

Spanish Economic and Financial Outlook

Spanish banks: Improved performance in the face of financial turbulence

2016

Volume 5 ♦ Number 2

March 2016



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Electronic edition

An electronic edition of this journal its available at
<http://www.funcas.es/Publicaciones/Index.aspx?Id=47&ddg=0>

Printed in Spain

Editorial and Production

Funcas
Caballero de Gracia, 28. 28013 Madrid (Spain)

Ownership and Copyright:

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ISSN print edition 2254-3899

ISSN electronic edition 2254-3880

Depósito Legal: M-10678-2012

Prints: Cecabank.

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Letter from the Editors

Although financial market tensions have eased since the start of the year, doubts remain about the situation in China and other emerging markets, as well as a possibility of a new global recession. In response to financial market volatility, falling oil prices, and the deteriorating outlook for the global economy, in its latest monetary policy meeting on March 10th, the ECB announced a larger than expected stimulus package, which included interest rate cuts and an expansion of its quantitative easing asset-buying program. Market reactions to the initial announcement were positive, but Draghi's comments that interest rates probably would not fall any further amid concerns over the impact for European banks raised concerns over the possible limits of ECB policy.

In this context, the March SEFO takes a detailed look at the role of the ECB during the latest crisis and post-crisis period, together with the additional actions that will be needed from European institutions to construct a more united and resilient Europe. The ECB has been critical to Europe's emergence from the crisis. In addition to consolidating its traditional role of guaranteeing price stability, it took on new tasks, such as guaranteeing financial stability and banking supervision. But the ECB cannot act alone to secure the integrity of the European project. This will require further strengthening of European institutions. In the immediate future, the objective will be the completion of banking union. Over the longer term, progress on

fiscal and political union will also need to be considered.

We then assess the economic outlook for Spain over the short and medium term, as well as present considerations on how to improve longer term growth perspectives. After growing at a rate of 3.2% in 2015, the impact of the one-off factors that stimulated growth last year is wearing off. This, together with worsening global economic conditions, at least in 2016, has led us to expect slower GDP growth in Spain this year and next, 2.7% and 2.3%, respectively. On the fiscal front, the 2015 deficit target of 4.2% will be surpassed. For the economy as a whole, downside risks are considerable, deriving from the possibility of renewed tensions in financial markets and the possible negative impact of prolonged domestic political uncertainty on investment and employment decisions.

While Spain's economic recovery currently outperforms that of the EU, restoring growth potential and modernising the Spanish economy remain key objectives. Increasing competitive advantage of sectors towards a knowledge-based economy will require building up technological and human capital, creating the right incentives for entrepreneurship, and improving institutional quality and social inclusion. Taking advantage of attractive investment opportunities for infrastructure projects and SMEs arising from the recent creation of the European Fund for Strategic Investments (EFSI), or the Juncker plan, should form a part of

Spain's efforts to change its productive model and foster sustained job creation in the wake of the crisis.

Our financial sector analysis starts off with a broad snapshot of the key challenges for banks' operating climate and their implications for banks in general and, in particular, in the case of Spain. A prolonged period of low (in some cases zero or negative) interest rates, pressing regulation mainly based on higher capital requirements and technology-related disruptive change are the main actual and forthcoming challenges for the banking industry. In Spain, low interest rates pose a more intense threat, given Spanish banks' high degree of reliance on the traditional banking model. Increased capital requirements, however, appear to be more manageable for most Spanish banks, which have improved their levels of capitalisation and typically have lower risk profiles. Both global and Spanish banks' adaptation strategies in response to these challenges will likely forge a new industry structure and financial innovation technologies should be an important part of it.

Focusing in greater detail on Spanish banks, despite the financial market turbulence in early 2016, they have increased their profitability and solvency. Joint profits of the six largest Spanish banks increased in 2015 by 8.1% relative to the previous year. Solvency has improved – banks' fully-loaded core tier 1 capital (CET1) ratio rose from 10.9% in 2014 to 12.2% in 2015. Private sector credit growth is expected to return to positive figures in 2016. Finally, Spanish banks may benefit in the medium-term relative to their peers elsewhere thanks to the enhanced transparency exercises

undertaken. Nevertheless, as we stated previously, the outlook remains challenging.

For example, we examine the effects of a potential new challenge - the inclusion of government debt within banks' risk-weighted assets, in the leverage ratio and in the large exposure limit, which all represent alternatives currently forming part of the EU regulatory debate. The significant weight of government debt on banks' balance sheets in several European countries, including Spain, has been fuelling ongoing debate about the regulatory treatment of these bond holdings. A reduction in sovereign bond holdings could weaken the link between banks and sovereigns and free up funds for private sector lending. However, penalising these holdings would also reduce banks' ability to stabilise the sovereign bond markets and could exacerbate financial fragmentation in the event of stress in the EMU. Banks' returns are currently being eroded by increased regulatory requirements and negative rates. Before introducing limits or haircuts on sovereign bond holdings, it might be advisable to make progress on banking union to prevent further erosion of banks' profitability from causing financial stability issues.

Finally, we look at progress on two areas related to the financial sector restructuring process: regional concentration of the Spanish banking sector and clean-up of bank exposure to the real-estate market. The deep restructuring of the Spanish banking sector has led to significant branch reduction, largely as a consequence of mergers within the sector. In parallel, there has been a notable increase in market concentration – now much higher than

the European average. Concentration varies greatly across the provinces, although increasing substantially during the crisis and almost across all of Spain. The increase in concentration has been so intense that in some provinces it may warrant assessment of potential implications for competition.

Various property market indicators point to a recovery in 2015, although below pre-crisis levels – in line with the correction of the sector's imbalances. As in the case of the Spanish economy's overall recovery, the property sector's future remains highly sensitive to global and domestic conditions. The recovery of the Spanish economy in 2015 allowed the financial sector to significantly reduce its volume of troubled assets, although the reduction needs to factor into account the transfer of assets to SAREB. A closer look reveals that the reduction in troubled assets has been due to the fall of NPLs, whereas progress on reducing foreclosed assets has been going very slowly, with the net effect being an accumulation on financial institutions' balance sheets. As regards SAREB, latest data reveal a significant reduction in its portfolio of financial assets; however, the value of its real-estate assets has remained largely unchanged since the initial transfer.

The ECB and banking union: Towards a more integrated and resilient Europe

José Manuel González-Páramo¹

Europe's recovery from the recent crisis is largely attributable to the role played by the ECB and the support of European authorities in creating the banking union. Despite noteworthy progress, further strengthening of Europe's institutional and legal framework is necessary to construct a more united and resilient Europe to face future challenges.

The recent crisis proved a formidable challenge for EU political and economic institutions. One of the European institutions critical to Europe's emergence from this crisis was the ECB, which, in addition to consolidating its traditional role as the guarantor of price stability, also took on new responsibilities. During the crisis and post crisis period, the ECB's tasks included defence of euro integrity, reliance on non-conventional monetary policy measures and a new mandate for banking supervision. Despite this broader role for the ECB, it cannot act alone to secure the integrity of the European project. This will require further strengthening of European institutions. One of the preliminary ways in which this institutional strengthening is being achieved is through progress on the banking union. In the immediate future, to complete banking union, additional steps will need to be taken to create a Single Deposit Guarantee Scheme (SDGS) and common public backstop under the Single Resolution Fund (SRF). Over the longer term, review of treaties and necessary transfer of sovereignty to make progress on fiscal and political union will also need to be considered as steps to deepen European integration.

The length and depth of the economic and financial crisis in Europe literally put our economic and political institutions at risk, forcing them to make decisions and take steps into uncharted territory. In insolation, any of the shocks to which the euro area has been subject in recent years – the banking crisis, sovereign debt crisis, risk of break-up of the euro, and finally, risk of deflation – would on its own have been destabilising. But the situation was compounded by Europe's

institutional architecture being too weak to adequately address all these risks. What is more, the lack of predictable and harmonised rules for crisis management led to a growing fragmentation in financial markets, such that banks' cost of funding came to depend to a large extent on the strength of their home country, thus reinforcing the vicious circle between banks and sovereign debt. The evolution and overlap of these shocks, in conjunction with the weakness of institutional

¹ BBVA Research. Note that this article was written in January 2016 and therefore the text does not reflect recent developments which took place in February and March.

architecture, proved to be a veritable stress test for the European authorities.

This 'perfect storm' was weathered successfully thanks to the role played by the European Central Bank during the crisis, and the institutional stimulus European authorities gave to building a genuine banking union. This article analyses the main successes achieved by Europe's institutions and the challenges to be addressed in the months ahead in the European institutional context in order to build a more integrated and resilient Europe.

The ECB's role during the crisis and future challenges

During the crisis, the European Central Bank (ECB) has consolidated its traditional monetary role as the guarantor of price stability, while it has also been able to take on new responsibilities as the guarantor of financial stability and as a banking supervisor.

Going forward, in the monetary policy arena, the big question is whether the ECB will manage to bring inflation to its target zone of 2% in 2017. The ECB, which has relied on non-conventional policy tools to confront the crisis, now needs to determine whether these measures are to become a permanent part of the 'typical' arsenal in the future. What is more, the key role it has played in preservation of the euro may turn against the ECB as long as its excessive risk-taking is seen as a sign of partiality or if future crises can be attributed to its intervention over this period. The solution is to advance towards a more integrated Europe characterised by greater solidarity.

The ECB: A controversial but necessary role in defending the integrity of the euro

Last autumn, Mario Draghi completed his first four years at the head of the ECB. He took over in the midst of the international financial crisis and had

to face a string of idiosyncratic shocks affecting the euro area. In addition to the banking crisis, there was the debt crisis, and the risk of the break-up of the euro, followed by the risk of deflation. Hopefully the second half of his mandate will be less challenging. But before looking to the future, it is worth exploring and taking a look back at the role played by the euro area's central bank.

In 2011, the ECB had to become actively involved in financial bail-out programmes for Ireland, Portugal and Greece. Its participation in the so-called 'Troika', along with the International Monetary Fund and the European Commission, gave it the credibility it needed at the time. Some people considered playing this key role to be overstepping its power, jeopardising the independence of its monetary policy mandate, and the financial stability of the euro area. As we shall see, the implementation of the European Stability Mechanism (ESM) is an important achievement, and the ESM has become established as a central instrument for the management of future crises.

