,615	1,603	-0.7	100

Source: CASS (Andorran Social Security System) / Department of Statistics.

Employment in the tobacco industry fell 13% between 2013 and 2016 but remained stable in 2017.

One of the main industries in Andorra is tobacco, which was marked by certain stability in 2017, in both employment and establishments. In 2017, there was an average of 239 employees, the same as the previous year, the lowest figure since the start of the historical series (early 1990s). It should be remembered that employment fell 13% between 2013 and 2016. This sector represents almost

15% of total industrial employment, a similar share to the food and beverage industry (14.7%). The number of establishments in the tobacco subsector was still six, the same as in the last three years, and tobacco imports increased 3%, to 28 million euros.

The electricity production and distribution sector is the fourth largest, in terms of employment, after the tobacco industry, the food and beverage industry and printing and graphic arts, with a total share of employees of 10.5%, and a positive variation of 5.2% compared with 2016. In 2017, national electricity production saw a year-on-year increase of 9.3%, thanks to: (i) the increase in solar production (80.3%, despite only providing 0.1% of total consumption); (ii) operation of the Combined Heat and Power plant in Soldeu since December 2016 (covering 0.7% of consumption); (iii) the increase in thermal production from urban waste at the Comella waste treatment plant (20.4%), and finally, (iv) the increase in hydroelectric power from setting up the mini hydroelectric power plant in Arcalis (3.2%), which is the most important source of electricity, producing 15% of total electricity consumed in Andorra.

In 2017, electricity production increased 9.3% and imported electricity fell.

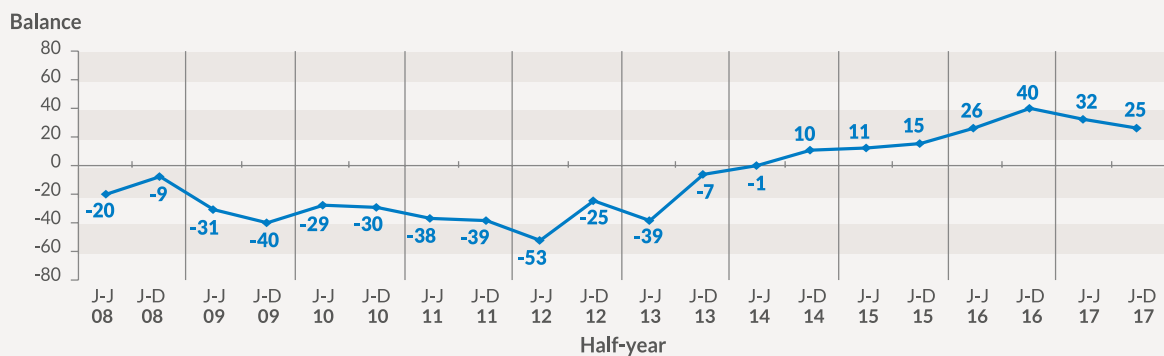
On the other hand, year-on-year domestic consumption fell 0.8%, contrasting with the increases in the previous two years. By sectors, energy consumption increased for households, industry, hotels and catering and other services, but this increase was offset by falling consumption in construction, public lighting, ski resorts and public administration. As a result of the combination of rising production and a slight fall in consumption, imports of electricity, which represent 81.2% of total consumption, fell 2.9% in 2017.

In 2017, fuel imports saw a similar trend to electricity consumption (-0.2%). By type, increases were only seen in imports of unleaded petrol (2.2%) and diesel (0.7%), while imports of domestic heating oil fell (by 3%).

In 2017, growth in industrial turnover slowed.

The results of the Chamber of Commerce's situation survey indicate that the recovery continued gradually in the industrial sector, although the rate of growth slowed in comparison with the previous year, in line with GVA data. Industrial businesses indicated an average increase in turnover of 3.1% - half a point less than the increase noted in 2016 - and a fairly stable rate of job creation.

BUSINESS ACTIVITY - INDUSTRIAL SECTOR



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

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

Chart 10.2

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

Table 10.2

		2015			2016			2017		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
1. Business activity (reviewed half-year)	Good	26	31	29	36	46	41	44	36	40
	Normal	60	53	57	54	48	51	44	53	49
	Bad	15	16	16	10	6	8	12	11	12
	Balance	11	15	13	26	40	33	32	25	29
2. Orders (reviewed half-year)	High	10	13	12	11	15	13	12	9	11
	Normal	50	57	54	60	56	58	63	64	64
	Low	40	30	35	29	29	29	25	27	26
	Balance	-30	-17	-24	-18	-14	-16	-13	-18	-16
3. Stocks of finished products (reviewed half-year)	Excessive	10	6	8	9	6	8	6	10	8
	Adequate	45	46	46	47	44	46	54	57	56
	Insufficient	2	0	1	3	4	4	6	1	4
	No stocks	44	49	47	41	46	44	34	32	33
	Balance	8	6	7	6	2	4	0	9	5
4. Average production capacity utilisation (in %) (reviewed half-year)		64.0	65.2	64.6	67.7	66.9	67.3	68.6	70.7	69.6
5. Production (compared with same half-year of previous year)	Higher	27	32	30	33	45	39	29	40	35
	Similar	53	44	49	45	38	42	56	38	47
	Lower	20	24	22	22	17	20	15	22	19
	Balance	7	8	8	11	28	20	14	18	16
6. Sales prices (compared with previous half-year)	Higher	7	4	6	13	7	10	14	11	13
	Equal	77	78	78	74	81	78	74	82	78
	Lower	16	17	17	13	12	13	12	7	10
	Balance	-9	-13	-11	0	-5	-3	2	4	3
7. Number of employees (compared with previous half-year)	More	8	10	9	6	12	9	9	11	10
	Same	82	83	83	86	75	81	83	85	84
	Less	10	7	9	9	13	11	8	4	6
	Balance	-2	3	1	-3	-1	-2	1	7	4

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

Specifically, in relation to business activity, businesses continued to evaluate progress positively in the final part of 2017, but less optimistically than in the two previous half-years.

Most indicators of activity and confidence in the sector confirmed an upswing but slower than in 2016. Industrial production saw a gentle increase in the second half of 2017, for the seventh consecutive half-year, although the rate of growth did not appear as strong as one year earlier. This upward trend in volumes of production, although very tentative and gradual, can be partly attributed to a more favourable trend in domestic demand, but also to an increase in the export rate of businesses due to the improvement in the external economic environment. Accordingly, it is notable that total exports of goods grew 17% in 2017, as a result of the gradual improvement in the European market, especially Spain and France.

Businesses' opinions on sales prices improved slightly. Specifically, in 2017, 13% of businesses felt that prices had increased in comparison with the previous half-year, whereas 10% felt they had fallen. This changing trend in prices is a logical result of the economic recovery, causing

an improvement in both domestic and external demand. Within this context, the trend in employment remained quite stable and improved slightly in the second half of 2017.

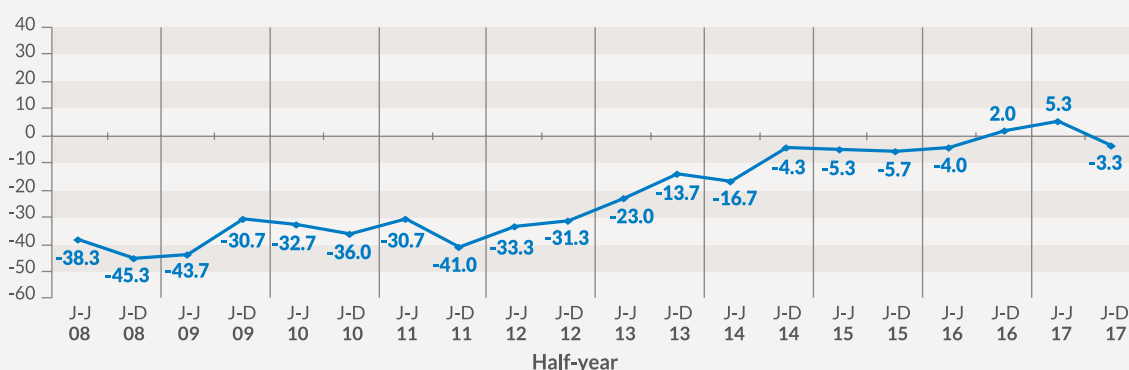
Optimism among industrial businesses slowed in comparison with the first half of 2018.

In the first half of 2018, optimism among industrial businesses fell. Industries predict that any improvement in the business situation will be slight, in line with rather moderate increases in orders and production volumes. In this context, the average productive capacity utilisation will remain around 70%, but businesses also suggest that the upward trend in sales prices will be more accentuated, with a slightly faster rate of job creation.

The confidence indicator, which captures the situation of activity in industry, appears to cool in the second half, suggesting that the recovery in this sector will remain weak in 2018.

As for the obstacles that limit business activity, apart from weak demand (mentioned by 58% of businesses) and increased competition (quoted by 45%), the other most significant concerns focussed on the shortage of qualified workers and increased operating costs, both factors indicated by 41% of the total surveyed businesses.

CONFIDENCE INDICATOR⁽¹⁾ - INDUSTRIAL SECTOR



(1) Average balances in the total order book, production trend and stocks of finished products turned around.

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

Chart 103

XI. Construction and related industries

2017 saw a strengthening of the expansion in the construction and related industries sector that started in 2015. According to official GDP figures published by the Government, construction GVA in 2017 saw a variation of 3.5%, higher than the 2.1% achieved in 2016 or the 0.2% in 2015. This recent expansive phase in the sector was preceded by a strong period of recession. Due to this trend, construction's share of total GVA began to recover, but remains low at only 5.9% in 2017, compared with a maximum of 12.6% in 2006.

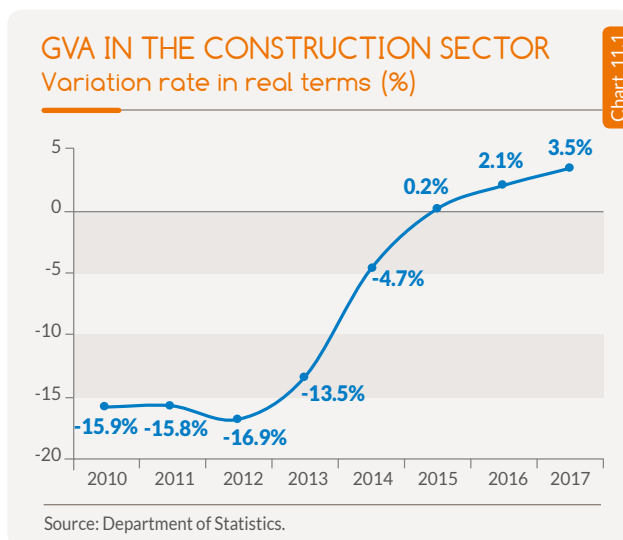
Growth in construction accelerated in 2017.

In 2017, the overall figures for the construction sector were positive for the second consecutive year, above all due to the impetus from new works and refurbishments, although civil works

also made a positive contribution this year. On the one hand, employment increased in the sector, for the second consecutive year, by an annual 2.1%, to reach 2,875 employees, after a long period of contraction between 2007 and 2014. Despite the recent increase, the number of employees in the construction sector is still 58% less than the maximum reached in 2006 (6,788 employees). In 2017, average wages increased 3.2%, the highest increase since 2007, driven by the shortage of trained workers in the sector. On the other hand, imports of building materials also increased in 2017, by 3.1%, contrasting with the negative trend of the previous year, showing that the sector is in a phase of recovery. Finally, the number of business establishments in the sector was 795 in 2017, 1.7% more than in 2016.

As for the residential sector, it should be noted that there has also been a strong upswing in the number of authorised projects in the last two years. In 2017, 591 projects were authorised, 15% more than the previous year. This increase is added to the 20% in 2016. Of the authorised 199,713 m², 50% were for new works; 44% for refurbishments, and the other 6%, for demolitions or extensions. These increases were significant because they started from very low figures after the major crisis experienced by the residential sector.

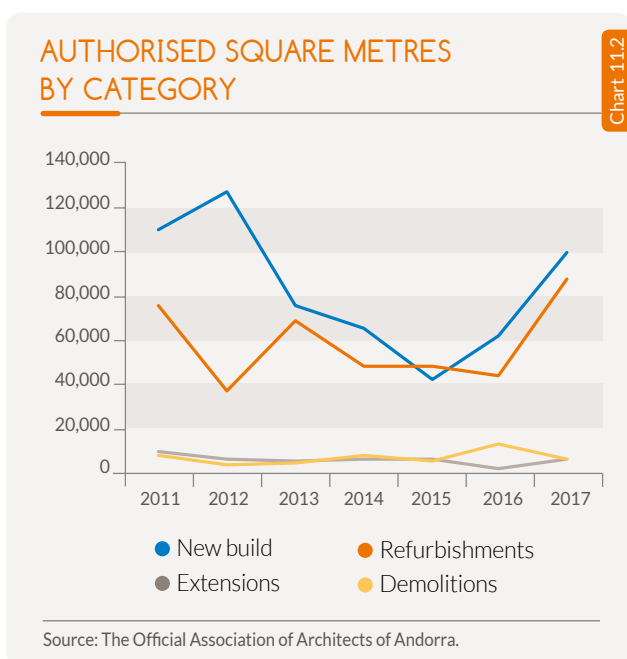
In 2017, the authorised square metres for refurbishments reached almost 88,000m², practically double the number authorised in 2016 (44,426m²), partly attributable to the simplification and improvement in the Renova plan procedures for improving energy efficiency in buildings. Since it was set up in 2011, the Renova plan has received 1,079 requests for subsidies (317 in 2017, 38% more than in the previous year), with the total cost of the presented projects being 45.1 million euros, for which subsidies for a total of 5.6 million euros were requested (1.5 million in 2017).



