

Spain

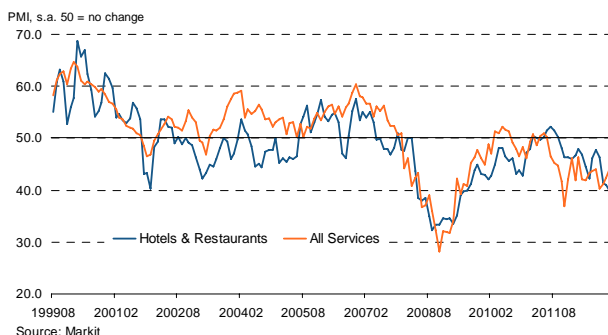
Activity at Hotels & Restaurants in Spain falls sharply after VAT rise

- **VAT rise hits demand in Hotels & Restaurants sector**
- **Activity falling at fastest pace since mid-2009**

In September 2012, Spain increased its headline rate of VAT from 18% to 21% to help reduce the budget deficit. The reduced rate of VAT eligible on certain items was also increased from 8% to 10%. Importantly, some reclassifications also took place meaning that some goods and services that had previously been eligible for the reduced rate were moved to the general rate. Effectively this led to a rise in VAT from 8% to 21% on these items. A number of the areas reclassified were part of the Hotels & Restaurants sector, and the early signs are that the increase has had a strong negative impact on already fragile demand in this part of the economy.

PMI data for the Spanish service sector as a whole signalled an eighteenth successive reduction in activity during December. The rate of decline remained marked, despite easing to the weakest since March 2012. Meanwhile, the Hotels & Restaurants sector posted a substantial contraction in activity, deteriorating at the sharpest rate since mid-2009.

Hotels & Restaurants PMI v All Services



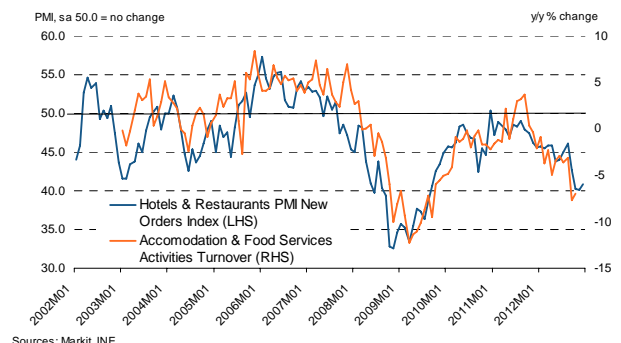
The activity index for the Hotels & Restaurants sector has been below the equivalent for the Spanish service sector as a whole in the past two months, having outperformed it during much of the first three-quarters of 2012. In fact, the sector had been the best

performing of all the broad categories covered by the PMI data in the third quarter of the year.

In the months following the rise in VAT, anecdotal evidence from PMI survey contributors indicated that the tax increase had hit demand. This is likely to have been more keenly felt in sectors such as Hotels & Restaurants, where the reclassification led to a sharper rise in the tax rate than the three percentage point increase in the general rate. Moreover, business sentiment in the sector has been negative in six successive months since the rise in VAT was announced in July.

Official data from the Instituto Nacional de Estadística (INE) for the 'Accommodation and Food Services Activities' sector has likewise started to point to falling turnover, with the rate of decline accelerating following the VAT changes. In the year to August 2012, turnover decreased -3.1%. Then after the rise in VAT the reductions have strengthened to -7.6% in September and -7.0% in October. The PMI New Orders Index suggests that further steep declines are likely at the end of 2012, with rates of contraction broadly stable between October and December.

Hotels & Restaurants Turnover



The deepening of the contraction in this area of the economy makes it even less likely that Spain will see a recovery in the early part of 2013.

Spanish services PMI data are released on the third working day of each month. For more information please contact economics@markit.com.

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