Maintaining the liquidity of Greece's banks via an emergency credit line while fears of a Greek exit from the euro were rife was also controversial. Following the principles established by W. Bagehot almost 150 years ago (Bagehot, 1873), the ECB took decisive action to provide liquidity to prevent a systemic crisis (allotment of liquidity to meet all demand, relaxing collateral policy, extending repayment periods for refinancing transactions, and providing emergency liquidity), always rigorously applying the relevant rules. This entails supplying liquidity to solvent banks in return for adequate collateral, mitigating both unnecessary exposures on its balance sheet and the problem of moral hazard.

The way in which this liquidity is provided includes refinancing operations, known by their initials LTROs and TLTROs. LTROs (long-term refinancing operations) are part of the ECB's open market operations, and are long term. Their maturities, initially three months, have been extended to three years in successive bouts of

the crisis. Considerable use was made of these modes of financing in the three-year auctions in December 2011 and February 2012, when a total of over a billion euros was applied for. Moreover, in June 2014, the ECB approved a new series of eight long-term financing operations, referred to as targeted longer term refinancing operations (TLTROs), with the specific aim of stimulating lending to the private sector in the euro area (excluding loans for home purchases). TLTRO² loans have maturities of four years (until September 2018), provided the banks comply with the predetermined criteria, namely demonstrating that credit has performed better than the benchmark defined by the ECB. If not, banks will have to repay the loans in September 2016. So far, six of the eight scheduled operations have taken place, with 418 billion euros being applied for. The volume of applications in these auctions was significantly less than originally estimated, particularly in the most recent auctions, given the excess liquidity in the system.

In parallel, following the outbreak of the financial crisis, the ECB adopted a fixed-rate full allotment procedure for all financing operations (this procedure has been extended until December 2017).

Once the ECB had ensured the financial system's liquidity needs had been met, in August and September 2012³ it launched its outright monetary transaction (OMT) programme. This was designed to safeguard the integrity of the euro and to transmit monetary policy in the single currency area. The programme allows the ECB to buy unlimited amounts of sovereign debt issued by countries in the euro area over a period of one and three years, provided strict conditions are met by beneficiary countries, so as to solve the 'moral hazard' problem. The announcement of this programme was a complete success, as it showed itself to be fully effective at eliminating

the risk of the euro's break-up, even before being brought into action. This success is due to two particular features of the programme: unlimited liquidity and the ECB's *pari passu* –rather than its previous preferential creditor– status. The programme faced a legal challenge from the German constitutional court, forcing the European Court of Justice (ECJ) to rule on its legality. In June 2015, the ECJ ruled that the programme is compatible with European Union law as the ECB has not exceeded its authority regarding monetary policy and the programme does not infringe the bar on offering monetary finance to Member States.⁴

The ECB vis-à-vis non-conventional monetary policy

In its more traditional monetary policy and price stability role, the ECB is using all the instruments available to it to enable inflation to converge to its 2% target. In 2014, and in 2015, in particular, it became clear that this objective was at risk. The conventional measures adopted up to that point had proven insufficient, mainly as a result of sluggish growth and the slump in the oil price. Raising inflation has become a critical issue, given the current context of high debt and risks to growth against a backdrop of persistently low inflation.

In this context, in September 2014, the ECB launched an asset purchase programme (APP), which initially included only private assets, but was expanded in January 2015 to include public debt issued by central governments and agencies and European institutions in the euro area.⁵ The programme set a monthly target of 60 billion euros until at least March 2017 (following an extension to its duration, which was originally until September 2016 and pending a decision of the monetary policy meeting in March, where it

² July, 3rd, 2014, https://www.ecb.europa.eu/press/pr/date/2014/html/pr140703_2.en.html

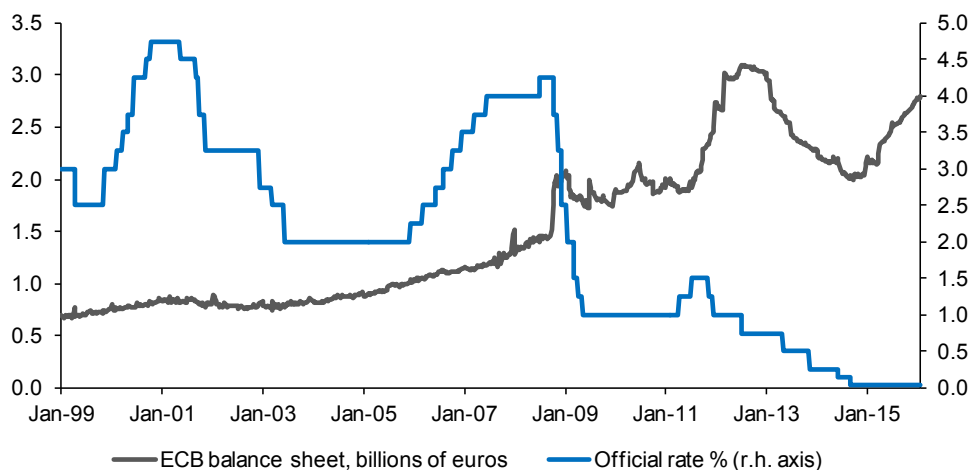
³ *Technical features of OMT* (September 6th, 2012). http://www.ecb.europa.eu/press/pr/date/2012/html/pr120906_1.en.html

⁴ In any event, the German constitutional court will have the last word, and on February 16th, there will be another session on OMT.

⁵ *Asset purchase programme* 22/01/2015 https://www.ecb.europa.eu/press/pr/date/2015/html/pr150122_1.es.html

Exhibit 1

European Central Bank balance sheet and official intervention rate



Source: ECB.

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is possible that it will be extended again). As a result, the size of the ECB's balance sheet has increased significantly (Exhibit 1), becoming an effective monetary stimulus tool in an environment where interest rates have reached zero.⁶

Another of the measures used by the ECB has been to cut the official interest rate to a record low of 0.05% and to move the deposit facility rate into negative territory, for the first time ever, where it is currently at -0.30%.

The route has not been easy. The ECB has faced criticism and even legal challenges to some of its decisions as regards the application of these measures. However, in hindsight and after intense discussions of recent years, facing these challenges has helped dispel some of the misunderstanding about the meaning and limits of the ECB's mandate. This has confirmed the independence of the Governing Council's

decision-making from the political viewpoints of Member States.

New times call for new approaches, and the ECB is proving itself to be especially pragmatic in this respect. The crisis has revealed that the capacity of central banks is not exhausted when interest rates reach zero. The available arsenal is broad, and the ECB will remain immersed in a context of non-conventional policies for some considerable time to come.

The current macroeconomic environment represents a change of monetary policy paradigm from previous stages of the ECB's existence. New times call for new approaches, and the ECB

⁶ The ECB estimates that the non-standard measures adopted since the summer of 2014 have produced a net effect equivalent to an interest rate cut of 100 basis points (under normal conditions). <https://www.ecb.europa.eu/press/key/date/2016/html/sp160204.en.html>

is proving itself to be especially pragmatic in this respect. The crisis has shown that the capacity of central banks is not exhausted when interest rates reach zero. The available arsenal is considerable.

Looking to the future, as stated above, the ECB has relied on non-conventional policy tools to confront the crisis and needs to decide whether these measures are to become permanent options. This is a fascinating debate, and one that affects not only the ECB but many other central banks that have drawn upon this new arsenal of monetary policy measures during the crisis. The ECB will rely on non-conventional policies for a considerable time, such that it is still too early to start thinking about an exit strategy.

Banking supervision: A new ECB mandate

Together with the foregoing, the ECB has also taken on a new and important responsibility in the form of single banking supervision for the euro area, better known as the Single Supervisory Mechanism (SSM). In early 2016, the SSM was already fully operational and has had many achievements. In little more than a year (the SSM came into effect in November 2014) it has developed its supervision methodology, obtained the necessary resources to implement it (around

a thousand staff in Frankfurt), and has become a key player in the global financial system, being one of the world's biggest supervisors in terms of assets under supervision.

These achievements, in such a short period of time, are due not only to the efforts made in Frankfurt, but also to the work of national authorities, which, it should not be forgotten, are part of the SSM alongside the ECB. Indeed, it is the national authorities that have the knowledge of entities' strengths and risks, which is a key factor in this first stage.

The SSM's new supervision methodology seeks to obtain a broad view of entities, beyond the content of their financial reports, in relation to four pillars: internal governance, risk management, business model, and capital and liquidity analysis.

The entry into force of the SSM has also affected entities' day-to-day operations. The SSM's key tool for its functions is the new supervision methodology, known as SREP (Supervisory Review and Evaluation Process). This methodology is a holistic and forward-looking process in which the supervisor aims to obtain a

Exhibit 2

The four pillars of SREP



Source: SSM and author's own elaboration.

broad view of the institution beyond the content of financial reports, although these remain extremely important. Rather than being a mechanical and purely quantitative process, it is understood as taking into account an analysis of qualitative aspects of the entity that require the supervisor maintain a constant dialogue with it. Specifically, the four pillars on which the SREP rests are: i) internal governance and risk management; ii) business model analysis; iii) capital; and iv) liquidity.

■ The first pillar involves, among other things, an exhaustive assessment of the entity's organisational structure, verifying that the decision-making processes are appropriate and that the members of the board of directors meet the requirements for them to carry out their duties. This aspect has always had particular significance for the SSM, where there is a clear commitment to international best practices. However, there are divergences between entities' models of corporate governance across the euro area. For example, two-level boards, in which there is a supervisory board concentrating on overseeing the management team, is a widespread structure in some countries such as Germany or the Netherlands, but is not found in other countries such as Spain or France. It must of course be recognised that no particular model of governance is intrinsically superior. The supervisor therefore has to know and monitor the weaknesses of each and enhance its strengths.

■ Analysis of the business model, the second pillar of SREP, assesses the ability to generate profits over twelve months (viability) and three years (sustainability). This is one of the aspects where it is less clear how SSM will carry out its analysis. As in the case of corporate governance structures, in the euro area there are almost as many different business models as entities, with no model necessarily being economically superior. On this point, the challenge is to evaluate whether entities are able to remain profitable in an environment

as difficult as today's. Moreover, the aim is to analyse an entity's capacity to generate profits over the whole cycle, as well as in the short and medium term. This is conceptually simple, but there are uncertainties regarding its practical implementation.