In 2017, new works, refurbishments and also civil works helped to boost the recovery in the sector.

The most common request was to change the windows in a private dwelling with an average age of 30 years, followed by replacement of the heating system or improvements to the roof and/or façade. For 2018, the direct subsidies entry of 1.5 million euros was renewed, with a new item of 150,000 euros for the Renova solar power programme, to encourage solar power installations.

It should be added that, as the Bill of law to promote the energy transition and climate change was presented to parliament in February 2018, it is planned to give an added impetus to housing stock improvements and efficiency, as the Bill includes measures such as energy certificates for buildings, which will be mandatory when buying and selling property from 2020.



In carrying out the 2018-2021 Statistics Plan, the Government's Department of Statistics published quarterly statistics on property transactions and statistics on housing and land prices, for the first time, referring to 2017. The results of the statistics show that there was an increase in property transactions that year, of 11.6% against 2016, and that the parishes of Sant Julià de Lòria, La Massana, Escaldes-Engordany and Canillo had the greatest increase in transactions that year.

In relation to the type of works, the total volume of new builds transferred in 2017 fell 67.5% against 2016, with apartments and parking spaces falling most. In contrast, transfers of used property increased 21.7%.

PROPERTY TRANSFERS AND AVERAGE PRICE PER M², PER PARISH

Table 11.1

	PROPERTY TRANSACTIONS				M ² PRICE FOR PROPERTY TRANSACT. (EUROS)			
	2016	2017	Absolute variation	Relative variation (%)	2016	2017	Absolute variation	Relative variation (%)
Canillo	324	375	51	15.7	1,204.5	1,245.0	41	3.4
Encamp	379	387	8	2.1	1,248.6	1,374.6	126	10.1
Ordino	135	134	-1	-0.7	1,309.3	1,419.7	110	8.4
La Massana	274	337	63	23.0	1,311.2	1,374.4	63	4.8
Andorra la Vella	294	272	-22	-7.5	1,851.6	2,250.3	399	21.5
Sant Julià de Lòria	64	116	52	81.3	1,330.9	1,352.3	21	1.6
Escaldes-Engordany	239	286	47	19.7	1,688.6	1,819.2	131	7.7
Total	1,709	1,907	198	11.6	1,392.1	1,525.7	134	9.6

Source: Department of Statistics.

As for the value of properties transferred in 2017, the total fell 10.6% against the previous year. The fall in value for properties was most significant for commercial premises and stores (warehouses), as fewer properties were transferred and of a smaller size in 2017. From the geographical point of view, La Massana and Escaldes-Engordany were the two parishes with the most significant fall in value for transferred properties.

Finally, the price of housing and land, in global terms, increased 9.6% against the previous year. An increase in the price per m² occurred in all parishes, notably in Andorra la Vella (21.5%) and Encamp (10.1%).

As for the subsector of public works, in 2017, the central Government made lower real investment than in 2016, while the local Comú governments pushed investment strongly, after the steep downturn in the previous year. The aggregate real investment of the central and Comú governments gives a total of 63.7 million euros, 19% more than the previous year. This increase offsets the decrease of 17% in the previous year.

Real investment rose 19% in 2017, with a steep increase by local Comú governments that offset the reduction by the central Government.

Settled real investment by the central Government reached 39.86 million euros, a figure that represents a reduction of 10.5% compared with the investment made in the previous year. The concept of investment in "assets for general use" fell most (6.5 million less than the previous year), due to the reduction in investment on roads. Among the most important investments is notably

the new seat of Justice (3.6 million euros) and the refurbishment of Hotel Rosaleda, a *noucentista* building that is protected as a building of cultural interest (2.3 million), Radio Andorra (433,154 euros) and school refurbishments, among others.

The following table lists the public works settled in 2017 by the Ministry of Land Planning by programme. The total investment figure is 31.75 million euros; the other 8.11 million euros of the total 39.86 were for investments carried out by other ministries.

On the other hand, real investment by the Comú governments increased 165%, going from 9 million euros in 2016 to 23.8 million in 2017, the highest investment figure since 2008, when it reached 40 million euros. It should be noted that this increase was preceded by a steep fall of 51% in 2016. So, in 2017, not only was the decline from the previous year recovered but the level of investment regained pre-crisis levels. By parish, the greatest expenditure in investment was by Escaldes-Engordany, with 9.1 million euros, and Andorra la Vella, with 4.9 million euros; then come Encamp (3.4 million), Canillo (2.4 million), La Massana (1.8 million), Ordino (1.4 million) and finally, Sant Julià de Lòria (with only 758 thousand euros).

The Chamber of Commerce's situation surveys indicate that construction is starting to recover. In fact, business activity in the second half of 2017 is the most optimistic in the last twelve years, though starting from low levels, due to

GOVERNMENT PUBLIC WORKS. PUBLIC INVESTMENT* 2017 BY PROGRAMME (categories)

Table 11.2

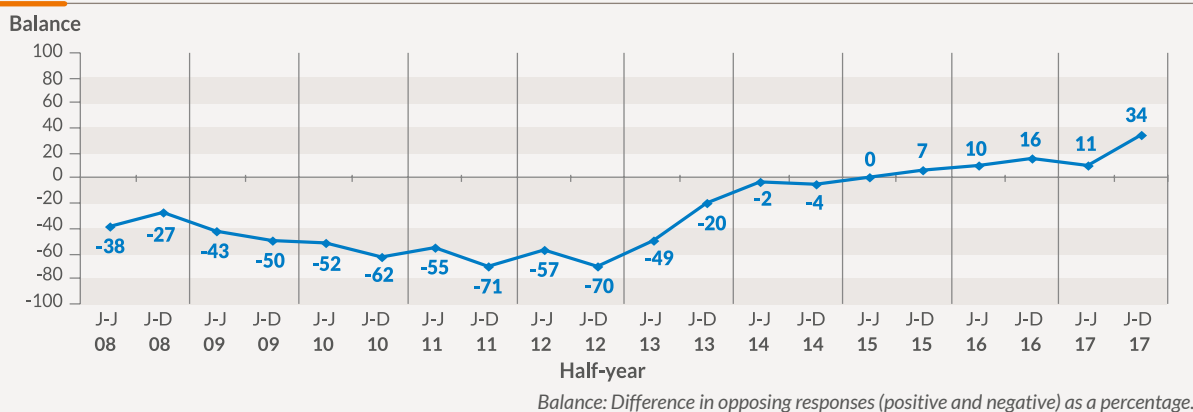
Description	Total settled investment public works 2017 (Euros)
Government infrastructure	1,962,176
Judicial infrastructure	3,665,867
Prison	125,374
Security and public order	0
General health admin.	31,252
School infrastructure	2,149,553
Education	3,316
Sports and PE	409,693
Environmental management and monitoring	174,639
Waste management	0
Heritage management	328,843
Cultural infrastructure	3,019,594
General admin.	1,016,288
CG road infrastructure	7,721,022
Other roads	0
Road maintenance	8,585,670
Natural risks. Road infrastructures	1,249,548
Sectoral plan. New road infrastructures	54,314
Rivers and streams treatment	701,226
Cartography and topography	15,986
Agricultural activity	1,672
Strategic and transport projects	538,000
Tourism regulation and promotion	0
Total	31,754,033

*Total settled public works relates to real investment by the Ministry of Land Planning.

Source: Ministry of Land Planning.

BUSINESS ACTIVITY - CONSTRUCTION SECTOR

Chart 11.3



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

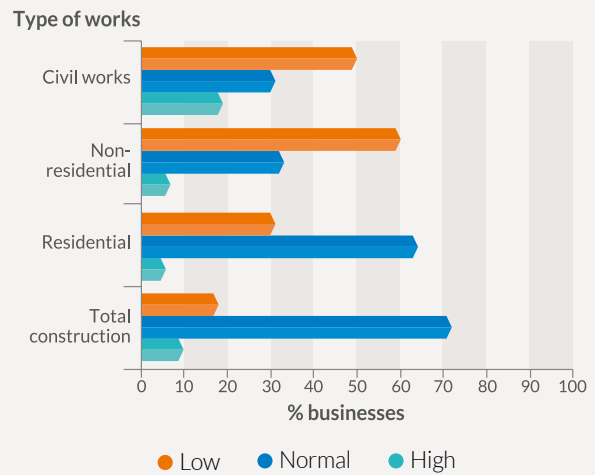
the major crisis that hit the sector. Equally, the volume of completed works also shows better levels of activity than in 2016, with an increase in completed works in most businesses. The recovery in contracted works is the result of less negative behaviour in public works and a slight upturn in demand for housing, implying that the correction in the property sector is finally reaching an end. The volume of contracted civil works is still low but not as low as in previous years, in a context of healthier public budgets. Finally, unit contract prices confirmed the stable trend that began in the first half of 2017, after twenty consecutive half-years of steep falls. As for the labour market, moderate growth was seen in the number of employees in the sector.

In the first half of 2018, construction businesses indicate an improvement in business prospects, if still slight and not enough to ensure satisfactory levels of activity. In the opinion of businesses, both completed and contracted works saw a very slow increase in the first half of 2018. By type of works, a very low level of activity is expected to persist in the subsector of non-residential building, while the branch of residential building is expected to become slightly more dynamic, thanks to the reforms and refurbishments that will still play an important role in driving activity in this works segment. On the other hand, civil works will continue to struggle

Business activity is the most optimistic in the last twelve years, though starting from very low levels.

CONTRACTED WORKS - CONSTRUCTION SECTOR (half-year July-December 2017)

Chart 11.4



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

BUSINESSES' OPINIONS OF DEVELOPMENTS IN THE CONSTRUCTION SECTOR (% of businesses)

Table 11.3

		2015			2016			2017		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
1. Business activity (reviewed half-year)	Good	15	24	20	31	28	30	24	34	29
	Normal	70	59	65	49	60	55	63	66	65
	Bad	15	17	16	21	12	17	13	0	7
	Balance	0	7	4	10	16	13	11	34	23
2. Volume of executed works (compared with same half-year of previous year)	Higher	32	29	31	38	45	42	27	54	41
	Equal	42	36	39	26	26	26	49	32	41
	Lower	26	36	31	36	29	33	24	15	20
	Balance	6	-7	-1	2	16	9	3	39	21
3. Contract unit prices (compared with previous half-year)	Higher	0	2	1	0	2	1	2	0	1
	Equal	68	74	71	83	79	81	87	95	91
	Lower	33	24	29	18	19	19	11	5	8
	Balance	-33	-22	-28	-18	-17	-18	-9	-5	-7
4. Number of employees (compared with previous half-year)	More	5	15	10	15	10	13	18	15	17
	Same	82	75	79	69	71	70	69	73	71
	Lower	13	10	12	15	19	17	13	12	13
	Balance	-8	5	-2	0	-9	-5	5	3	4

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

to regain ground, although it is hoped that the improvement in the economy might leave a wider margin for investment in future public budgets. Employment prospects in the sector are looking up and prices also started a tentative upward trend throughout 2018.

The shortage of qualified workers, indicated by 61% of businesses, has become the biggest limiting factor.

In relation to factors that limit improvements in business, the shortage of qualified workers has become the biggest limiting factor, indicated by 61% of businesses, the highest percentage since 2004. On the other hand, weak demand

(a factor cited by 51% of constructors) and increased competition (cited by 46%) are also major obstacles, but have decreased in importance since the previous year.

It should be considered that there is still a large volume of buildings pending sale, which continues to limit new investment projects, in a context where new building is unlikely to perk up without the support of credit and a stronger recovery in the labour market and wages.

XII. Services

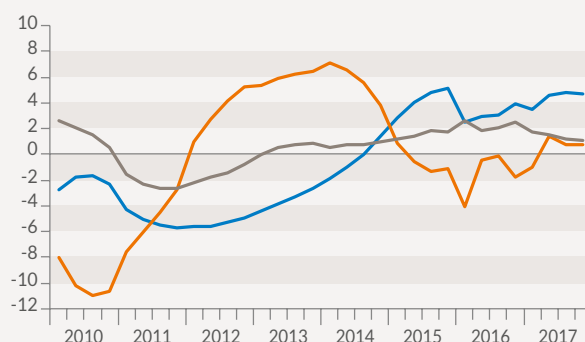
The services sector is central to the Andorran economy, concentrating 88.5% of GVA and 87.7% of total employment. The major importance of this sector means that its development largely determines the behaviour of Andorran GDP. In 2017, the service sector continued its positive trend for the fifth consecutive year and, moreover, growth accelerated. According to the Department of Statistics, the real increase in GVA in the services sector in 2017 was 2.1%, higher than the 0.9% of the previous year.

In 2017, the services sector was still the driving force behind the Andorran economy, in a context where the improvement in the tourism situation again favoured a recovery in activity in the branches of related services, such as hotels and catering and transport; in contrast, the positive influence of commerce decreased.

In 2017, the services sector was still the driving force behind the Andorran economy, with an increase in GVA of 2.1%.

The outcome in 2017 was favourable to the three major subsectors, but with different intensities and trends. So, the sector of Commerce, hotels and catering, transport, information and communications saw the most notable increase, of 4.4% year-on-year, 1.3 points more than in 2016. In contrast, the subsector of Public administration, education, health, social and personal services saw real growth of 1.4%, but the increase was slower than in the previous year (2.3%). Finally, the subsector Financial, real estate, professional

GVA OF THE SERVICES SECTOR BY BRANCHES OF ACTIVITY
Interannual variation rate (%)



Source: Department of Statistics.

and technical activities saw the weakest growth, of 0.5%, although it was able to reverse the negative trend of the previous two years.

In December 2017, there were 7,242 businesses in the services sector, 5.3% more than the previous year. If we consider the bulk of the business network, broken down by subsectors,

In 2017, there were 51% more businesses in the services sector than ten years earlier.

we can see how, for the first time, the sector of real estate and business services surpassed commerce and vehicle repairs. The sector of real estate and business services concentrates almost 32% of total businesses (2,307

businesses in 2017 with very high year-on-year growth, of 20.3%), followed by commerce with a share of 26.4% (with 1,914 businesses and a decline of 2.5%) and, in third place, hotels and catering, concentrating 11.7% of businesses (850 businesses, two less than in 2016).

If we compare the current number of businesses in the services sector with the number there was before the crisis in 2007, we can see that the number of businesses has grown significantly. Overall, it can be said that until 2013, there were no significant changes, but from that year on, there was an upward trend, reaching the figure of 7,242 businesses in 2017, 51% higher than in 2007. Apart from the improvement in the economic context, one factor that has favoured this growth was the Foreign Investment Law that came into force in 2012.

NUMBER OF BUSINESSES IN THE SERVICES SECTOR*

	2007	2016	2017	% var. 17/16	% total 2017
Commerce and motor vehicle repairs (etc.)	1,592	1,964	1,914	-2.5	26.4
Hotels & catering	746	852	850	-0.2	11.7
Transport, storage & communications	230	287	287	0.0	4.0
Financial system	80	114	112	-1.8	1.5
Real estate & rental activities; business services	862	1,918	2,307	20.3	31.9
Public administration, defence & mandatory social security	36	35	33	-5.7	0.5
Education	48	94	100	6.4	1.4
Health & veterinary activities, social services	246	448	463	3.3	6.4
Other social activities & community services; personal services	396	610	632	3.6	8.7
Extraterritorial bodies	7	6	6	0.0	0.1
Special regimes	-	1	1	0.0	0.0
Domestic work for the community	550	549	537	-2.2	7.4
Total	4,793	6,878	7,242	5.3	100

*Not including Households employing domestic staff and voluntary declarants (no activity).
Note: Data for December of the relevant year.

Source: CASS (Andorran Social Security System).

Regarding the size of these businesses, 81.4% have less than 6 workers, so the business network is formed basically of micro-businesses. In relation to 2016, the number of businesses in all size groups has risen, except businesses with more than 100 workers, of which there are 54 businesses, one less than in the previous year.

As for employment in the services sector, in 2017 the number of employees grew 3.3%, higher than the 1.9% recorded in the previous year. In total, the number of employees in the services sector has reached 33,061, divided as follows: 26.7% work in the sector of commerce; 15.1%

Box 12.1

RECYCLING IN ANDORRA

Andorra is one of the most advanced European countries in matters of recycling, considering almost 90% of its surface area is natural land and its goal is to be a model of respect for the environment and nature.

It should be remembered that the country has 80,209 inhabitants but receives more than 8 million tourists every year. Consequently, the Principality produces 109,748 tonnes of waste every year but does not have enough space or infrastructure to be able to reuse it, so it has to rely on treatment plants in Spain. In Andorra, there are two large plants: the packaging sorting plant and the waste treatment plant (Ctrasa), both in La Comella. The sorting plant only gathers and sorts waste from the different recycling bins. The waste treatment plant evaluates the energy value of everything that comes from waste bins.

According to Eurostat, Andorra is among the most advanced countries for recycling in Europe, as 63% of the 109,748 tonnes of waste go directly to the appropriate recycling plants. The energy value is 35% of the generated waste (in the EU it is close to 30%) and only 2% goes into landfill. Andorran data are more positive than those of other countries, only Slovenia or Germany achieve a higher percentage of recycled products. For example, some countries that

are considered leaders in reuse and green policies, such as Norway or Sweden, send a larger proportion of products to incinerators than Andorra. Moreover, Ctrasa uses it to produce 4% of the electricity consumed in Andorra. In 2017, 15,784.12 MWh generated from burning waste were entered into the FEDA electricity network.

Collection of bins is the responsibility of the local Comú governments, and each implements their own policy. Nevertheless, there are common standards, such as the obligatory separation of organic matter at the eight shopping centres in Andorra, and also the 21 hotels and 17 restaurants that have joined the scheme voluntarily. Hotel and catering businesses are listed as individual waste producers since 2008. This obliges them to separate paper, glass, packaging and vegetable oil. Moreover, inspections to ensure compliance with legislation were resumed mid-2007.

Following this line of environmental protection, the new regulations came into force in November 2007, obliging shops to charge 10 or 15 cents for plastic bags and stipulating that till staff cannot offer them to customers unless requested. These regulations are in line with EU recommendations and those that have started to apply in other countries, such as Spain in 2018.

in real estate and professional activities; 15% in hotels and catering, and 13.2% in public administration. Overall, these four subsectors concentrate 70% of total employees in services.

In 2017, the most notable growth in social security registrations, in rates of variation, were recorded in transport and communications (11.5%) – though this sector's share is only 3.7% – and real estate activities and business services (9.3%). In absolute terms, the most important increases in registrations were seen in the real estate and professional activities sector (424 jobs more than in 2016) and hotels and catering (255 more jobs).

The growth in employment that occurred in the last four years brought the number of registered close to the 2007 figure (when it reached 33,574 employees). In fact, the 2017 figure is only 1.5% lower than for 2007. It should also be said that part of the reduction in employees was due to employees becoming self-employed, hence the increase in the number of micro-businesses.

The sectors that created most employment in 2017 were real estate and professional activities, and hotels and catering.

NUMBER OF EMPLOYEES IN THE SERVICES SECTOR (annual average)

Table 12.2

	2016	2017	% var. 17/16	% total 2017
Commerce and motor vehicle repairs (etc.)	8,754	8,838	1.0	26.7
Hotels & catering	4,702	4,957	5.4	15.0
Transport, storage & communications	1,102	1,228	11.5	3.7
Financial system	1,947	1,867	-4.1	5.6
Real estate & rental activities; business services	4,571	4,995	9.3	15.1
Public administration, defence & mandatory social security	4,317	4,377	1.4	13.2
Education	585	583	-0.5	1.8
Health & veterinary activities, social services	1,926	2,003	4.0	6.1
Other social activities & community services; personal services	2,733	2,869	5.0	8.7
Households employing domestic staff	1,138	1,127	-1.0	3.4
Extraterritorial bodies	17	14	-15.9	0.0
Domestic work for the community	209	203	-2.8	0.6
TOTAL	32,002	33,061	3.3	100

Source: CASS (Andorran Social Security System) / Department of Statistics.

Monthly wages for the whole of the services sector fell 0.4%, after an increase of 4.7% in the previous year. This slight decline contrasts with the wage stability that occurred in the whole Andorran economy. The subsector responsible for this decrease is the financial sector, where the average wage fell 5.6% against 2016, as wages in the other subsectors grew at very moderate rates, below 2%, except in the health sector, where there was a slight decline of 0.9%.

Wages in services fell due to the financial sector.

1. Commerce

Commerce is one of the pillars of the Andorran economy, with a share of total employment of 23.4%, compared with the share of hotels and catering and the financial sector. In terms of GVA, the commercial sector represents 16.4% of Andorra's total, in 2016 figures. The trend in this sector has been marked by the crisis and falling activity during the 2006-2015 period, but there were signs of improvement in the last part of 2016, which were not consolidated in 2017, when the sector stabilised.

2017 saw stability in the commerce sector.

Andorra has traditionally been a shopping destination, but it is cause for concern that the increased inflow of tourists and gradual improvement in the overall economic situation are not improving commercial results, as expected. In fact, 2017 was a very good year for the tourism sector, with an increase in visitors of 1.6%; in contrast, the retail trade again saw a less favourable balance in the major economic sectors. So, shops indicated a gradual downturn in the volume of sales which, in 2017, resulted in a fall in turnover of 0.8% on average – contrasting with the modest increase in 2016 (0.9%) – and also a slight increase in levels of employment.

The available sectoral indicators confirm that retail trade stagnated. On the one hand, employment in the sector remained practically stable, as it only grew 0.3%, to 5,396 employees, similar to the increase of the previous year, after 10 years of downturn. The average wage stood at about 1,637 euros, 1.8% higher than the previous year but still one of the lowest wages within the services

sector. On the other hand, electricity consumption in the commercial distribution sector fell 0.5%, and lastly, the number of retail establishments fell 0.4% to 1,371 (6 fewer establishments than in 2016).

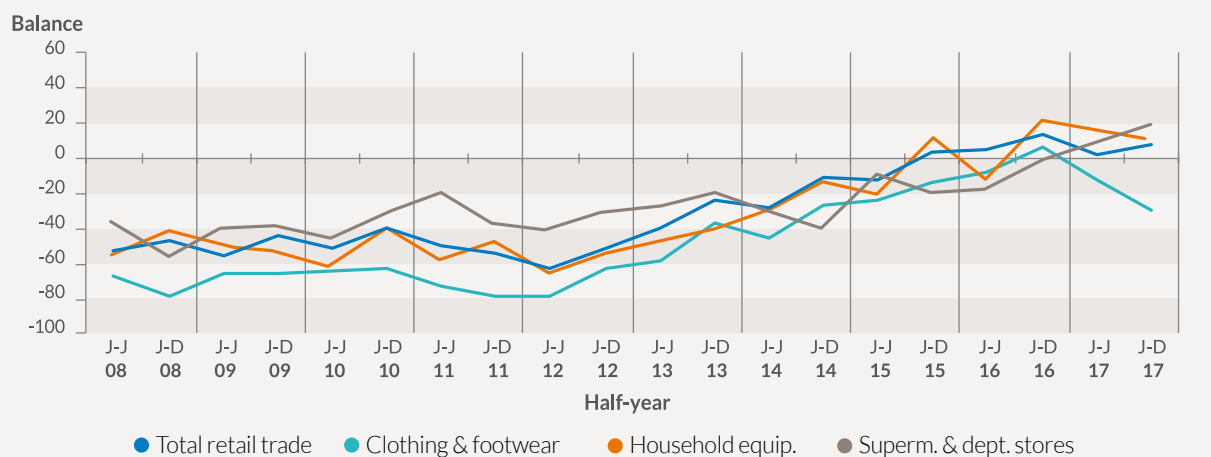
One of the best indicators of the trend in commerce is the performance of imports of goods, because they are among the majority of sales in Andorran commerce. Overall national imports grew 6.6% against 2016, boosted especially by imports of motor vehicles, thanks to the major growth in registrations in 2017, but if we exclude tobacco (which increased 3%), building materials (3.1%) and fuels (23.9%), we can see that other articles intended for commerce as such grew 5.5%, compared with 8.0% in the previous year.

Imports of goods increased, boosted by the good performance of vehicle registrations.

As usual, the performance of imports according to types of goods varied greatly. In 2017, imports of most food products increased, except cereals, oils and fats, seeds and cocoa. Among the non-food articles, the following ten chapters stand out for their contribution to global import growth in 2017, in decreasing order: motor vehicles, fuels, machines and electrical apparatus, air or space navigation, perfumery, boilers and mechanical apparatus, apparel (knitted or crocheted, and not), beverages and works of art.

The Chamber of Commerce's surveys confirm these results. Businessmen's evaluations of business activity show a positive balance in the second half of 2017, for the fifth consecutive year, but reflect a fall in levels of optimism when compared to the previous year.

BUSINESS ACTIVITY - RETAIL TRADE



Balance: Difference in opposing responses (positive and negative), as a percentage.

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

2017 was marked by an improvement in vehicles and supermarkets and department stores, and a downturn in the segments of clothing and footwear and electronics.