Although banks' profitability improved slightly in 2015, many entities have levels of return on equity below their cost of capital, casting doubts on the medium- and long-term viability of their business.

This low profitability is due to both structural and temporary factors: i) sluggish economic growth, leading to slow credit growth; ii) persistently low interest rates; iii) an excess of unproductive assets (from defaults or foreclosures) in some European financial systems, which puts a brake on future business; iv) new regulatory requirements on capital, liquidity and leverage, among others; and v) the effects of the digital transformation on the banking sector. This is all forcing banks to rethink their strategy. Identifying which businesses can generate recurrent revenues in excess of the cost of capital and which cannot is one of the key challenges for entities' managers and supervisors.

■ The last two pillars – liquidity risk and capital – look at factors such as credit risk, market risk and funding risk. There are still divergences in these areas in terms of the implementation of the regulation across countries, such that it is not possible to talk of complete uniformity or comparability. However, the European authorities are working actively on this and laying the foundations for convergence within a reasonable time frame.

On the last two pillars, the supervisor encourages entities to undertake a self-assessment of their liquidity and capital risks. This self-assessment is known as ICAAP (Internal Capital Adequacy Assessment Process) and ILAAP (Internal Liquidity Adequacy Assessment Process). In both cases, the supervisor tries to analyse

the robustness of entities' capital and liquidity under stress scenarios as well as under normal circumstances.

This first supervision exercise under the SSM, which was preceded by a review of the quality of banks' assets and a first stress test, was rated very positively. Evidence of this is the euro area's resilience in the face of the Greek crisis in the summer of 2015. As Rome was not built in a day, the SSM could not be built in a year. Three factors stand out among the main challenges for the next few years: i) harmonisation of regulations and supervisory practices, an issue on which, with the national options and discretionalities project, progress is on the right track; ii) viability of business models; and iii) greater European and international cooperation, and perhaps the transparency with which supervision is exercised and the dialogue between supervisors and institutions should be strengthened. There has been a marked improvement on this point, as highlighted by the recent publication of the SSM's supervisory priorities for 2016.

However, the significance of the ECB's new role goes beyond addressing these three challenges. Its real importance lies in its capacity to achieve two objectives: rebuilding confidence in the banking system and undoing the fragmentation of the financial system.

Going forward the ECB alone is not enough

The exceptional role of the ECB during the crisis needs to be understood in the context prevailing during this unique period. The key role it has played in holding the euro together may ultimately have negative implications if the excessive risks taken are seen as a sign of partiality in application of monetary policy, or if, justifiably or not, the ECB is held responsible for future crises, damaging its credibility.

What path should be taken to strengthen the role of each of the European institutions? As mentioned, the ECB cannot remain the main pillar in the fight against crises in Europe indefinitely. Other European authorities have to assume their responsibilities, through a dual strategy of developing a harmonised legal framework and strengthening the institutional framework with closer

The ECB cannot remain the main pillar in the fight against crises in Europe indefinitely. Other European authorities have to assume their responsibilities, through a dual strategy of developing a harmonised legal framework and strengthening the institutional framework, with closer integration and new transfers of sovereignty to supranational authorities.

integration and new transfers of sovereignty to supranational authorities. The "Five Presidents' Report" (discussed in more detail below) lays the foundations for the European institutional framework and is the ideal complement to the ECB.

Banking union and the "Five Presidents' Report"

Banking union emerged as a quantum leap for the monetary union, a major stride towards financial integration and towards the completion of the construction of the euro. The progress so far on achieving banking union has been tremendous, indeed inconceivable just a few years ago. In fact, it represents a significant transfer of sovereignty from those countries sharing the common currency to the new supranational authorities, with a large component of solidarity from the public sector, to an extent unprecedented since the birth of the euro.

Banking union is a forward-looking project and therefore designed not to resolve the problems of the past but to avoid and address the problems that

may arise in the future. Banking union has come a long way, but its successful implementation so far should not lead to complacency, as the future challenges are far from trivial.

Successfully completing it along the lines set out in the road map known as the *“Five Presidents’ Report”* is now even more necessary than ever in order to continue making progress on building genuine monetary, economic and political union.

Banking union is a first step on the way to addressing the challenges of the future

The first step towards the constitution of the European institutional framework after the crisis was taken in late 2012 with the report *“Towards a Genuine Economic and Monetary Union”*,⁷ the final version of which was approved by the European Council in December of that year. This document, which was referred to informally as the *“Four Presidents’ Report”*, was directed by the president of the European Council, Herman Van Rompuy, in collaboration with the presidents of the ECB, the European Commission and the Eurogroup. Van Rompuy presented a first view of the profound institutional reform Europe needed to undertake in June 2012 in an attempt to calm the markets by signalling European Union leaders’ firm determination to move towards a more united Europe.

The report proposed the creation of a banking union, fiscal union, and economic union, so as to develop a stronger and more integrated Europe as a means of overcoming the crisis. The strategy, which was approved in December, proposed a path towards banking union to achieve three goals: (i) increasing the strength and resilience of the EU’s banks through enhanced prudential and supervisory requirements; (ii) reducing the cost of bank failures by providing an effective resolution

framework that seeks to avoid bank bail-outs and enhance deposit protection; and (iii) reducing the fragmentation of financial markets in Europe by breaking the vicious circle between banks and sovereign debt by centralising decisions and responsibilities in new supranational institutions, and by establishing a genuinely European network of solidarity such that participating banks will come to share risks.

Banking union has three main components. The first is the development of a new harmonised regulatory framework applicable to all financial institutions operating in the European Union (the Single Rule Book). The regulatory areas in which harmonisation of legislative frameworks is being pursued are:

- *Common regulations to strengthen capital and liquidity requirements* (known as CRR/CRD IV).⁸ These regulations implement new global standards on bank capital laid down by the Basel Committee on Banking Supervision (Basel III) in the European Union’s legal framework. The new banking legislation strengthened the capital requirements, demanding more and better quality capital, and included regulations on liquidity and leverage in order to reduce the likelihood of bank failures. The CRR/CRD IV package came into force in January 2014 (including the Directive’s implementation in national legislation) and can now be said to be fully in place and taken on board by financial institutions and the market.
- *Common regulations to address financial difficulties while minimising recourse to taxpayers’ money* (known as BRRD).⁹ BRRD establishes a series of common rules applicable to all European Union countries to address the resolution of banking groups facing capital or liquidity problems, minimising the cost to taxpayers and safeguarding the

⁷ http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ec/134069.pdf

⁸ CRD4-Capital Requirement Directive (Directive 2013/36/EU) and CRR-Capital Requirement Regulation (Regulation 575/2013).

⁹ BRRD-Bank Recovery and Resolution Directive (Directive 2014/59/UE).

critical operations the entity may perform. A key plank of the new regulations is that the cost of recapitalising an entity will fall mainly on private creditors through what is termed a 'bail-in', rather than on taxpayers. The principle of "more bail-in and less bail-out" undoubtedly helps break the sovereign/banking sector linkage.¹⁰ It is worth noting that the BRRD entails significant institutional change. It creates a new resolution authority with extensive powers of intervention in entities both during resolution processes and when establishing preventive measures (e.g. resolution plans) facilitating a potential future resolution. The BRRD was phased in gradually over the course of 2015 (it came into effect in Spain on June 18th, 2015, with Law 11/2015).

- *A new version of the Directive on deposit guarantee schemes* (known as DGSD),¹¹ aiming to harmonise financing and coverage of deposit guarantee schemes throughout the European Union, which came into force in July 2015. Under this Directive, bank deposits from all banks operating in the European Union are guaranteed up to a maximum of 100,000 euros per customer and bank in the event of a bankruptcy. One of the main points addressed by the Directive is how guarantee schemes are to be financed. In general, deposit guarantee schemes will be financed with *ex ante* contributions from financial institutions determined according to their size and risk profile. If *ex ante* contributions prove insufficient, the fund will collect *ex post* contributions from the banks, and in the last resort option, it will draw upon alternative financing mechanisms such as public loans, loans from deposit guarantee schemes in other Member States or private loans from third parties. Finally, it should be noted that the harmonisation of the rules on deposit guarantees does not include the creation of a single guarantee scheme for the euro area. As

will be discussed in more detail below, this is an issue that will need to be addressed in the years ahead.

The second pillar of banking union is the Single Supervisory Mechanism (SSM). The SSM changes the rules of the game for banking supervision, entailing the creation of a centralised system of European supervision that encompasses both the ECB and the national supervisory authorities in the countries of the euro area. The ECB will directly supervise 'significant credit institutions' and will work very closely with national supervisory authorities to supervise the other credit institutions. It can take over responsibility for a less significant bank if necessary to ensure the overall functioning of the SSM. Creation of the SSM is the complement to monetary union and a common legislative framework that ensures homogeneous interpretation and application of supervisory practices across the EMU.

And finally, the third pillar of banking union is the Single Resolution Mechanism (SRM). The SRM therefore comprises a new centralised decision-making system on banking resolution throughout the euro area comprising the National Resolution Authorities (NRAs), a new Single Resolution Authority, a Single Resolution Fund and a single set of rules for resolution (in line with the framework for the management of the crisis defined in the BRRD).

Banking union represents the biggest transfer of sovereignty in Europe since the creation of the euro.

The Single Resolution Authority, which has been fully operational since January 1st, 2016, will apply the resolution rules determined in the BRRD uniformly to entities located in the euro area.

¹⁰ Proof of this is that the rating agencies are changing their risk assessment methodologies to eliminate sovereign support from financial institutions' ratings. This change in rating methodologies meant the loss of 1 or 2 levels in the ratings of the main European financial institutions in 2015.

¹¹ DGSD-Deposit Guarantee Scheme Directive (Directive 2014/49/EU).

This new Brussels-based authority can impose preventive measures to minimise the impact of an institution's resolution. But, perhaps its most important role is during resolution itself. The Single Resolution Fund may be drawn upon up to a limit of 5% of the total liabilities of the institution being resolved in cases where the bank's private resources are insufficient to cover the cost of the resolution process, and once private creditors have assumed losses of at least 8% of the institution's total liabilities. The Single Resolution Fund is one of the major innovations of this third pillar. It will be financed by European banks and is due to reach its general target level of 55 billion euros in 2024. Its financial capacity will be progressively mutualized, starting at 40% at its inception (2016) until it reaches 100% in 2024.