From a sectoral point of view, a significant improvement can be seen in the subsector of vehicles and accessories and supermarkets and department stores, with comparatively better results than in the rest of commerce. From a more negative aspect, the downturn in activity in the branches of clothing and footwear and electronics stands out. This downturn in activity in the subsector of clothing and footwear is due to slower expenditure on consumption of those articles,

BUSINESSES' OPINIONS OF DEVELOPMENTS IN THE RETAIL TRADE (% of businesses)

Table 12.3

1. Business activity (Reviewed half-year)		2015			2016			2017		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
Total retail trade	Good	16	25	21	27	32	30	25	28	27
	Normal	56	53	55	51	51	51	52	53	53
	Bad	28	22	25	22	18	20	23	20	22
	Balance	-12	3	-5	5	14	10	2	8	5
Food	Good	12	29	21	26	29	28	26	29	28
	Normal	58	46	52	62	59	61	51	53	52
	Bad	30	26	28	12	12	12	23	18	21
	Balance	-18	3	-8	14	17	16	3	11	7
Clothing & footwear	Good	9	16	13	23	26	25	12	9	11
	Normal	59	54	57	46	54	50	65	53	59
	Bad	32	30	31	31	20	26	24	38	31
	Balance	-23	-14	-19	-8	6	-1	-12	-29	-21
Household equipment	Good	15	26	21	19	41	30	31	33	32
	Normal	50	61	56	50	41	46	56	44	50
	Bad	35	13	24	31	18	25	14	22	18
	Balance	-20	13	-4	-12	23	6	17	11	14
Health & Hygiene	Good	20	35	28	43	48	46	26	26	26
	Normal	80	50	65	57	43	50	48	57	53
	Bad	0	15	8	0	10	5	26	17	22
	Balance	20	20	20	43	38	41	0	9	5
Electronics	Good	0	14	7	15	27	21	7	14	11
	Normal	71	71	71	54	60	57	57	71	64
	Bad	29	14	22	31	13	22	36	14	25
	Balance	-29	0	-15	-16	14	-1	-29	0	-15
Vehicles & accessories	Good	16	13	15	20	19	20	28	39	34
	Normal	56	61	59	56	46	51	48	46	47
	Bad	28	26	27	24	35	30	24	14	19
	Balance	-12	-13	-13	-4	-16	-10	4	25	15
Other trade	Good	22	30	26	33	32	33	28	29	29
	Normal	49	51	50	49	54	52	46	56	51
	Bad	29	19	24	18	14	16	26	15	21
	Balance	-7	11	2	15	18	17	2	14	8
Supermarkets & department stores	Good	20	30	25	25	30	28	25	40	33
	Normal	50	20	35	33	40	37	58	40	49
	Bad	30	50	40	42	30	36	17	20	19
	Balance	-10	-20	-15	-17	0	-9	8	20	14

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

together with unusually high temperatures in autumn, which slowed sales for the winter. As for other trade, although the trend in business was still favourable overall, a slight loss of momentum can be seen in comparison with the previous year.

In parallel, retail sales did not show clear signs of recovery in 2017 either. According to shopkeepers' opinions, the global sales figures were very similar to those of the previous year. The weak trend in the labour market and loss of family purchasing power, in a context of rising inflation and containment in wages, do not encourage consumers to buy, and consumer expenditure is still cautious.

By subsectors, the only branches of commerce that saw a year-on-year increase in sales on annual average, despite a very moderate profile, were supermarkets and department stores. At the other extreme, the year-on-year decline in sales was mostly concentrated in the subsectors of clothing and footwear and electronics, while the sales figure stabilised in the branch of household equipment, vehicles and accessories and the branch of other trade.

BUSINESSES' OPINIONS OF DEVELOPMENTS IN THE RETAIL TRADE (% of businesses)

Table 12.4

2. Sales figures (reviewed half-year compared with same half-year of previous year)		2015			2016			2017		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
Total retail trade	Higher	17	30	24	24	36	30	28	28	28
	Similar	37	39	38	41	33	37	34	34	34
	Lower	46	31	39	35	31	33	38	38	38
	Balance	-29	-1	-15	-11	5	-3	-10	-10	-10
Food	Higher	13	29	21	29	30	30	29	26	28
	Similar	35	38	37	35	30	33	39	35	37
	Lower	52	32	42	35	41	38	32	39	36
	Balance	-39	-3	-21	-6	-11	-9	-3	-13	-8
Clothing & footwear	Higher	13	26	20	21	38	30	19	16	18
	Similar	22	49	36	35	34	35	38	25	32
	Lower	66	26	46	44	28	36	44	59	52
	Balance	-53	0	-27	-23	10	-7	-25	-43	-34
Household equipment	Higher	25	27	26	13	36	25	40	22	31
	Similar	41	53	47	58	39	49	34	31	33
	Lower	34	20	27	29	24	27	26	47	37
	Balance	-9	7	-1	-16	12	-2	14	-25	-6
Health & Hygiene	Higher	25	45	35	48	35	42	25	35	30
	Similar	55	35	45	48	30	39	45	30	38
	Lower	20	20	20	5	35	20	30	35	33
	Balance	5	25	15	43	0	22	-5	0	-3
Electronics	Higher	0	29	15	23	36	30	17	14	16
	Similar	36	21	29	23	29	26	25	36	31
	Lower	64	50	57	54	36	45	58	50	54
	Balance	-64	-21	-43	-31	0	-16	-41	-36	-39
Vehicles & accessories	Higher	23	23	23	17	30	24	18	46	32
	Similar	50	23	37	42	35	39	36	25	31
	Lower	27	55	41	42	35	39	46	29	38
	Balance	-4	-32	-18	-25	-5	-15	-28	17	-6
Other trade	Higher	17	31	24	23	41	32	30	27	29
	Similar	33	43	38	44	32	38	31	46	39
	Lower	50	26	38	33	27	30	39	27	33
	Balance	-33	5	-14	-10	14	2	-9	0	-5
Supermarkets & department stores	Higher	20	30	25	36	36	36	42	40	41
	Similar	40	10	25	18	27	23	25	30	28
	Lower	40	60	50	46	36	41	33	30	32
	Balance	-20	-30	-25	-10	0	-5	9	10	10

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

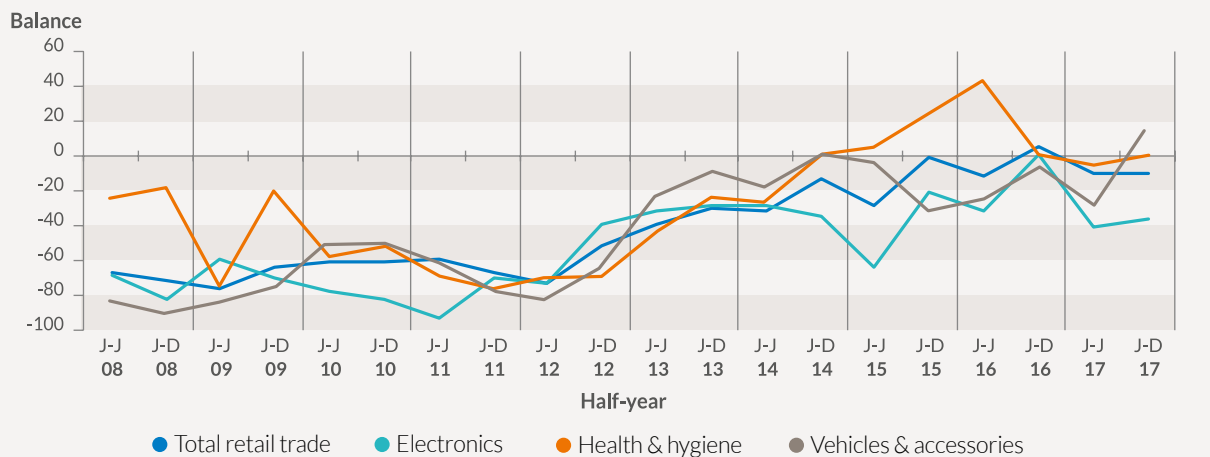
The Chamber of Commerce's situation survey highlights that levels of stocks were still high, especially in the subsectors of vehicles and accessories and clothing and footwear. Finally, regarding prices, most commerce continued to apply reductions to encourage consumption, while the rate of job creation in the labour market remained very moderate.

Businesses' expectations for the first half of 2018 remain stable. Shopkeepers do not expect any change in consumption and suggest that sales will remain at very modest levels in most branches of commerce. The trend in employment will be quite stable and sales prices will start to move slowly upward. Weak demand – cited by 59% of commercial establishments – is still the main obstacle limiting growth in activity, followed closely by increased competition (49%). In third place is notably the loss of attractiveness of the area, a factor mentioned by 40% of commerce, which is already more concerning than the increase in operating costs (36%).

Prospects for commerce in the first half of 2018 remain stable.

SALES FIGURES COMPARED WITH THE SAME PERIOD IN THE PREVIOUS YEAR - RETAIL TRADE

Chart 12.3



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

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

The change in consumer behaviour is affecting Andorran commerce.

As has been mentioned, commerce is struggling more than other economic sectors to recover from the crisis, despite good results in tourism and growth in the Andorran economy. It is

possible that structural changes are occurring in the pattern of consumption on a global scale, also affecting Andorran commerce. On the one hand, a change in the behaviour of the consumer is detected who, with the same budget, values the experience (sleeping in a hotel or going to a restaurant) much more than buying articles. Andorra Turisme's surveys confirm this hypothesis, as the number of persons spending the night increases and the number of same-day visitors falls, the latter coming almost exclusively to shop. There is also a surge in e-commerce and, in parallel, the consumer expects constant promotions, which reduces the business margins of the sector. To this is added other factors more specific to Andorra, such as the fact that there are still outdated shopping areas, rental prices for premises that never adjusted to the crisis, little innovation or difference in branding between the large franchises, and lack of staff training.

To meet these challenges, the Government has prepared a Strategic Plan for shopping tourism which is already underway.

Box 12.2

STRATEGIC PLAN FOR SHOPPING TOURISM

In March 2016, the first diagnosis of the Strategic Plan for shopping tourism was presented, with the aim of repositioning Andorran commerce. Among the aspects to be improved, the study mentions the lack of major brands, the mix of cheap and luxury shops, the need to improve the image of some shops, and the lack of staff training in the commercial sector. Among the strong points of the commercial sector are notably the continued concentration of shops covering all types of segments; specialised shops, especially in the

sectors of sport, motorcycles and chemist's; shopping centres, department stores and large stores that offer attractions; shops with large stocks, and also cross-border shopping. Other positive aspects include the fact that Andorra's image is associated with shopping and it has a high level of public safety. Additionally, the fact that a large number of sports events are organised and the country has attractions such as Caldea-Inúu, Naturlàndia, Grandvalira and Vallnord, which are a magnet for tourists.

After this first diagnosis, on 8 November 2016, the commercial and business sector of the country was presented with a second phase of the Strategic Plan, aimed at short, medium and long-term actions to position Andorra as a benchmark shopping destination.

In this second phase, 111 actions have been proposed, 59 of which are on a national scale and 52 on a sectoral scale, involving both the public and private sectors. The study establishes eleven priority actions:

1. To carry out the series of tourism and leisure-based projects currently under study: Green infrastructure plan, Thyssen Museum (inaugurated in March 2017), The Cloud, Multifunctional area, Casino, Whitewater Park.
2. To improve border access, maximise means of air transport.
3. To carry out a global reform of the town and entrance to the town of Pas de la Casa.
4. To make a town plan for the Meritxell/Vivand sector.
5. To create more prestigious events, mostly cultural.
6. To improve the quality of Pas de la Casa's offer to complete its *One Day Shopping* positioning by introducing outlets.
7. To attract new brands / propose shopping areas that meet their expectations.
8. To implement a loyalty programme for the sector.
9. To focus communication on the Andorran shopping experience.
10. To train staff and shopkeepers to improve the quality of the service.
11. To hold more top sporting events.

In 2017, the strategic shopping tourism plan already entered the phase for implementation of the actions defined in the previous work. A public-private partnership was created to pilot the plan, The Andorran Council for Competitiveness in Commerce (CACC), managed mainly by a monitoring committee that includes the Chamber of Commerce. According to the plan itself, 50% of the actions may materialise in 2017-2018. In fact, 39 actions are already underway in the first quarter of 2018, according to the Government. Measures that have already been started include enhancement of the shopping areas in the central hub, creating the multi-functional area, and shortening the sales season. The Government proposes to reduce the sales season from six months to four, two in summer and two in winter. This will be done at the end of the defined period, to maintain the advantage of starting earlier than neighbouring countries.

The new plan for revitalising commerce that began to be introduced in the last months of 2017 includes, among other aspects, the creation of a quality certificate for establishments. The Andorran Chamber of Commerce will be in charge of awarding this certificate based on objective criteria and standards to be met by the establishments.

Another important measure for the sector is boosting e-commerce. So, in August 2017, the Government passed a Bill of law on payment services and electronic money, to join the Single Euro Payments Area (SEPA). This change will encourage e-commerce in Andorra, which had been limited until now because many businesses operating on the Internet, such as Paypal, do not include transactions in Andorra.

2. The financial system

The financial system, consisting mainly of the banking and insurance sectors, represents 20.5% of Andorra's GVA (according to 2016 data). It is the most important sector in the economy in terms of GVA, but not in terms of employment, as it represents 5% of total employees. The main business areas of the financial sector are private banking and asset management, insurance and commercial banking, both for individuals and businesses.

According to official GDP data published by the Government, in 2017, Financial, real estate, professional and technical activities saw a minimal increase in GVA of 0.5%, but this is still an improvement when compared with the decrease of 1.6% in 2016.

Finance is the most important sector of the Andorran economy for GVA.

One of the great challenges that the Andorran banks have had to face in recent times was the transformation to meet international standards on transparency and cooperation, after signing 24 information exchange agreements and seven double taxation agreements, and also the automatic exchange of tax information. This challenge has been converted into an opportunity to adapt strategies to an internationally-recognised banking model.

Despite the complex environment, the financial sector has maintained and consolidated its main economic figures. The number of employees for the whole of the financial sector fell 4.1%

The financial sector has maintained and consolidated its main economic figures.

against the previous year, largely due to early retirements carried out by the banking entities, but it is still at a high level in 2017, about 1,900 individuals. Average wages for this sector, which are the highest of all the sectors in the Andorran economy, also saw a drop of 5.6%. As for the network of businesses and establishments, on 31 December there were 178 establishments (6 more than in 2016), while the number of bank branches remained at 41.

The core of the Andorran financial system is the banking system, consisting of five groups: Andbank, MoraBanc, Crèdit Andorrà, BancSabadell d'Andorra and Vall Banc. It should be remembered that the process ended in 2016 that had started one year earlier as a result of the note from the US administrative authority, the Financial Crimes Enforcement Network (FinCEN), leading to the bank Banca Privada d'Andorra (BPA) being put into administration by the Andorran National Institute of Finance (INAF), and the later creation of a new entity by the national Agency for the Resolution of Banking Entities (AREB), called Vall Banc, to receive the lawful clients, assets and liabilities from the former BPA. In April 2016 – one year and one month after the note from FinCEN – the new entity was sold, for 29 million euros, to the US investment fund J.C. Flowers, and Vall Banc started operating on 11 May 2016.

Andorra has passed with flying colours the first report of the Moneyval fifth round of evaluations, the Council of Europe body that evaluates anti-money laundering and terrorist financing measures. On 14 November 2017, Moneyval published the report on the 5th evaluation of Andorra. The report makes a very positive assessment of the deep legislative changes made in Andorra relating to the prevention of money laundering and terrorist financing, and also the classification of tax offence. The assessors highlight that these changes show a deep commitment to matters of preventing money laundering and terrorist financing, not only by the Government and authorities, but also the financial system in general. The report also praises Andorra for requesting and providing legal assistance with other jurisdictions on a proactive basis. Finally, it urges work and supervision to implement the action plan adopted on a national scale and mitigate any risk in these areas and to foster coordination between supervisory authorities.

In short, the Andorran financial system has successfully dealt with the constant regulatory changes in international standards, such as implementing regulations relating to tax transparency, measures towards international mutual assistance in criminal matters and combatting money laundering and terrorist financing, and the legislation within the monetary agreement in terms of banking regulations.

The sector has known how to adapt to the new international conditions and has done so while maintaining an added dimension. So, in 2017, the number of employees in all five banks was 2,658, a very similar figure to the previous year (2,668 employees), of which about 55% work in Andorra (about 1,472 employees).

The credibility and rigour of the Andorran financial system, together with the development of an important supply of financial products and services and the gradual consolidation of the

Box 12.3

LEGAL CHANGES IN THE ANDORRAN FINANCIAL SECTOR

On 12 February 2016, the Principality of Andorra and the European Union (EU) signed an agreement for the automatic exchange of information in tax matters (AEOI), which came into force on 1 January 2017. This agreement incorporates the new global standard for the automatic exchange of information approved by the OECD and applied in the EU under Directive 2014/107/EU.

Law 19/2016, approved by the General Council on 30 November 2016, regulates the legal framework needed to achieve this AEOI commitment.

Within this legal framework, in 2017, Andorra has been collecting bank data to make the first exchange of tax information in September 2018 with 41 countries, including all those of the European Union. The number of countries will slowly increase and is expected to exceed 80 countries in 2020. This exchange will mean that the data of foreign taxpayers with an account in Andorra will be sent to the local authority by the banking entities, investment schemes and insurance companies. Then, the local authority will automatically send this information to the tax authority of the relevant country, on an annual basis.

The data to be exchanged include the account number, tax identification number, name, address and date of birth of any taxpayers resident abroad with an account in Andorra, income (interest, dividends, etc.), income from the sale or transfer of assets and the balance of the accounts. The rule is applied to both natural and legal persons.

Another important legislative change for the sector was Law 14/2017, of 22 June, on preventing and combatting the laundering of money or securities and terrorist financing, which transposes the EU Directive on preventing the use of the financial system for laundering money or financing terrorism, which entered into force on 20 July 2017.

Finally, the Government has started proceedings to join the International Monetary Fund (IMF) in 2019, providing Andorra with backup to cover any potential financial needs in specific situations of stress, among other aspects.

The banking groups have maintained healthy liquidity and solvency ratios.

significantly in the last few years, with an increase of about 60% between 2007 and 2017, accelerating from 2011. Despite this growth, banks have maintained healthy liquidity and solvency ratios.

The financial statements for 2017 are the first that have been prepared according to the International Financial Reporting Standards (IFRS) adopted by the EU. These new standards involve major changes in the criteria for accounting, assessment and the method of presenting the data in the consolidated financial statements. 2016 data appearing in this report have been reformulated according to the new standards, so they differ from those published in the 2016 annual report.

Despite the changes occurring in the general environment, there was an increase of 1.5% in clients' assets under management, reaching a historic figure of 46,138 million euros, a sign of stability and strength in the Andorran financial market. The total volume of assets of the five banking groups was 14,145.4 million euros. The

process of international expansion of Andorran banks (present in 14 countries on four continents), have enabled activity in this sector to grow. Assets under management have grown

The aggregate profit for all the banking entities was 131 million euros.

Andorran banks ended the year with a net attributable profit of 131 million euros, a figure that represents a decrease of 15.8%. These results are influenced by the negative interest rates, which push the financial margin down, and by the growing costs of adapting to the new legal framework of the European banking sector.

Within assets, the two largest components are the chapter “Loans and receivables”, which represents 46.4% of the total assets and includes loans and discounts, and the component “Financial assets and derivatives”, which represents 33% of the total assets. The third group is the section “Cash, balances and demand deposits”, which represent 13.5%. Specifically, gross lending to clients was 5,982.8 million euros in 2017, 5.0% less than the previous year, a trend that is partly linked to the banks being more cautious when conceding loans and a still weak economic trend.

As for liabilities, the balances of Andorran banks increased from 2010, once the worst of the global financial crisis passed. The trend in clients’ deposits was directly influenced by the variation in interest rates and, therefore, international capital markets, and also the expansionary policy of banking entities. The financing structure of the Andorran banks is characterised by the major importance of “Clients’ deposits”, which represent 71.8% of aggregate liabilities. “Own funds” represent 8.5% and “Results” 0.9%, according to the annual report of Andorran Banking.

As a result, Andorran banks have maintained good levels of capitalisation, with an improvement in the liquidity ratio and a slight fall in the solvency ratio in 2017, to average figures of 65.4% and 21.7%, respectively. The three and a half points difference in the solvency ratio compared with the previous year can be explained by the impact of application of the International Financial Reporting Standards (IFRS) for the first time. However, the figure doubles the requirements of Andorran banking standards.

As for return on equity, Andorran banks ended 2017 with ROE of 9.85%, above the European average of 6.1%, according to EBA (European Banking Authority) data.

As for Andorra’s sovereign rating, in the 19 January 2018 assessment, Standard & Poor’s confirmed the long and short-term rating as BBB/A-2 with a “stable” outlook. Fitch gave Andorra the same rating (BBB/F-3), but with a “positive” outlook on 17 February 2018. The assessors value positively the schedule of reforms carried out by the Government, Andorra’s sound economic activity, the decrease in public debt and convergence with international standards, with the resulting positive image of Andorra abroad.

In 2017, the soundness of the Andorran system was confirmed for yet another year, showing strength in a context of negative interest rates and the continued adaptation of services and processes to international standards. Another challenge to the Andorran banking system is the investment being made in the field of digital transformation, guided by improvements in customer services and quality standards in banking.

AGGREGATE DATA FOR THE ANDORRAN BANKS

Table 12.5

Thousand euros	2016	2017-IFRS
Total assets	14,492,462	14,145,382
Gross loans & discounts	6,299,918	5,982,759
Assets under management	45,434,271	46,138,071
Results	155,933	131,267
ROE	9.73%	9.85%
ROA	1.03%	0.88%
Efficiency ratio	59.98%	68.05%
Solvency ratio	25.10%	21.74%
Liquidity ratio	61.41%	65.37%

Note: The 2016 data are those published by Andorran Banking in the 2016 annual report and therefore not reformulated according to the IFRS.

Source: Andorran Banking and the annual reports of banking institutions.

Andorra’s long-term sovereign rating remains at BBB.

CONSOLIDATED BALANCE SHEETS (Thousands of euros)

Table 12.6

	ANDBANK		MORABANC		CRÉDIT ANDORRÀ		BANCSABADELL D'ANDORRA		VALLBANC		TOTAL	
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
ASSETS												
Cash, cash balances in central banks and other demand deposits	1,447,004	1,595,411	19,104	43,005	251,265	325,221	22,079	43,050	167,552	174,329	1,907,004	2,181,016
Financial assets held for trading	339,490	426,335	194,835	223,441	5,547	40,509	30,445	37,263	-	11,213	570,317	738,761
Financial assets designated at fair value through profit or loss	-	-	357,145	356,757	201,545	235,134	39,526	34,827	14,953	149,786	613,169	776,504
Financial assets available for sale	230,468	318,075	419,793	335,107	270,128	333,822	59,040	53,084	62,883	116,582	1,042,312	1,156,670
Loans and receivables	1,664,601	1,703,068	1,360,329	1,502,145	2,647,418	2,733,717	428,833	385,158	467,998	448,312	6,569,179	6,772,400
Hold-to-maturity investments	291,569	449,128	66,408	31,601	1,603,403	1,579,095	154,495	135,683	-	12,182	2,115,875	2,207,689
Derivatives - Hedge accounting	90	43	753	43	-	-	1,241	1,058	-	-	2,084	1,101
Fair-value changes in hedged items in portfolio for hedging interest rate risks	4,184	4,546	12	-	25,611	34,359	-	-	-	-	29,807	38,905
Investment in joint ventures and associates	2,000	-	31	50	31,491	26,696	-	60	47	36	33,569	26,842
Assets covered by insurance and reinsurance contracts	-	-	35,961	38,021	2,760	2,706	-	-	47	-	38,721	40,727
Tangible assets	34,788	25,405	83,120	80,540	127,155	139,053	25,148	26,479	59,009	59,028	329,220	330,505
Intangible assets	251,284	229,838	10,550	10,587	112,717	106,953	257	261	16,687	10,410	391,495	358,049
Tax assets	31,600	17,735	6,936	7,031	25,694	31,613	201	118	273	2,145	64,704	58,642
Other assets	79,197	174,925	7,565	14,165	51,898	62,046	6,659	5,240	28,605	6,743	173,924	263,119
Non-current assets and disposable groups of items held for sale	46,965	42,820	15,153	18,589	103,285	111,188	5,799	5,388	92,800	-	264,002	177,985
TOTAL ASSETS	4,423,240	4,987,286	2,577,695	2,661,082	5,459,917	5,762,112	773,723	727,669	910,807	990,766	14,145,382	15,128,915
LIABILITIES												
Financial liabilities held for trading	58,088	28,187	16,167	18,479	4,772	7,212	-	-	-	-	79,027	53,878
Financial liabilities designated at fair value through profit or loss	-	-	405,870	461,982	123,374	123,094	39,526	34,836	-	-	568,770	619,912
Financial liabilities at amortised cost	3,709,259	4,210,464	1,739,956	1,767,667	4,493,974	4,889,126	638,123	609,639	741,517	768,065	11,322,829	12,244,961
Hedging derivatives	3,089	4,454	3,148	4,663	42,192	48,661	1,150	604	-	-	49,579	58,382
Fair-value changes in hedged items in portfolio for hedging interest rate risks	-	-	779	-	-	-	-	-	-	-	779	-
Liabilities covered by insurance and reinsurance contracts	-	-	86,094	83,158	254,287	294,370	-	-	-	-	340,381	377,528
Provisions	40,054	94,391	26,004	24,941	62,305	64,228	1,175	1,139	2,679	149,548	132,217	334,247
Tax liabilities	25,027	16,385	5,360	5,294	2,169	8,721	1,180	409	3,294	4,721	36,970	35,530
Other liabilities	80,283	155,007	17,067	24,203	55,746	64,597	11,202	7,169	12,668	10,989	176,966	261,965
Liabilities included in disposable groups of items held for sale	-	-	-	-	-	-	15	-	86,660	-	86,675	-
TOTAL LIABILITIES	3,915,800	4,508,888	2,300,445	2,390,387	5,038,819	5,500,009	692,371	653,796	846,758	933,323	12,794,193	13,986,403
NET EQUITY												
Capital	78,842	78,842	42,407	42,407	63,462	70,000	30,069	30,069	30,000	30,000	244,780	251,318
Issued equity instruments other than capital	73,441	73,441	-	-	-	-	-	-	-	-	73,441	73,441
Accumulated earnings	375,208	341,595	145,608	148,469	-	-	-	-	16,319	(648)	537,135	489,416
Revaluation reserves	1,942	1,942	-	-	-	-	2,288	2,288	-	-	4,230	4,230
Other reserves	(58,338)	(63,018)	75,841	63,721	293,721	151,029	38,535	31,250	10,232	10,232	359,991	193,214
Own shares (-)	(1,605)	(1,605)	-	-	-	-	-	-	-	-	(1,605)	(1,605)
Profit/loss of financial year allocated to owners of parent company	39,153	44,642	23,517	22,695	50,194	31,532	10,039	10,161	8,353	16,967	131,256	125,997
Interim dividend (-)	-	-	(12,925)	(13,800)	-	(7,900)	-	-	-	-	(12,925)	(21,700)
Minority interests	-	-	(4)	(4)	-	-	-	-	-	-	(4)	(4)
Own funds	508,643	475,839	274,444	263,488	407,377	244,661	80,931	73,768	64,904	56,551	1,336,299	1,114,307
Other global accumulated profit/loss	(1,810)	695	2,806	7,207	4,972	8,319	421	105	(855)	892	5,534	17,218
Minority interests	607	1,864	-	-	8,749	9,123	-	-	-	-	9,356	10,987
TOTAL NET EQUITY	507,440	478,398	277,250	270,695	421,098	262,103	81,352	73,873	64,049	57,443	1,351,189	1,142,512
TOTAL NET EQUITY AND LIABILITIES	4,423,240	4,987,286	2,577,695	2,661,082	5,459,917	5,762,112	773,723	727,669	910,807	990,766	14,145,382	15,128,915

Source: Andorran Banking and the annual reports of banking institutions.