To conclude, banking union represents the biggest transfer of sovereignty in Europe since the creation of the euro. Throughout the process, there has been a strong political will and a sense of urgency at the level of both the European institutions and

Member States. Although complacency at times risked stalling the process, Europe's leaders fortunately managed to reach a consensus on the key issues.

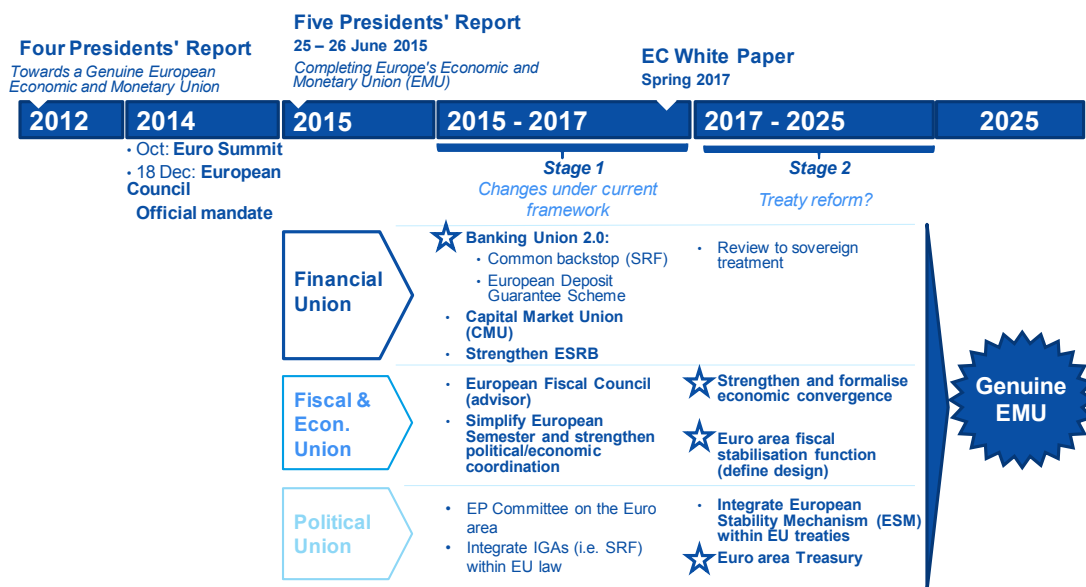
However, Europe's authorities are today aware that a Single Deposit Guarantee Scheme is needed. Starting banking union without this fund was accepted temporarily as a lesser evil in order to get banking union under way in 2015. But banking union will need to be completed in the near future with a Single Deposit Guarantee Scheme and closer economic and political integration.

The European project for the next ten years as a mechanism to confront the challenges of the future

The new step taken by Europe towards greater integration was set out in the report "Completing Europe's Economic and Monetary Union" presented in June 2015, better known as

Exhibit 3

Towards a genuine European Economic and Monetary Union



* ESRB – European Systemic Risk Board, IGAs – Intergovernmental Agreements, SRF – Single Resolution Fund

Source: BBVA Research.

the “Five Presidents’ Report”¹² (the President of the European Commission, Jean-Claude Juncker, the President of the Euro Summit, Donald Tusk, the President of the Eurogroup, Jeroen Dijsselbloem, the President of the European Central Bank, Mario Draghi, and the President of the European Parliament, Martin Schulz).

This new European proposal is half way between ambition and pragmatism. It correctly establishes the need to bolster the euro area’s financial stability by developing new mechanisms of solidarity while ensuring that governments and economic actors behave responsibly. This pragmatism is manifested throughout the types of goals established in two distinct stages. In the first stage, work focuses on ambitious but achievable goals, while in the second stage, it focuses on other more ambitious aims that require a profound rethinking of European and national institutions. Specifically, in the short term, *i.e.* between now and June 2017, the plan seeks to complete banking union by creating a Single Deposit Guarantee Scheme (SDGS) for banks operating in the euro area and a common public backstop for the Single Resolution Fund (SRF).

- Setting up a common deposit guarantee scheme is essential to completing banking union and, thus, making progress towards eliminating the risks of fragmentation associated with the sovereign/banking vicious circle. The proposal presented by the European Commission on November 24th, (European Commission, 2015) is undoubtedly a step in the right direction, establishing different levels of shared responsibility over time. Viewed in isolation, the reinsurance system envisaged for the period up to 2020 in the first phase (referred to as European reinsurance), does not appear to be a major advance on the current system. However, the path embarked upon with what is termed co-insurance or progressive mutualisation as of 2020 will facilitate the transition to the third phase. The path charted by this roadmap ends with full mutualisation or pooling in 2024 with

exclusive use of the SDGS. This will not be easy to achieve, as there is a split within the EU over how fast progress ought to be.

- As regards the public backstop, there has been a lot of discussion about the financial power of the Single Resolution Fund. There are many doubts about how the resolution of an entity will be financed during the Single Resolution Fund’s transitional period, when the existing resources will be limited. Additionally, the fund may be too small in absolute terms in the event of a systemic crisis and widespread bank failures. It is therefore necessary to devise a public backstop that gives credibility to the whole process. One solution would be to assign this role to the ESM (European Stability Mechanism), which was designed to provide support during the sovereign-debt crisis, but which has adequate financial capacity, resources, and governance, along with the authority to directly recapitalise crisis-stricken entities, which seems to fit the bill for the backstop role. However, giving it this role would mean reforming the ESM treaty, a step some countries remain reluctant to take.

The ECB’s role in the current banking and sovereign crisis could be taken on by the ESM or an equivalent body. In this way the ECB would therefore need to limit its participation as

Setting up a Single Deposit Guarantee Scheme is essential to completing banking union and, thus, making progress towards eliminating the risks of fragmentation associated with the sovereign/banking sector linkage. However, it will not be easy to achieve, as there are divisions within the EU regarding the speed at which progress needs to be made.

a guarantor of financial stability to an advisory role, while acting as a provider of liquidity in the last

¹² http://europa.eu/rapid/press-release_IP-15-5240_en.htm

resort, avoiding many of the issues concerning its independence mentioned above.

Over the longer term, from 2017 to June 2025, the unavoidable, but complex, review of the European Union's treaties and the necessary transfer of sovereignty to strengthen fiscal and political union, needs to be considered. Three elements have been highlighted in order to be able to complete the architecture of Europe's Economic and Monetary Union (EMU).

- First, economic union needs to be deepened, which requires closer convergence between countries and strict compliance with the rules already agreed, as well as completion of banking union, as already discussed.
- Secondly, fiscal union between member countries needs to be sped up. This necessitates establishing a macroeconomic stability mechanism for the euro area. The creation of a euro area Treasury would be a positive step towards the coordinated development of common fiscal policies. We need to arrive at a situation in which ever more decisions in the euro area are taken at the supranational level.
- Thirdly, greater democratic participation and parliamentary scrutiny of progress towards political union is needed. An economic government for the euro area, backed by an elected parliament for the euro area, would strengthen accountability and the acceptance of reforms. This requires a bigger transfer of sovereignty from the national to European level, where it will be essential to guarantee that national parliaments are better coordinated and their views are taken into account at the European level. It is essential to formalise a joint decision-making mechanism between national parliaments and the European Parliament.

In mid-2017, the European Commission is due to publish a white paper with a roadmap for the development of this second phase (2017-2025), such that 2016 will be a busy year and a key one in terms of political debate. It is important

that this debate be approached in an inclusive way, by means of a public consultation and with the support of expert groups. Only then will it be possible to guarantee it has the legitimacy and support necessary for the European project to progress successfully.

Concluding remarks

Over the last four years, European political and economic authorities have made considerable strides towards the construction of a more united and resilient Europe that is better able to weather future crises. However, there is still work to be done, and the successes reaped should not lull us into complacency. We need to complete banking union and embark on the path towards fiscal union and political union. In short, the aim is to build on the current euro as it exists today to equip it with a more robust architecture, able to confront the challenges of tomorrow. This is essential in order to be better able to withstand future financial and economic shocks, and to ensure the ECB works optimally by eliminating the constraints on its monetary authority operations – an institutional structure characterised by the segmentation of capital markets and banks, without a single fiscal authority acting as a counterpart.

The recipe has been known since the “Four Presidents’ Report” in 2012. The roadmap the European authorities are due to follow over the coming years was unveiled in the summer of 2015 in the “Five Presidents’ Report”, with the aim of making further progress towards European integration. The plan aims to achieve genuine monetary union within ten years, with a gradual two-stage approach. The first stage, ending in 2017, seeks to complete banking union with the implementation of a Single Deposit Guarantee Scheme in the euro area. And the second, from 2017 to 2025, envisages the unavoidable, but complicated, treaty review to make progress towards fiscal and political union.

At present, European countries express differences in terms of their points of view and levels of ambition, which could be a stumbling block on the road ahead. European leaders need to take a long-term view when addressing these topics, making sure they are sufficiently forward looking. Now, more than ever, there is a need to clarify the extent to which the countries concerned are willing to transfer sovereignty, and how fast they want to move forward on the construction of the Europe we want for the future.

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Spain's economic slowdown in an uncertain context

Ángel Laborda and María Jesús Fernández¹

Fears of a global recession seem unfounded, but a high degree of financial market volatility still represents significant risks for the global economy. In Spain, one-off growth drivers in 2015 are wearing off, compounded by the worsening of global conditions, which is expected to slow GDP growth this year and next, while downside risks remain considerable.

Financial market tensions have eased since the first few weeks of the year, but the global economy's fundamentals remain weak, and the situation is still marked by uncertainty. Fresh bouts of turbulence cannot, therefore, be ruled out. In Spain, lower expected global growth, in conjunction with the progressive exhaustion of one-off factors that drove economic growth in 2015, point towards a slowdown in 2016 and 2017. The downside risks are also considerable, as global uncertainty is coinciding with domestic political obstacles of forming a new government.