Data reformulated by applying IFRS in force on 31 December 2016.

3. Tourism

According to the official GDP figures, the sector of hotels and catering represents about 8% of Andorran GVA (according to 2016 data), but the indirect impact of tourism is higher, as it strongly influences other sectors, such as commerce and leisure and sporting activities, which greatly depend on visitors. This means that the favourable trend in tourism that has been seen since 2014 was fundamental to the improvement in Andorra's economic situation. The sustained growth in the sector was the result, on the one hand, of the overall improvement in surrounding countries and, on the other hand, various actions to stimulate demand carried out by both the public sector and by private operators. According to the situation surveys for all economic sectors, the one with the most positive trend in 2017 was again the hotel sector, for the third consecutive year. The rise in proximity tourism, especially from Spanish tourists, largely contributed to this more favourable trend in hotel and catering activity.

TREND IN VISITORS AND TOURISTS
2011-2017



Source: Department of Statistics.

The number of visitors has risen for the fourth consecutive year.

This improvement in tourism is reflected in the increase in the total number of visitors which occurred again in 2017 (1.6%), for the fourth consecutive year, putting the total number of visitors at 8,152,148. This figure is close to that of 2010 (8.5 million) but still far from the 11 million visitors received by Andorra before the crisis.

The increase in entries of visitors was led solely by strong growth in the number of tourists, who spend the night and, therefore, spend more inside the country. Specifically, they reached the figure of 3 million tourists, 6.5% more than in 2016. This progress was offset – but only partly – by a reduction of 1.1% in same-day visitors, to 5,149,288.

In 2017, the number of tourists reached a high of 3 million.

By nationalities, the growth in Spanish visitors (2.8%) and other nationalities (6.8%) stands out, while the number of French visitors fell 1% in 2017. As a result, Spain consolidates its position as the main country of origin of visitors, with 51.6% of the total. The importance of France decreases to 40%, and other nationalities rises to 8.4%. In the specific case of tourists, the trend rose strongly in the case of Spanish (8.3%), while the number of French tourists stabilised. As a result, Spanish tourists have come to represent 72% of the total. In contrast, the number of same-day visitors fell, both of Spanish and French nationality (-2.4% and -1.2%, respectively), while other nationalities increased (9.9%). Nevertheless, the majority of same-day visitors are French (54%), with a high concentration in August. So, the French market is characterised by a very high level of seasonality, with a predominance of same-day visitors, but the behaviour of Spanish visitors is clearly different. There is a notably high influx of Spanish tourists in August, but at levels that are comparable to other times of the year, such as the skiing months and, secondly, Easter Week.

Altogether, this has resulted in an increase in the total number of overnight stays in the various establishments, of 5.3% against 2016, to reach the figure of 8,738,438, the highest in recent

TOTAL VISITORS BY NATIONALITY AND FRONTIER

Table 12.7

		2016	2017	% var. 17/16	% total 2017
Total by nationalities	Spanish	4,093,378	4,209,681	2.8	51.6
	French	3,293,202	3,260,291	-1.0	40.0
	Others	638,685	682,176	6.8	8.4
Spanish frontier	Spanish	3,854,786	3,949,087	2.4	48.4
	French	323,016	302,153	-6.5	3.7
	Others	484,914	524,130	8.1	6.4
French frontier	Spanish	238,592	260,594	9.2	3.2
	French	2,970,186	2,958,138	-0.4	36.3
	Others	153,771	158,046	2.8	1.9
TOTAL VISITORS		8,025,265	8,152,148	1.6	100

Source: Department of Statistics.

years. The average overnight stay remained at 2.9 days, in line with the average for the last decade. The increase in overnight stays was led by hotels, increasing 13.3%, and campsites, increasing 64%. In contrast, the number of overnight stays in apartments – which includes aparthotels and tourist apartments since 2017 – fell 18%. Consequently, hotels have increased their share and are still by far the most important type of accommodation (64% of the total). In second place are apartments, with a share of 16% in 2017, and then homes of friends or family, with 9.1% of the total.

The number of employees in the sector grew 5.4%, 2017 being the third consecutive year of increase.

The upward trend in tourism is corroborated by the progress in other indicators for the hotels and catering sector. Specifically, the number of employees in the sector grew 5.4%, the third consecutive year that this figure has risen.

Moreover, wages in the sector saw an increase of 2.3% in the context of an improving economic trend, added to growth of 2.1% in 2016. The number of establishments also grew 2.7% (27 new establishments), to reach a total volume of 1,029 establishments, the highest figure in the whole available series. In line with this growth, electricity consumption increased 1.9% in the case of hotels and catering, while it fell 9.8% in ski resorts because the snow cannons were used less due to a good snow season. Equally, the number of permits for non-EU workers in the hotel sector saw a positive trend of 39.3% in the 2017-2018 season, compared with the previous season, and a variation of 6.2% in EU permits. In contrast, practically no variations were seen in the number of permits for workers on the slopes and ski rentals in comparison with the previous season.

During the winter months, the importance of activity linked to skiing can be measured by the number of passes sold. Sales of passes in the 2017-2018 season show a positive trend in comparison with the previous season. After some years in which the crisis was reflected in this activity, the 2017-2018 season came close to the levels before the crisis, in which sales of passes stabilised at around 2.5 million.

2.5 million passes were sold in the 2017-2018 season, 1.4% more than in the previous season, a figure that is close to the 2005-2006 winter record.

The 2017-2018 season started on 1 December and ended on 8 April at Grandvalira and Vallnord-Pal-Arinsal, and 30 April at Vallnord-Arcalis. In total, the three resorts were open for an

PASSES/DAY SOLD BY SEASON

Table 12.8

Season	Ski days (Passes/day 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
2017 - 2018	2,514,049	1.4

Note: estimated as 20 days use per pass for seasonal passes.

Source: Ski Andorra.

The accommodation supply remained stable in comparison with the previous year, with 235 establishments.

representing 2,372 homes used for tourism and 11,966 beds (putting this niche in the tourism supply well above the other types except hotels), 28 mountain huts, 8 campsites, 1 camping area, 1 summer camp, 2 hostels, 7 tourist houses and 8 rural accommodation.

It should be noted that once the 21 regulations of the new Law on tourist accommodation come into force, the more than 2,300 furnished tourist apartments registered in Andorra will have one year to be regularised and obtain the certificate to operate.

In 2017, there was an increase of four hotel establishments and one *hostal*, an increase that was offset by the reduction in the number of *pensions*, apart-hotels and tourist apartments.

As a result, the number of hotel beds reached 27,874, already 84% of the total supply of beds by type of establishment. On the other hand, the number of beds in apart-hotels remained about 2,600, and beds in tourist apartments fell 281, to 2,002 beds. Among the other types of accommodation, beds in furnished tourist apartments predominate, 11,966 in 2017, 7.4% more than the previous year.

average of 132 days. Easter Week extended the winter season until the end of April. The number of passes/day sold was 2,514,049, 1.4% more than the previous season, and approached the record figure reached in winter 2005-2006. In contrast, visits to other leisure services fell 0.9% (Caldea and Inúu spa, the Ice Palace, Naturlàndia, museums, monuments and mountain huts). In parallel, the ski resorts continued to increase investment to improve and equip the installations. Investment this year was 15.4 million euros. Many campaigns were also continued abroad, as was the organisation of major events and the promotion of activities to attract potential clients. Adequate numbers of skiers were attracted from international markets. The increase in numbers from the French, UK and Russian markets and the consolidation of the Belgian and Nordic markets stand out.

Despite the rising tourism demand, the supply of accommodation remained stable compared with the previous year, with 235 establishments – having suffered a serious downturn between 2009 and 2016 – bringing stability also in the number of beds, which were close to 33,000 in 2017. Of the accommodation supply, 171 are hotels, 20 apart-hotels, 11 *hostals/residencies*, 6 *pensions* and 27 tourist apartments. On the other hand, there are also 128 classified other tourist accommodation, including 73 businesses operating homes used for tourism (EGHUT),

The number of hotel beds increases as do furnished rental apartments.

Regarding the accommodation supply (beds) per parish, a high concentration can be seen in parishes considered to be at the “foot of the slopes” (Encamp 18.9%, Canillo 20.7%, and La Massana 16.5%), and also central parishes (Andorra la Vella 18.2% and Escaldes-Engordany 17.5%). In Sant Julià de Lòria (2.2%) and Ordino (5.9%), despite having important infrastructures, the distance between the town centres and the infrastructures reduces the “foot of the slopes” effect. In 2017, there was an increase in the number of beds in Encamp, Ordino, Escaldes-Engordany and La Massana, and a decrease in Sant Julià de Lòria, Canillo and Andorra la Vella. As for the number of establishments, they increased from 49 to 51 in Encamp, but fell from 38 to 37 in La Massana and from 35 to 34 in Andorra la Vella.

TOURIST ACCOMMODATION SUPPLY BY PARISHES

Table 12.9

	2016		2017		% var. 17/16		% total 2017	
	Establ.	Beds	Establ.	Beds	Establ.	Beds	Establ.	Beds
Canillo	45	7,014	45	6,865	0.0	-2.1	19.1	20.7
Encamp	49	6,068	51	6,262	4.1	3.2	21.7	18.9
Ordino	27	1,927	27	1,967	0.0	2.1	11.5	5.9
La Massana	38	5,406	37	5,454	-2.6	0.9	15.7	16.5
Andorra la Vella	35	6,097	34	6,039	-2.9	-1.0	14.5	18.2
Sant Julià de Lòria	8	774	8	735	0.0	-5.0	3.4	2.2
Escaldes-Engordany	33	5,677	33	5,777	0.0	1.8	14.0	17.5
Total	235	32,963	235	33,099	0.0	0.4	100	100

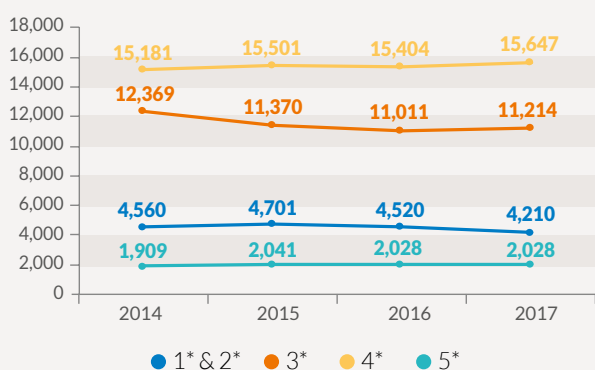
Note: Data on 31 December of the relevant year.

Source: Department of Tourism / Department of Statistics.

The number of beds increased in the higher categories and fell in categories 1* and 2*.

TREND IN THE NUMBER OF BEDS BY CATEGORY OF TOURIST ACCOMMODATION

Chart 12.5



Source: Department of Tourism / Department of Statistics.

As for categories of tourist accommodation, 53% of beds offered are in higher categories (4* and 5*). In 2017, the number of beds in lower categories (1* and 2*) fell 7%, while the number of 3* and 4* beds increased, which are also the most abundant, clearly indicating the sector’s emphasis on quality. The number of 5* beds is the same as the previous year. Hotels are constantly improving the category of their beds to attract clients with higher purchasing power. On the other hand, clients with more basic accommodation requirements also find an acceptable, broad supply of other types of accommodation, such as furnished holiday apartments.

As for the spa, Caldea, the operating company (SEMTEE, SA) is continuing its business strategy aimed at increasing frequency and average entry per user, with a policy of promoting new projects such as Caldea Likids (spa area for children aged 3 to 8) or Inuú. In

2017, the spa received 400,965 visits, 3% more than in the previous year, representing 14,000 more people than in 2016, figures that are comparable to those before the crisis. Likids almost tripled the number of entries compared with 2016, with more than 11,500 children, while Inuú

maintained numbers, but at a higher price. As a result, Caldea ended the 2017 financial year with net profits, after a period in which the business had seen consecutive losses due to the economic crisis and the investment effort involved in opening Inuú. Caldea ended 2017 with annual income of 14.7 million euros and a net profit of 245,400 euros, contrasting with the -63,800 in 2016.

Caldea ended 2017 with net profits.

As for Camp de Neu La Rabassa, in the 2017-2018 winter season, the snow park was open for a total of 98 days and recorded 36,238 visitors. The number of visitors per day was very similar to the previous season: an average of 370 visitors/day compared with 374 in the previous winter. This was a particularly good season for snow, with all snow activities available over the whole season, a total of 15 km of cross-country skiing trails, snowshoes, toboggan slope and snowbikes. In contrast, Naturlàndia, the ecological theme park at La Rabassa, received 118,847 visitors in 2017, much fewer than the 183,100 visitors in the previous year.

In 2017, the Ice Palace also had better results than in 2016. Specifically, operating income grew at a rate of 2.2%, while costs fell at a similar rate (-2.4%) and current subsidies fell 10.4% (to 369,000 euros). Altogether, this resulted in a positive result of 129,000 euros (127,000 in 2016). Moreover, investment reached the figure of 206,000 euros, contributing to improvements in the installations.

Cirque du Soleil's show had a positive impact on tourism in July.

The Government estimated that the impact of *Scalada Stelar*, the show by Cirque de Soleil, was almost 20 million euros, and that 20% of tourists in Andorra in July attended it. The

plan is for the Cirque de Soleil to perform there for the next two summers. An addition to the cultural offering this year was the new Carmen Thyssen Andorra Museum, which opened on 16 March 2017, and received an average of nearly 2,000 visitors per month.

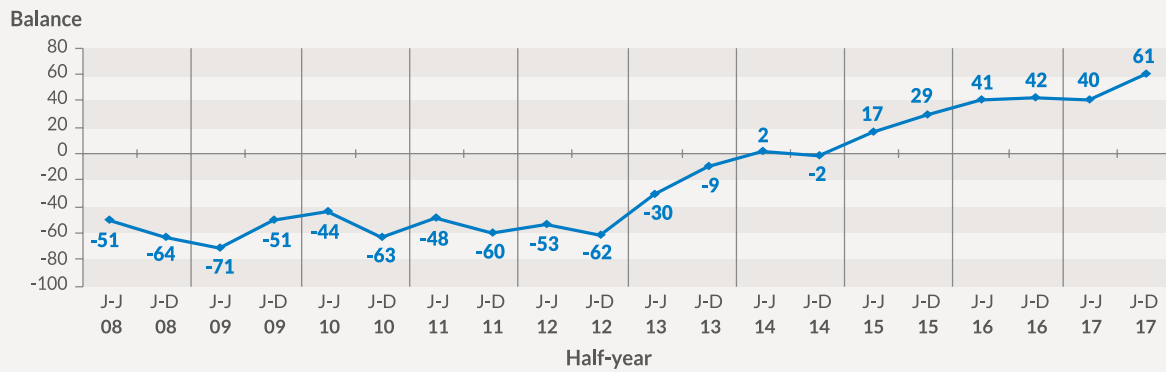
A new project to increase Andorra's attractiveness to tourists is the construction of a casino. At the end of June 2018, the contract was awarded to Jocs SA, the only one of nine candidates that bid with 100% Andorran capital. The casino complex will be built on a piece of land located in Carrer Prat de la Creu. The installation will be connected to the town square and consist of four floors and two underground floors. In total, there will be a smoke-free area of 4,000 m², containing restaurants, leisure activities and other events. The facilities, employing nearly 200 people with an investment of 15 million euros, are expected to attract some 190,000 new visitors.

Based on hoteliers' responses to the Chamber of Commerce's situation surveys, 2017 was notably good for tourism, favouring continued expansion in the sector, especially in the second half of the year. So, according to business opinions gathered in the situation survey of the second half of 2017, a major improvement was seen in business activity compared with previous half-years, confirming the impression that the recovery in the sector is strengthening and, moreover, stabilising.

From a geographical point of view, the improvement was noted in both the more commercial areas of the country, traditionally more dynamic outside the skiing season, and the peripheral areas, especially La Massana and Sant Julià de Lòria, which achieved overall satisfactory levels of activity.

BUSINESS ACTIVITY - HOTEL SECTOR

Chart 12.6



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

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

This good trend in hotel activity can mostly be explained by the excellent result in tourism from the summer campaign, with more than one million tourists arriving in Andorra (12.2% more than the previous summer), but also thanks to the positive results of specific actions to encourage shopping, such as Andorra Shopping Festival or Black Friday, which help to increase the inflow of tourists in the low season. From a geographical point of view, the average level of occupancy only saw a slight year-on-year fall in the second half of 2017 in Canillo; in contrast, the trend was quite stable in Encamp and increased in the other parishes, mainly Escaldes-Engordany,

The summer 2017 campaign was excellent, with 12.2% more tourists than in the previous year.

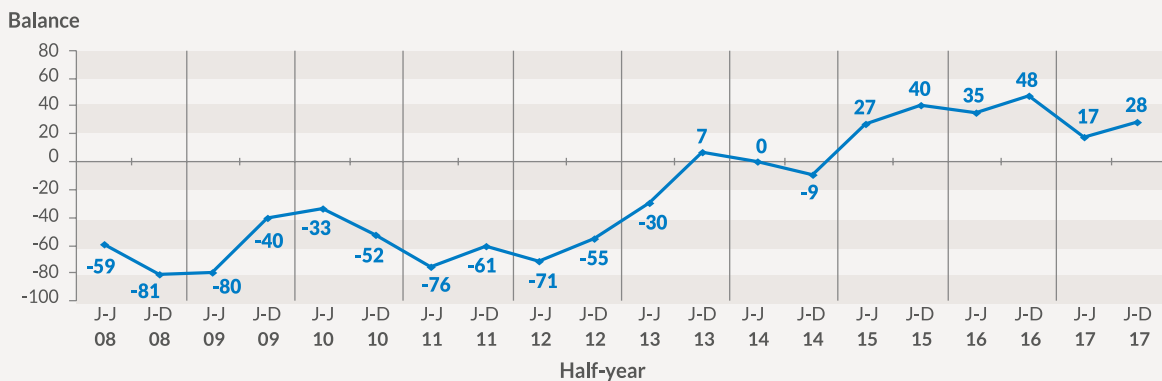
Sant Julià de Lòria and La Massana. According to the opinions of hotel businesses, the number of employees saw a slight year-on-year increase and sales prices headed slightly upward.

As for the distribution of clients per country of origin, Catalonia is still the most important place of origin, with 41% of tourists in 2017, compared with clients from the rest of Spain, with 24%. In a year-on-year comparison, a stable trend can be seen in French travellers - representing 19% - and an upward trend in clients from more distant points, a group that has increased its global share of the total to 17%.

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LEVEL OF OCCUPANCY IN COMPARISON WITH THE SAME PERIOD OF THE PREVIOUS YEAR - HOTEL SECTOR

Chart 12.7



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

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

BUSINESSES' OPINIONS OF DEVELOPMENTS IN THE HOTEL SECTOR (% of businesses)

Table 12.10

		2015			2016			2017		
		Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average	Jan-Jun	Jul-Dec	Average
1. Business activity (reviewed half-year)	Good	25	40	33	55	51	53	45	65	55
	Normal	67	49	58	31	40	36	50	31	41
	Bad	8	11	10	14	9	12	5	4	5
	Balance	17	29	23	41	42	42	40	61	51
2. Average distribution of clients (%) (reviewed half-year)	Catalonia	42	39	41	36	43	40	40	42	41
	Rest of Spain	23	27	25	27	25	26	24	23	24
	France	20	21	21	18	21	20	19	19	19
	Others	14	13	14	19	11	15	18	16	17
3. Level of reservations (reviewed half-year)	High	8	19	14	25	13	19	16	27	22
	Adequate for period	65	51	58	55	67	61	67	58	63
	Low	27	26	27	18	20	19	16	13	15
	Reservations not taken	0	4	2	2	0	1	0	2	1
	Balance	-19	-7	-13	7	-7	0	0	14	7
4. Average level of occupancy (compared with same half-year in previous year)	Higher	47	49	48	48	55	52	31	49	40
	Equal	33	42	38	40	39	40	55	30	43
	Lower	20	9	15	13	7	10	14	21	18
	Balance	27	40	34	35	48	42	17	28	23
5. Prices paid by clients (compared with previous half-year)	Higher	31	11	21	36	36	36	40	38	39
	Equal	53	49	51	53	38	46	47	29	38
	Lower	16	40	28	11	27	19	14	33	24
	Balance	15	-29	-7	25	9	17	26	5	16
6. Number of employees (compared with same half-year in previous year)	More	16	19	18	11	25	18	14	15	15
	Same	65	70	68	87	73	80	81	78	80
	Less	18	11	15	2	2	2	5	7	6
	Balance	-2	8	3	9	23	16	9	8	9

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

Businesses' opinions for the first half of 2018 are still more optimistic and indicate that the recovery in this sector will continue to strengthen. The good trend in demand will affect sales prices, which will continue a stronger upward trend, and also the labour market, with a moderate increase in employees in the sector. In businesses' opinions, the shortage of qualified staff has become the main obstacle to good business activity – almost 8 of every 10 hotels indicated it – clearly above other factors, such as the increase in operating costs (cited by 55% of those surveyed) and the increase in competition (mentioned by 45%).

4. Transport and communications

Following the line of the main sectors of the economy, activity in the branch of transports and communications showed a positive trend in 2017. The sector of transport and storage represents 1.7% of total GVA, and the sector of information and communications 4.9% (2016 data). In terms of employment, the transport sector (including overland and air transport and related activities, including travel agencies) represents 2.4% of total employees, and the sector of mail and communications, only 0.9%, in 2017.

In 2017, employment in the transport and communications sector increased 11.5%.

In 2017, there were 1,228 employees in the whole sector, 11.5% more than the previous year. This increase is added to that of 2016, which was 4.3%. The two branches saw a positive trend in the labour market, although it

was more important in the case of the sector of mail and telecommunications (19.3% compared with 8.8% in the transport segment).

The improvement in the economic context resulted in a moderate increase in the average wage for the whole sector, of 1%, in line with the previous two years. The increase is due to the subsector of transport, as wages in the segment of mail and communications fell 3.9%.

Another indicator of activity in the sector that is improving is the number of establishments, which grew 3.4% in 2017, to 429. However, this increase can only be explained by the growth in establishments dedicated to activities related to transport and travel agencies (from 200 to 217) which, in turn, was undoubtedly favoured by the overall improvement in tourism. In contrast, the number of establishments in other categories of transport and the segment of mail and communications fell slightly.

As for vehicle registrations, the data show a two-digit increase for the fifth consecutive year, 18.2% in 2017. In absolute terms, 4,552 vehicles were registered in 2017, the highest figure since 2007. This very positive trend in demand benefitted from the incentives to buy eco-friendly vehicles, sponsored by the Government (Engega programme). By type of vehicle, car registrations, concentrating 70% of the total, grew 19.1%. The other two categories with most registrations are motorcycles, which saw an increase of 14.1%, and vans, with 8.2%. Then come lorries and special vehicles, which increased 45.8% and 21.6%, respectively, highlighting the relaunch of investment plans by businesses in the face of favourable economic prospects.

There was an extraordinary increase in car registrations, making Andorra the country with most vehicles per person in the world.

As a result of this extraordinary growth in registrations, the number of vehicles increased for the second consecutive year, at a rate of 3.9%, the highest since the start of the rising trend in

VEHICLE REGISTRATIONS (units)

	2014	2015	2016	2017	% var. 17/16	% total 2017
Cars	2,194	2,431	2,686	3,198	19.1	70.3
Motorcycles	525	574	718	819	14.1	18.0
Vans	167	200	244	264	8.2	5.8
Lorries	45	33	59	86	45.8	1.9
Special vehicles	39	29	37	45	21.6	1.0
Mopeds	14	19	17	11	-35.3	0.2
Snowbikes	16	19	12	30	150.0	0.7
Others*	79	89	79	99	25.3	2.2
Total	3,079	3,394	3,852	4,552	18.2	100

(*) Consisting of private trailers and agricultural tractors.

Source: Department of Transport.