International context

Financial market tensions at the start of the year eased in mid-February, even though concerns about the situation in China and other emerging economies, and the fear of another global recession, have not subsided. The worsening global uncertainties have put expectations of further interest rate rises in the U.S. on hold, while raising the prospects of more robust quantitative easing by the European Central Bank. This was ultimately confirmed at the Governing Council's meeting on March 10th, when the ECB decided to cut the interest rate on its main refinancing operations to zero, lower interest on deposit facilities by 10 basis points to -0.40%, and scale up the asset purchase programme to 80 billion euros a month, while extending it to corporate

bonds, and paying financial institutions taking borrowed liquidity under the new targeted longer-term refinancing operations (TLTRO) framework up to 0.4%.

The U.S. economy continued to create jobs at a brisk pace in the first two months of the year, although the progress of certain activity indicators, such as the industrial production index, orders and PMI indices was less positive. In the Eurozone, the poor results obtained on indicators such as the economic sentiment index or the Purchasing Managers' Index (PMI) suggest that the slowdown in the second half of 2015 (with quarter-on-quarter growth of 0.3%) has continued into the start of 2016. However, there are no potentially recessionary signs in any of these economic areas. Moreover, although China's slowdown may

¹ Economics Trend and Statistics Department, Funcas.

have a negative impact on developed economies, in Europe's case, this will be offset by the boost from the lower oil price, although the impact of this on the U.S. economy is less clear cut.

China's slowdown may have a negative impact on developed economies. In Europe's case, this will be offset by the boost from the lower oil price, although the impact of this on the U.S. economy is less clear cut.

Fears of a global recession seem unfounded. Even if the high degree of financial market volatility, that may be associated with monetary policies based on quantitative easing causing asset bubbles, represents a significant risk. Fresh bouts of turbulence cannot therefore be ruled out. These could lead to bankruptcies or balance of payments crises in some emerging countries, and the consequent heightened uncertainty could further weaken the real global economy.

Recent developments in the Spanish economy

Spain's GDP grew by 0.8% in the fourth quarter of 2015, the same rate as in the previous quarter. In annualised terms, this growth was equivalent to 3.2% (all quarter-on-quarter growth rates below will be given in these terms). Growth in year-on-year terms was 3.5%. This result was in line with expectations, given the results of the indicators for the period, although it was higher than in previous forecasts. Over the year as a whole, GDP grew by 3.2% on the previous year.

The rise in all domestic demand components slowed in the fourth quarter, resulting in a 2.3 percentage-point contribution to quarterly growth, compared to 4.8 pp in the previous quarter. Slower growth of domestic demand was compensated for by a larger positive contribution from the external

sector (0.9 pp) after three straight quarters of negative contributions. The change was caused by a sharp slowdown in import growth. Over the year as a whole, domestic demand contributed 3.7 pp, and the external sector -0.5 pp.

Private consumption growth slowed in the fourth quarter to a quarter-on-quarter rate of 3%. Over the year as a whole, this variable rose by 3.1% from the previous year. This growth was mainly driven by employment growth and the increased real disposable income resulting from falling energy prices and tax cuts. With respect to the start of 2016, the indicators available for the month of January, such as retail sales, new vehicle registrations, and sales of consumer goods by large companies, continued to grow without showing any signs of a slowdown. The retail trade confidence indicator for January and February was in line with the results of the last quarter of 2015, although the consumer confidence index fell. This may be partly because of the domestic political uncertainty (Exhibits 1.1 and 1.2).

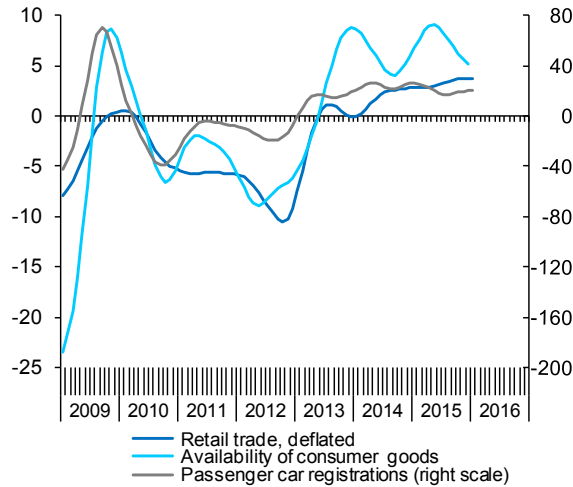
General government consumption grew by 1.7% in the fourth quarter in real terms, but dropped by 3.9% in current prices. Nevertheless, over the year as a whole, this component of demand grew in real terms by 2.7%, with nominal growth of 3.1%. Real growth contrasts with the drop of 1% forecast in the macroeconomic framework accompanying the State Budget for 2015.

Investments in capital goods and other non-construction products moderated its quarterly progress to 6.8%. This makes 12 uninterrupted quarters of positive rates, and, what is more, at an average rate exceeding that seen in the pre-crisis boom years. Nevertheless, its current level is still 3% below the peak reached in the second quarter of 2008. The annual increase in 2015 was 7.5%. This growth is being driven by the recovery in demand, improved financing conditions, and the need to replace and modernise production equipment in the wake of the severe cut in the rate of business investment during the crisis.

Exhibit 1

Consumption and capital goods investment indicators**1.1 - Consumption Indicators (I)**

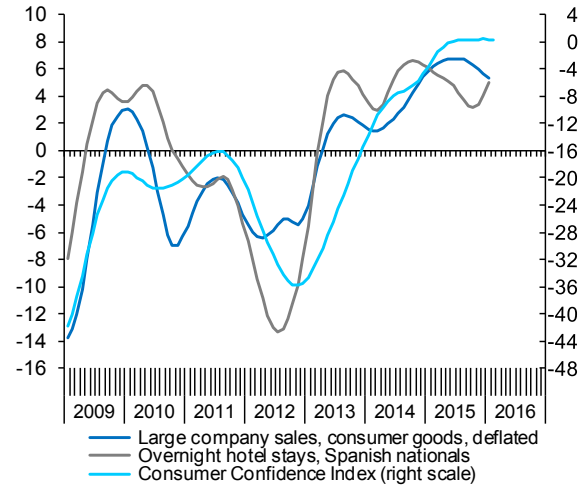
Annualised moving quarterly change in %, smoothed series



Sources: Ministry of Economy, INE, DGT and Funcas.

1.2 - Consumption Indicators (II)

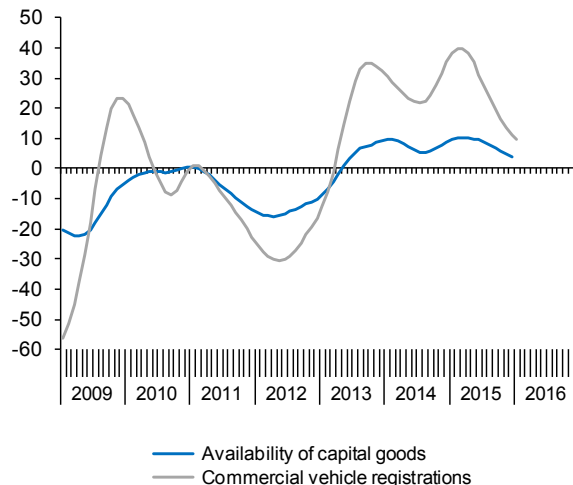
Annualised moving quarterly change in % and index (CCI), smoothed series



Sources: European Commission, INE, AEAT and Funcas.

1.3 - Capital goods GFCF indicators (I)

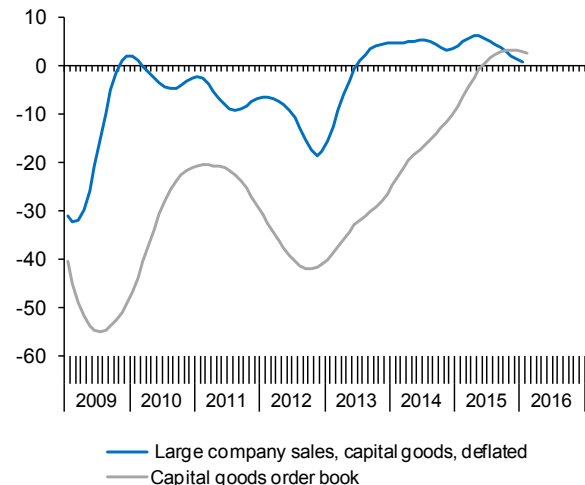
Annualised moving quarterly change in %, smoothed series



Sources: Ministry of Economy, DGT and Funcas.

1.4 - Capital goods GFCF indicators (II)

Annualised moving quarterly change in %, smoothed series



Sources: Ministry of Industry, AEAT and Funcas.

Few indicators are available in this segment of demand for the first quarter of 2016. Registrations of goods vehicles picked up in January, although the overall trend was downward. Large corporations' sales of capital goods also rose

in January after four months of decline, and the index of orders of capital goods in January and February dropped in comparison with the fourth quarter average, although it remains fairly high (Exhibits 1.3 and 1.4).

The quarterly increase in construction investment was 2.5%, which is the slowest rate in the last seven quarters. Both the housing investment component and other constructions registered positive rates. However, housing investment growth failed to live up to the expectations created by the sharp rise in new housing permits and an accelerating trend. In the case of non-residential construction, on the other hand, the slowdown in growth is in line with the reduction in public contracting following the municipal and regional elections (Exhibit 2.6).

Housing sales grew by 11.1% in 2015, according to the INE's statistics, or 7.4% according to the Ministry of Public Works and Transport. However, both sources registered a drop in the number of transactions in the last quarter, which –according to INE data– became more pronounced in January. This result is consistent with the drop in lending for housing purchases in the fourth quarter of 2015 and in January 2016, after two years of increases. It is unlikely that this deterioration in real-estate activities represents a change in trend. It is more likely to be a transitory dip reflecting current uncertainties. In any event, prices are still rising.

There was a reduction in goods imports and exports in the fourth quarter, while trade in services grew. Over the year as a whole, total exports rose by 5.4% and imports by 7.5% in real terms, equivalent to a rise of 5.8% and 5.9%, respectively, in current prices. In other words, lower prices of energy products and other commodities meant that imports grew more in volume terms than nominal terms. Over the year as a whole, the total trade balance turned a surplus of 2.5% of GDP, the same as the previous year, reducing the energy deficit –due to the drop in the oil price– and reducing the non-energy goods surplus.

From a supply-side perspective, all sectors registered positive growth rates in the fourth quarter, although the only sector in which growth accelerated was construction – which is somewhat inconsistent with the slowdown in investment in

housing and other constructions. Over the year as a whole, progress was made in most sectors, particularly construction, with growth of 5.3%, followed by manufacturing, where growth of 3.7% was the best result this sector has seen since 2001.

In January 2016, the industrial production index continued its trend towards deceleration apparent since half way through the previous year, and the industrial climate index worsened in January and February. However, in January and February, the PMI rose to above its level in the last quarter of 2015. The January data for sales of industrial goods by large companies were also positive, while job creation in the sector, according to social security affiliation figures continued to rise at a similar rate to that seen in the final months of 2015 (Exhibits 2.1 and 2.2).

Growth in activity in services weakened in the first few months of the year, as highlighted by the changes in PMI, sales by large services companies and the sectoral confidence indicator. Social security affiliation in the services sector as a whole slowed in January and February. However, this was mainly a result of the public-sector recruitment freeze, as the slowdown was almost imperceptible in the case of market services. Inflows of tourists also continued to grow rapidly in January (Exhibits 2.3 and 2.4).

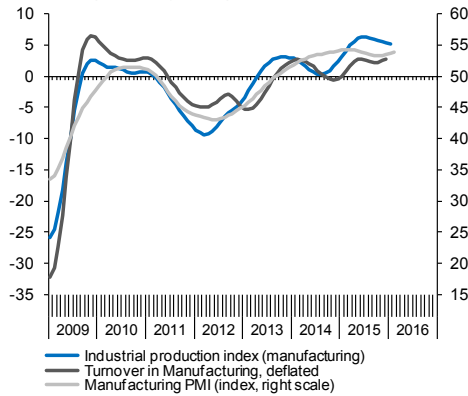
In the case of construction, the positive trend in new housing permits suggests increased activity in the residential segment, while the drop in official tenders indicates a further decline in public works. The indicator for sales by large construction companies and developers was highly negative in January and the confidence indicator also worsened. Nevertheless, social security affiliation has continued to rise rapidly, with just a slight trend towards a deceleration.

Total employment (in full-time equivalent job terms) rose by 2.4% in the last quarter of 2015, and 3% over the year as a whole, an increase

Exhibit 2

Industrial activity, services and construction indicators**2.1 - Industrial sector indicators (I)**

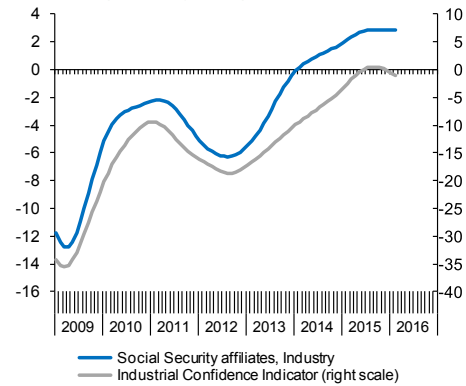
Annualised moving quarterly change in % and index, smoothed series



Sources: INE, Markit Economics Ltd and Funcas.

2.2 - Industrial sector indicators (II)

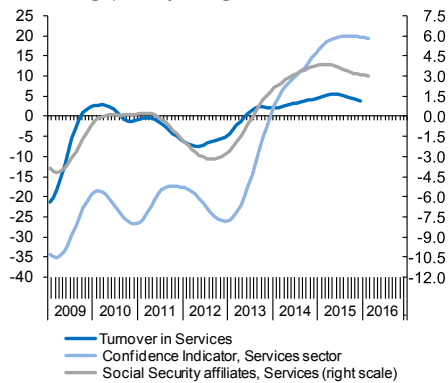
Annualised moving quarterly change in % and index, smoothed series



Sources: European Commission, Ministry of Labour and Funcas.

2.3 - Services indicators (I)

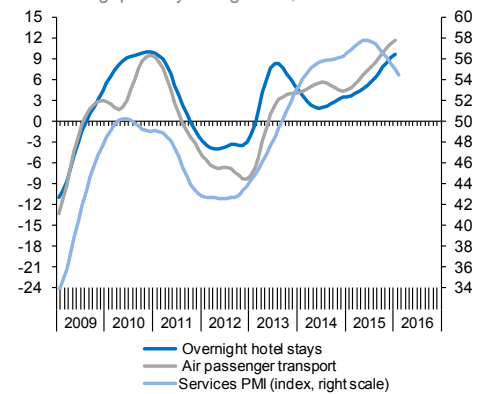
Annualised moving quarterly change in % and index, smoothed series



Sources: European Commission, Ministry of Labour, INE and Funcas.

2.4 - Services indicators (II)

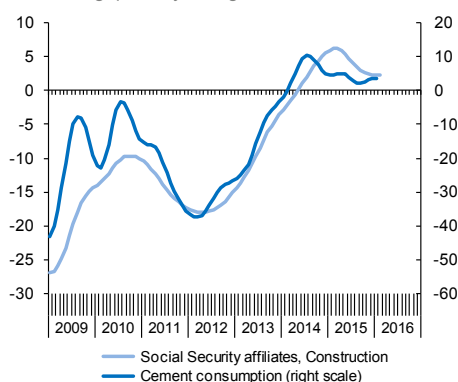
Annualised moving quarterly change in %, smoothed series



Sources: INE, AENA, Markit Economics Ltd. and Funcas.

2.5 - Construction sector indicators (I)

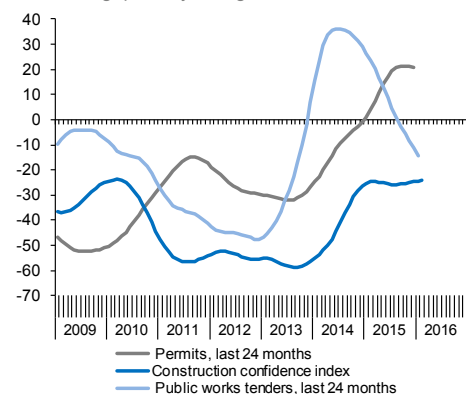
Annualised moving quarterly change in %, smoothed series



Sources: Ministry of Labour, OFICEMEN and Funcas.

2.6 - Construction sector indicators (II)

Annualised moving quarterly change in %, and index, smoothed series



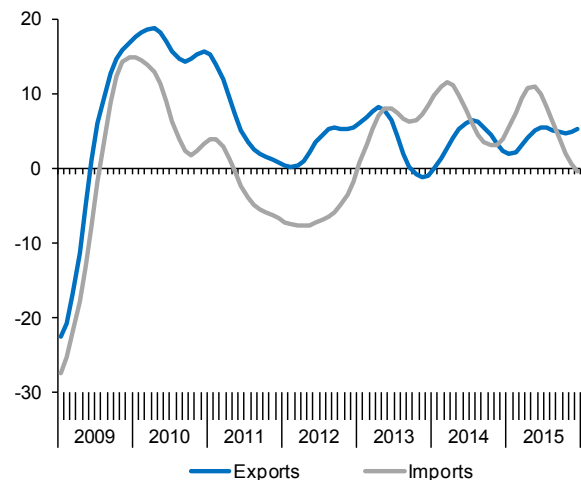
Sources: Ministry of Industry, SEOPAN and Funcas.

Exhibit 3

External sector

3.1 - Exports/Imports at constant prices (Customs)

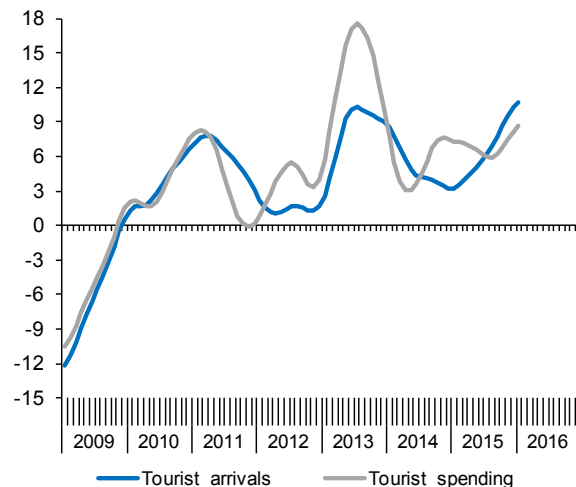
Annualised moving quarterly change in %, smoothed series



Source: Ministry of Economy.

3.2 - Tourist sector

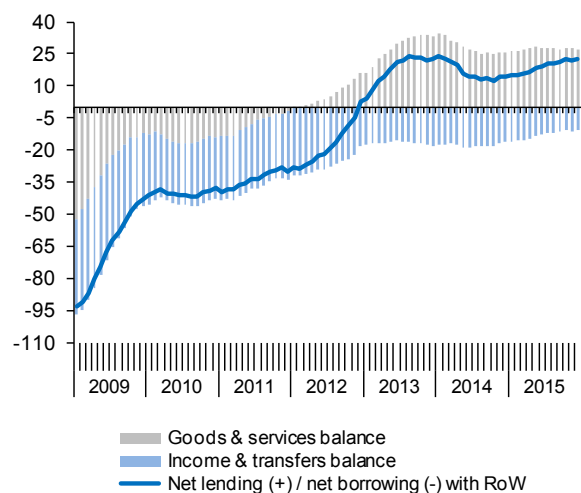
Annualised moving quarterly change in %, smoothed series



Source: Ministry of Industry.

3.3 - Balance of payments (I)

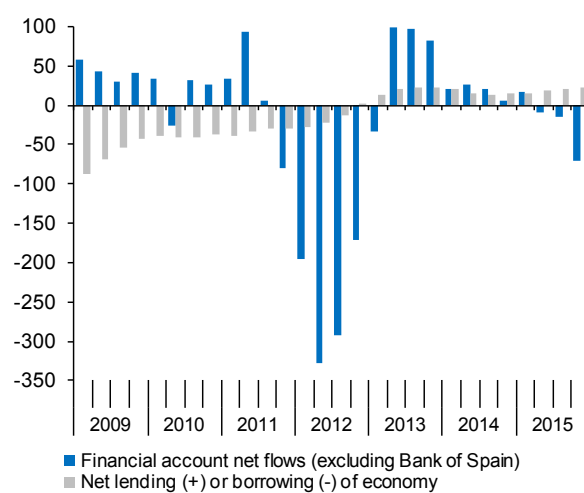
EUR billion, cumulative last 12 months



Source: Bank of Spain.