Table 12.11

THE ENEGGA PROGRAMME

At the end of October 2017, the Government announced a second phase of the Engega programme because the allocation of 850,000 euros for the first phase had run out before the final date of 15 November. This was intended to extend the first offer of financial aid to electric transport, and also to improve energy efficiency and vehicle safety, with an additional allocation of 150,000 euros. The second offer follows the same conditions as the first, providing 166 subsidies (130 for cars, 20 for vans and 16 for motorcycles) and the programme aims to promote pure electric vehicles, although it continues to subsidise plug-in hybrid vehicles, to a lesser extent. The Engega programme emerged in 2016 as a three-year programme to put Andorra at the forefront of electric transport. In the first year Andorra already

reached third place in the world in relation to the percentage of sustainable transport, with 4.83%.

In January 2018, the supplementary 150,000 euros had already run out. With renewal of the programme, some new aspects were introduced. On the one hand, subsidies were increased from €9,000 to €10,000 for buying professional electric vehicles (N1 vans). On the other hand, subsidies were increased from €750 to €1,250 for scrapping a professional vehicle when buying an electric, plug-in hybrid or energy-efficient vehicle. Finally, Law 15/2016, of 20 October was amended, amending Law 4/2016, of 10 March, on promoting electric vehicles, eliminating the corrective factor favouring diesel vehicles in the formula for calculating horsepower.

2014. The number of vehicles per 1,000 inhabitants (of estimated population) is 1,128 counting all vehicles, and 763 counting only cars. This means that on average there are more vehicles than residents. In fact, Andorra is the country with most vehicles per person in the world, according to the latest data published by the Andorran Automobile Club (ACA). The study by the World Health Organisation (WHO) on the world situation and road safety in 2015 put Andorra in second place after Finland, among the countries with the greatest density of vehicles per inhabitant in the world, but Andorra beat the Nordic country in 2016.

The transport sector sees this high demand as an opportunity to introduce electric vehicles. In fact, there was a notable increase in registrations of electric and hybrid vehicles, largely due to the

Registrations of electric and hybrid vehicles have increased notably thanks to the Engega programme.

Engega programme subsidising the purchase of plug-in electric and hybrid vehicles. Specifically, in 2017, 102 x 100% electric vehicles and 113 hybrid vehicles were registered (plug-ins and non-plug-ins), much higher numbers than the 3 and 24 respective registrations in 2015,

before the Engega programme was started. These two categories of vehicles already represent 4.7% of the total, a percentage that places Andorra at the forefront for this kind of vehicle.

The Government's transport policy also plans to promote electric bikes and shared public transport. On the one hand, in summer 2018, the shared electric bike service Cicland was started, with fourteen docking stations around Andorra and about fifty bicycles available to users. Implementation of this new means of transport will go hand-in-hand with the creation of cycle lanes. The project foresees rentals of electric vehicles to complement the service. On the other hand, it is planned to make the price of public transport more attractive and increase its frequency. It should be noted that in 2017, the new national bus station was put into operation, which will receive an average of 50 buses every day.

Box 12.5

MAIN ACTIONS BY ANDORRA TELECOM IN 2017

If 2016 marked the end of copper lines, 2017 was an equally important year for Andorran communications, thanks to renewal of the active fibre optic network, a project that approached the challenge of changing the equipment in a total of 35,000 homes and businesses, completed in a record time of nine months. The changeover provided an internationally cutting-edge network, increased the universal service bandwidth to 300 Mbps and reduced the number of incidents to one fifth.

The renewal of technology is accompanied by a new range of mobile services with important advantages for the users. On the one hand, mobile contract data is increased substantially and, on the other hand, new specific services are created, which include connecting from abroad. Coverage of clients' needs is also extended with the elimination of the limit on download data for businesses. For individuals, domestic traffic becomes unlimited and international data is extended from 200 GB to 500 GB.

The company invested 20.4 million euros in 2017, with the change in fibre optic as its flag project. Other important milestones are the improvement in the platform of TV via Internet (it currently has 12,000 clients subscribed to the Som Televisió platform), optimising the virtual switchboards, modernising data transport and IP voice networks, and expanding international voice and data links. Throughout 2017, a major effort was also made to improve the mobile network both in coverage and speed and capacity.

In the area of public responsibility, the effort to digitalise society and develop ICTs materialised in the creation of the first incubator/accelerator, the NIU, supported by a wide network of mentors and advisers. 2017 ended with seven start-ups and the celebration of NIU Demo Day, a day with investors to finance projects of the NIU or other businesses.

The constant belief in actions with a social impact, such as the educational network XENA, the emergency

radio system TETRA or the public mail server andorra.ad, is confirmed with the acquisition by the fire service of the Lifeseeker system, a pioneering tool for locating missing persons, and the promotion of the app B-resol, for reporting cases of school bullying and encouraging mediation.

Avatel has been a major milestone in the company's diversification policy. The acquisition of 37.3% of the shares in the telecommunications operator on the Spanish side for 16.5 million euros makes Andorra Telecom a reference shareholder and enables it to offer, as priority provider, a whole series of services, such as monitoring the network, technical systems support or telephone assistance.

Also in the international field, the disinvestment from the operator MásMóvil represented a capital gain of 26.7 million euros. Finally, the contact centre Espic, in which Andorra Telecom has 50% of the shares, continues its upward trend with a turnover of 1.4 million euros, profits of 287,000 euros and a workforce of 59 employees in its third year of life.

As for profits, Andorra Telecom ended 2017 with a total turnover of 95.6 million euros, 10.8% higher than the budgeted 86.3 million euros. Two elements can explain this trend: on the one hand, the growth in client turnover, 6.8% higher than expected, and, on the other hand, the behaviour of income from roaming in Andorra, with a smaller downturn than expected, representing a total turnover of 39.6 million euros.

Revenue from roaming in Andorra, "roaming in", saw a decline of 10.2 million euros in relation to the historic figure achieved in 2016, the last before the new European Standard on *Roaming like at home* came into force. In total, the downturn was lower than expected by 5.6 million euros. The policy of adapting to the new European regulatory framework on roaming and the agreements with foreign operators have enabled mitigation of the expected decline in turnover.

Source: Andorra Telecom.

In relation to the branch of communications, the same dynamic as the last four years was confirmed, with an increase in the number of mobile contracts (5.5%), making the total 80,337 lines, together with stagnation in the number of land lines after a long period of decline. In 2017, there are 47,287 lines. On the other hand, there are 34,284 fibre optic lines, representing an increase of 5.5% against 2016. The ratio of Internet broadband lines per 100 inhabitants is already 46 and the ratio of mobile phone lines exceeds 107, so there are more mobiles than inhabitants in Andorra.

In 2017, fibre optic and mobile phone lines increased.

This dynamic is confirmed when observing the trend in telephone traffic. In 2017, national land line traffic fell 4.8%, while mobile traffic increased 9.4%. International traffic fell for the tenth consecutive year, 9.7% for incoming traffic and 4.6% for outgoing. For its part, national telephone traffic by fibre optic Internet grew 6.5%, much less than the increases seen in recent years as the network was rolled out and substituted ADSL. In contrast, international traffic via fibre optic Internet and national mobile Internet traffic continue to rise (62.7% and 44.2%).

A series of operators have decided to include Andorra as another EU country and not charge roaming since the entry into force in June 2017 of the new EU policy banning surcharges imposed by companies when clients used their mobiles in other EU countries. Andorra Telecom is also offering advantages to reduce the cost of roaming for its clients when they travel in Europe and the USA.

Timeline of the most significant economic developments in 2017

January

- 1 January, the Agreement on the automatic exchange of tax information, signed with the EU, enters into force.
- 1 January, Law 19/2016 on the automatic exchange of tax information enters into force.
- 1 January, the International Financial Reporting Standards (IFRS-EU) enter into force, applicable to entities operating in the Andorran financial system and collective investment schemes under Andorran law.
- 1 January, the Double Taxation Agreement (DTA) with Luxembourg becomes applicable.
- 1 January, the Double Taxation Agreement (DTA) with Liechtenstein becomes applicable.
- 27 January, the S&P rating is published: Standard & Poor's ratings agency confirms Andorra's ratings as BBB-/A-3 and maintains the stable outlook.
- The Mountain Skiing World Cup is held in Andorra.

February

- The national budget for 2017 is approved (Law 3/2017, of 9 February).
- 22 February, Arcalis mini-hydroelectric power station starts operating.
- 23 February, the first national Combined Heat and Power plant is inaugurated in Soldeu, having started operating on 1 December 2016.
- 24 February, the Fitch rating is published: the international agency, Fitch Ratings, maintains Andorra's BBB rating and raises the outlook from stable to positive.

March

- 7 March, Andorra Telecom starts to renew the active fibre optic network, enabling an increase in the universal bandwidth to 300 Mbps, triple the existing speed.
- The Andorran Council for Trade Competitiveness is created, a public and private partnership for promoting and coordinating execution of the actions proposed in the strategic Plan on Shopping Tourism.
- 16 March, the Carmen Thyssen Andorra Museum is inaugurated.
- 22 March, a long-term public debt issuance (bonds) of 260 million euros is approved, to refinance a previous issuance of the same value.
- 22 March, the Agreement between the Government of the Principality of Andorra and the Government of France is signed, relating to road improvements on the national roads 20, 320 and 22, between Tarascon in the Ariège and the border between France and Andorra.

April

- 23 April, the Paris Agreement on climate change, signed in New York on 22 April 2016, enters into force.
- 23 April, the Double Taxation Agreement (DTA) with Portugal enters into force (applicable on 1 January 2018).

May

- 4 May, the National Coach Station starts operating.
- 10 May, a long-term public debt issuance (bonds) of 60 million euros is approved, to replace an expiring loan policy for the same amount.
- Law 10/2017, of 25 May, on the exchange of information on request and the spontaneous exchange of information for tax purposes is passed.
- It is decided to start winding up Nevasa, the Grandvalira operating company.

June

- 7 June, Andorra signs the OECD multilateral convention to implement international taxation measures (BEPS).
- 8 June, the Agreement on the exchange of tax information with Italy comes into force.
- Law 12/2017, of 22 June, regulating and supervising insurance and reinsurance in the Principality of Andorra is passed (entry into force on 1 January 2018).
- Law 14/2017, of 22 June, on preventing and combatting the laundering of money or securities and terrorist financing is passed.
- The OECD includes Andorra in the list of most co-operative jurisdictions in tax matters: the Global Forum on Transparency and Exchange of Information for Tax Purposes (GF) gives Andorra a provisional rating of "Largely Compliant".
- The Trial World Championship is held.
- The Mountain Bike World Cup is held.

July

- 10 July, the Agreement on international road transport between Andorra and Spain enters into force.
- The classification of tax offence is approved (qualified Law 15/2017, of 13 July, amending qualified Law 9/2005, of 21 February, on the Criminal Code).
- General Law 16/2017, of 13 July, on tourism accommodation is passed.
- On 29 July, the S&P rating is published: Standard & Poor's rating agency raised the long and short-term ratings to BBB/A-2 and maintains the stable Outlook.

August

- 1 August, the Double Taxation Agreement (DTA) with the United Arab Emirates enters into force (applicable from 1 January 2018).
- 7 August, the Agreement between Andorra and the United Arab Emirates on the mutual promotion and protection of investments enters into force.
- 18 August, the Fitch rating is published: the International rating agency Fitch Ratings confirms Andorra's rating as BBB with a positive outlook.
- 21 August, the Vuelta a España cycling race reaches Andorra.

September

- 20 September, a short-term public debt issuance (bonds) of 100 million euros is approved, to refinance a previous issuance of the same value.
- 27 September, the Double Taxation Agreement (DTA) with Malta enters into force (applicable from 1 January 2018).
- 28 September, the Moneyval plenary approves the 5th round evaluation report of Andorra.
- Andorra Telecom obtains capital gains of 16.2 million euros by selling 66% of its shares in the Spanish operator MásMóvil.

October

- 9 October, the Agreement between the Andorran Government and the Italian Government on the regulation of international road transport of passengers and goods enters into force.
- Law 17/2017, of 20 October, on the tax system for restructuring businesses is passed (amended by Law 21/2017 of 23 November).
- Qualified Law 18/2017, of 20 October, on transfers to the local Comú governments is passed (entry into force on 1 January 2018). On 14 March 2018, the Constitutional Court issues a judgement declaring unconstitutional a part of the criteria for distributing transfers to the Comú governments.
- Qualified Law 19/2017, of 20 October, on amendment of the qualified Law delimiting the powers of the Comú governments, is passed.
- The first Andorran Financial Summit is held.

November

- 15 November, a long-term public debt issuance (bonds) of 100 million euros is approved, to refinance a previous issuance of the same amount.
- Andorra Telecom becomes a controlling shareholder of Avatel Telecom, purchasing 37.3% of the company shares for 16.5 million euros.
- 30 November, Laws 29/2017 and 30/2017 amending Law 19/2016 on the automatic exchange of tax information are passed. These laws expand the list of states with which information will be exchanged automatically from 2018 and 2019.
- Law 28/2017, of 30 November, on the 2018-2021 Statistics Plan is passed.

December

- Ecofin recognises the advances made by Andorra towards transparency and cooperation in tax matters and does not include Andorra in the list of non-cooperative countries.
- Andorra Telecom sells its last block of shares in MásMóvil.

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D'ANDORRA