3.4 - Balance of payments (II)

EUR Billions, moving sum 4 quarters



Source: Bank of Spain.

equivalent to 487.7 thousand jobs. In terms of the Labour Force Survey, employment rose by 522 thousand, although the reduction in unemployment was somewhat larger, at 554 thousand, as the reduction in the working-age population caused the labour force to shrink. The average annual

unemployment rate dropped by 2.3 percentage points to 22.1% (Exhibits 4.1 and 4.2).

There was a slight drop in employment in the manufacturing industry in the fourth quarter, but this followed strong growth throughout the first

half of the year, such that over the year as a whole there was a rise of 2.9%, the best result since 2000. In any event, the sector in which employment increased most in relative terms over the year as a whole was construction. Employment growth in public administration, health and education came

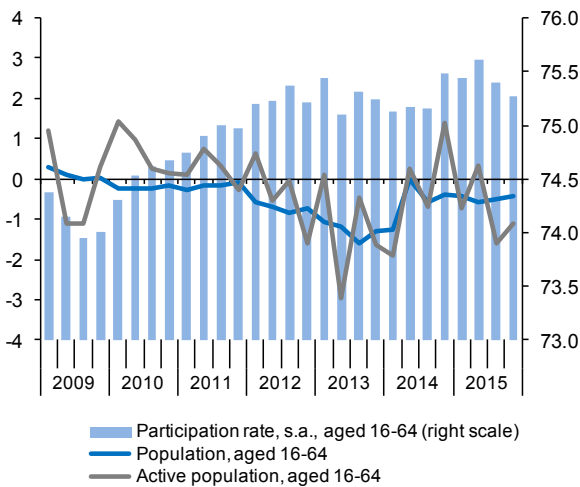
to 2%. Growth in the total number of social security affiliates slowed in January and February 2016. However, this was due to the drop in agricultural employment caused by the unusually early end of the olive harvest, and the freeze on public sector recruitment. Excluding these two sectors,

Exhibit 4

Labour market indicators

4.1 - Labour supply

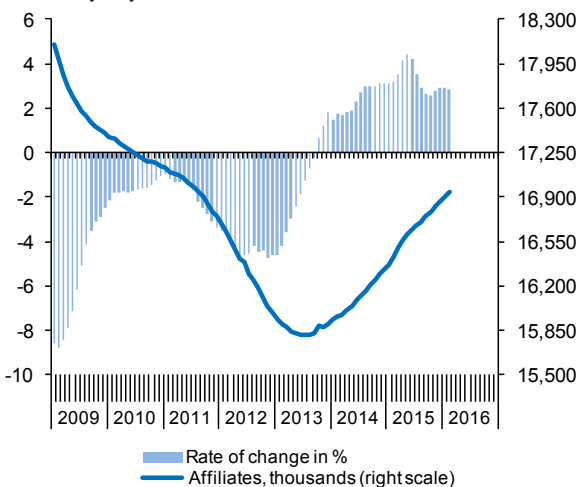
Annualised change q-o-q in % and percentage of population aged 16-64



Source: INE (LFS).

4.3 - Social Security affiliates

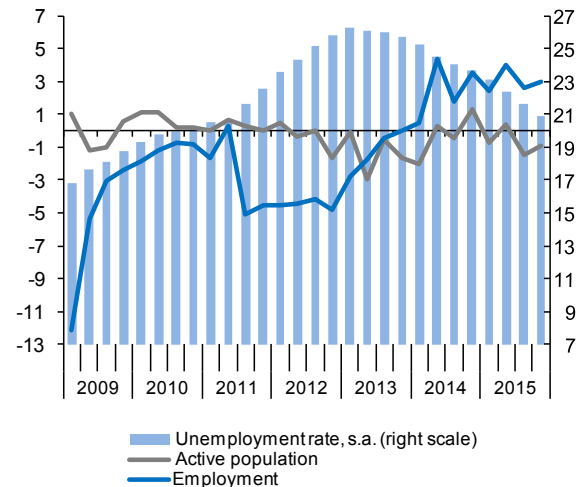
Annualised moving quarterly change in % and thousands, seasonally-adjusted data



Source: Ministry of Labour and Funcas.

4.2 - Employment and unemployment (LFS)

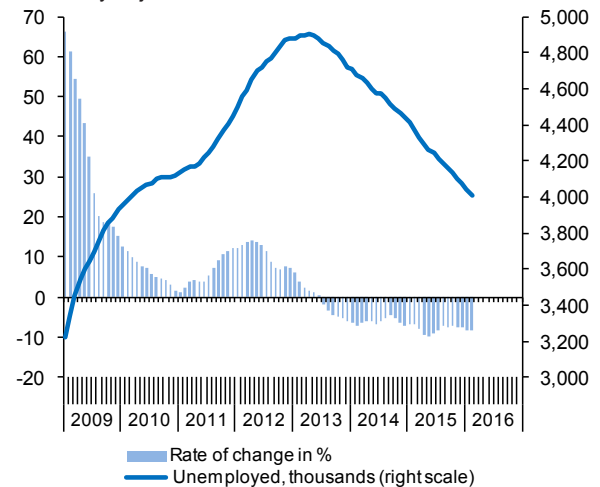
Annualised change q-o-q in % and percentage of working age population



Source: INE (LFS).

4.4 - Registered unemployment

Annualised moving quarterly change in % and thousands, seasonally-adjusted data



Source: Ministry of Labour and Funcas.

affiliation grew at a rate similar to that in previous months (Exhibits 4.3 and 4.4).

In short, the activity and demand indicators for the start of 2016 are giving contradictory signals. However, taken together, using the synthetic activity indicator prepared by Funcas, they suggest a deceleration of the growth rate, which in non-annualised terms, could be somewhere between 0.6% and 0.7% in the first quarter of the year.

Activity and demand indicators for the start of 2016 are giving contradictory signals. However, taken together, using the synthetic activity indicator prepared by Funcas, they suggest a deceleration of the growth rate.

Productivity of the economy as a whole showed positive growth in the fourth quarter, as in the preceding quarters, such that it rose at an annual

rate of 0.2% in 2015. Productivity also rose in the manufacturing industry over the year as a whole, at 0.8%, although this was its slowest rise since the start of the crisis. Compensation per employee grew by 0.5% across the economy in 2015 (although this was largely a result of public sector employees being paid Christmas bonuses withheld in the wake of the crisis) and dropped by 0.1% in manufacturing industry. As a result of the foregoing, unit labour costs rose slightly across the economy as a whole in 2015 for the first time since 2009, while ULC continued to fall in manufacturing industry. Wage increases relative to last year agreed through collective bargaining up until February averaged 1.1%, indicating faster wage growth in 2016.

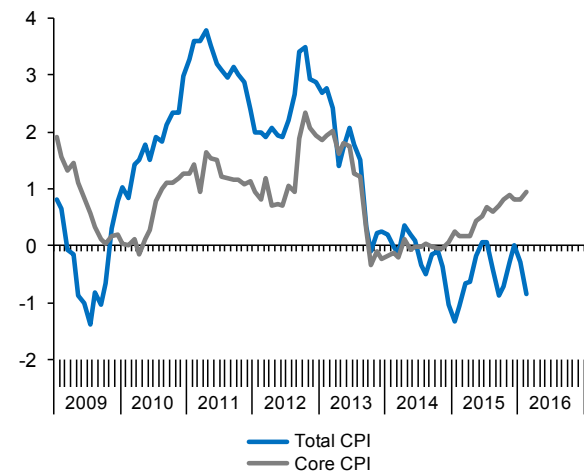
Further falls in the price of energy products have meant that the inflation rate in the first few months of 2016 has been negative and lower than expected. Nevertheless, the core rate has remained at positive levels, with a slow upward trend, as a result of the depreciation of the euro and recovery in domestic demand. Apart from the energy products group, all the other components

Exhibit 5

Price indicators

5.1 - Consumer Prices Index

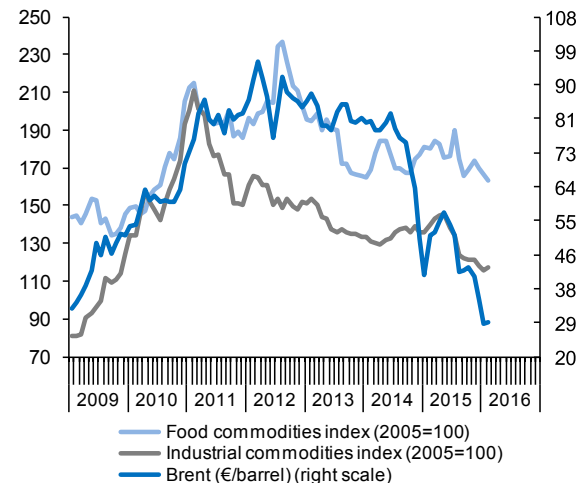
Change y-o-y in %



Source: INE (CPI).

5.2 - Commodities prices in €

Euros and index

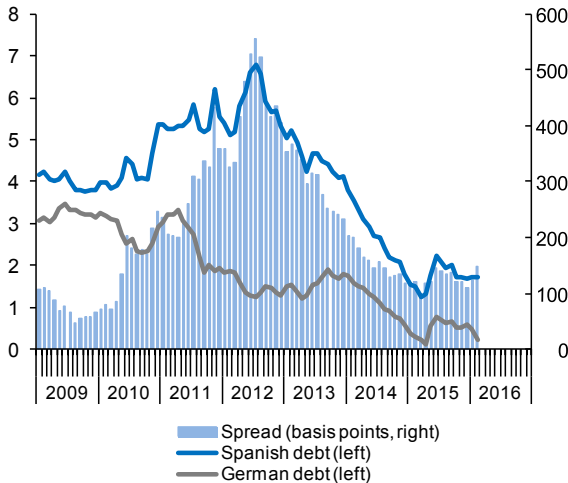


Sources: Ministry of Economy and The Economist.

Exhibit 6

Financial indicators**6.1 - Government 10 years bonds rate**

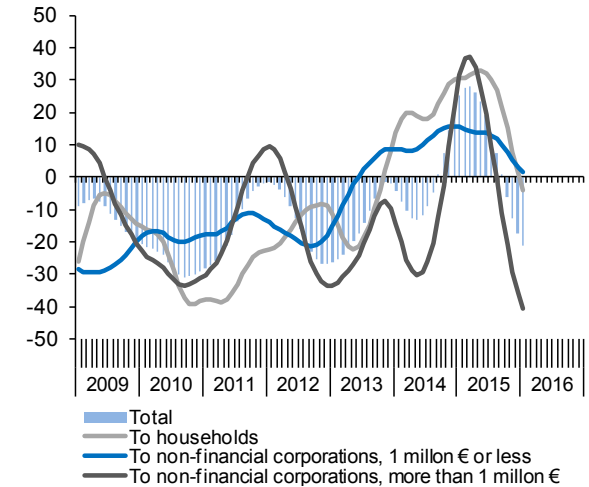
Percentage and basis points



Sources: ECB and Bank of Spain.

6.2 - New business loans

Annualised moving quarterly change in %, smoothed and s.a. series



Source: Bank of Spain and Funcas.

of the consumer basket have shown positive inflation rates, such that the current situation cannot be considered deflationary (Exhibits 5.1 and 5.2).

The current account of the balance of payments turned a surplus of 1.5% of GDP in 2015, according to provisional figures. This was more than the 1% surplus recorded in 2014, due to the lower energy bill and smaller interest payments abroad. The trade surplus in non-energy goods, by contrast, dropped as a result of faster growth in imports than in exports (Exhibits 3.1 and 3.3). The financial balance, excluding the Bank of Spain, registered net outflows of 70.2 billion euros, as a result of Spanish investments abroad – which rose by 40% – exceeding foreign investments in Spain, which were halved (Exhibit 3.4).

Spain's net lending position vis-à-vis the rest of the world rose to 2.2% of GDP, compared with 1.6% in 2014, as a result of the national savings rate rising faster than the investment rate. The household savings rate in the period to the third

quarter of the year (the most recent period for which data are available broken down by sectors), fell in comparison with the same period the previous year, while the savings rate of non-financial corporations increased, and that of the general government was less negative (Exhibits 7.1 and 7.2).

The deleveraging of private-sector agents continued to progress throughout 2015, in both absolute and relative terms. In the third quarter of 2015, household debt represented 107.7% of their gross disposable income, compared with 114.3% a year earlier. In relation to GDP it represented 68.6% in the third quarter of 2015, compared with 73.6% in 2014. In the case of non-financial corporations, the debt ratio dropped from 116.2% of GDP in the third quarter of 2014, to 107.2% in the same period of 2015 (Exhibit 7.4).

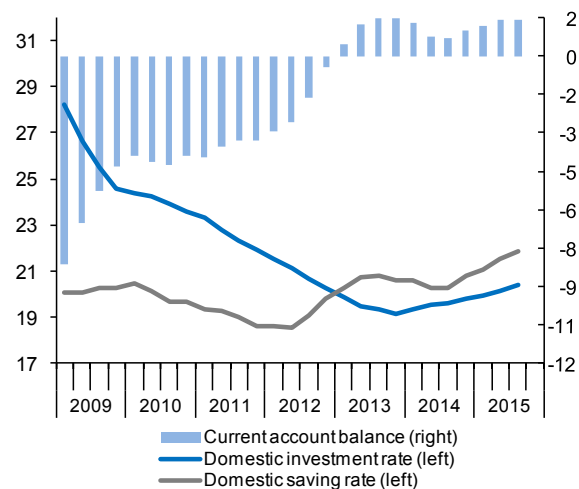
Declining debt volumes are not incompatible with new credit growth, which recovered somewhat in 2015, in the case of lending to both businesses and households. Nevertheless, in the last quarter

Exhibit 7

Financial imbalances

7.1 - Domestic saving, investment and current account balance

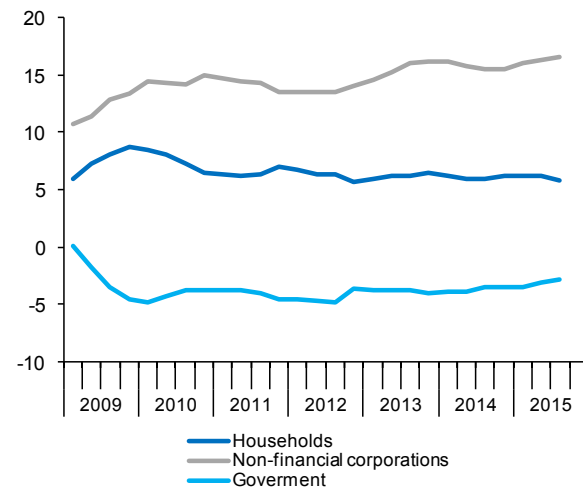
Percentage of GDP, 4-quarter moving average



Source: INE.

7.2 - Saving rates

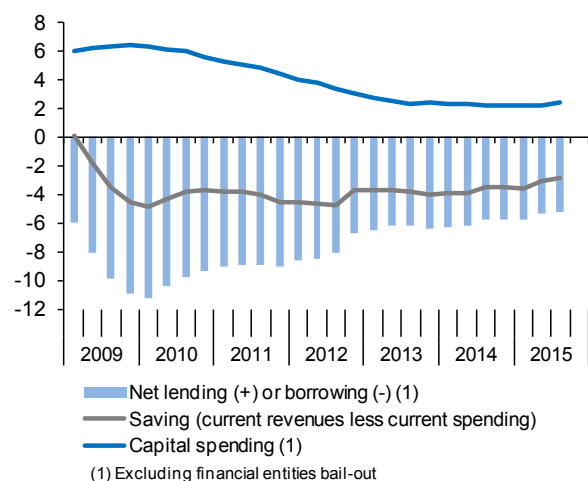
Percentage of GDP, 4-quarter moving average



Sources: INE and IGAE.

7.3 - General Government deficit

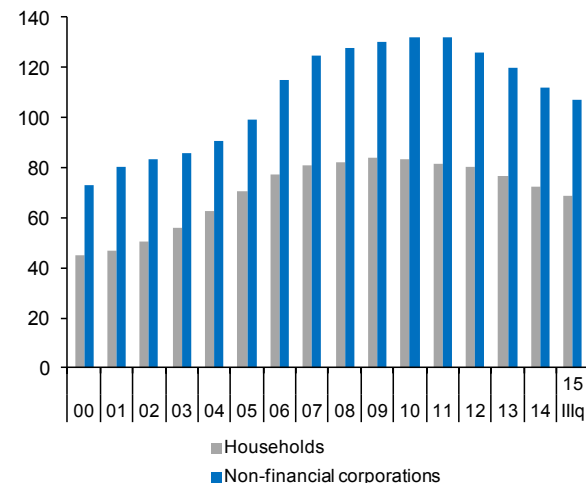
Percentage of GDP, 4-quarter moving average



Sources: INE and IGAE.

7.4 - Gross debt

Percentage of GDP



Source: Bank of Spain (Financial Accounts).

of the year there was a significant drop, which sharpened further in January 2016 (Exhibit 6.2). It is still too early to say whether these declines represent a permanent trend change in the path of this variable's recovery, or a transitory interruption

that may be related to international and domestic uncertainties.

In the period to November 2015, the combined deficit of the central government, the social

security funds, and the autonomous regions came to 41.8 billion euros, 5.4 billion euros less than in the year-earlier period, a figure equivalent to 3.87% of annual GDP. This result is still under the 4.2% target for the year, but given December's highly negative seasonality, particularly in the case of the social security accounts, the target will be surpassed. The final result is probably very close to 5% of GDP.

The 2015 deficit target of 4.2% will be surpassed and the final result will probably be close to 5% of GDP.

General government debt, in this case based on data to December 2015, rose to 1,070.3 billion euros, 36.5 billion euros more than in December 2014. Nevertheless, thanks to increased nominal GDP growth (3.8%) the ratio to GDP dropped by three tenths of a percent, to 99%. The autonomous regions were responsible for the majority of this increase in debt.

Forecasts for 2016-2017

In the first few months of this year, the price of oil dropped considerably relative the scenario contemplated in the previous forecasts, which would suggest that they should be revised upwards. However, a number of other factors are acting in the opposite direction. These include slower-than-expected growth of the global economy, in the case of both developed and emerging economies, and increased uncertainty deriving from this and other factors, that triggered serious tensions in international financial markets in the first two months of the year. The impact of these factors will be reflected in a sharper slowdown in growth towards the third quarter of the year.

Consequently, the GDP-growth forecast for 2016 has been revised downwards one tenth

of a percent to 2.7%. This scenario does not consider the possible impacts of domestic political uncertainty, as these may vary according to how the situation evolves over the coming months. In any event, this represents a significant risk factor that may translate into worse-than-expected economic performance. 2017 should see a return to quarter-on-quarter growth rates in the order of 0.6%, once the current global uncertainty has passed, despite which the annual rate will be below this year's, at 2.3%. The same pattern of contributions to growth of the past two years will be maintained, *i.e.* a positive contribution from domestic demand and a negative contribution from the external sector (Exhibits 8.1 and 8.2).

Growth in private consumption will pick up speed in 2016 to 3.3% thanks to the stimulus from the lower oil price, job creation, and income-tax cuts. This stimulus will run out of steam in 2017, when oil prices are expected to rise slightly, such that this variable is likely to grow by 2.6% next year. As regards public consumption, given the deficit reduction targets, a slowdown is to be expected in both years relative to the sharp rise in 2015 (Exhibit 8.3).

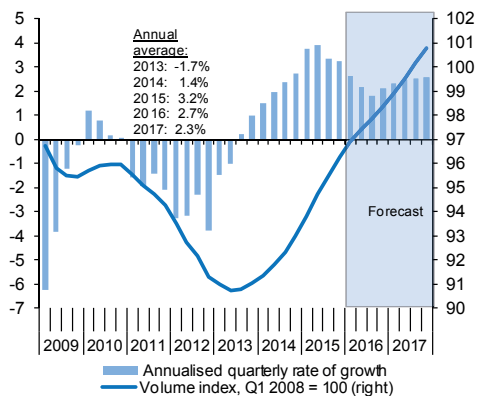
Expected growth in investments in machinery and capital goods in 2016 has been revised downwards as, together with exports, this is one of the components of demand on which the effect on the Spanish economy of slower global growth and heightened international uncertainties will most strongly be felt.

Expected growth in investments in machinery and capital goods in 2016 has been revised downwards to 5.1%, as, together with exports, this is one of the components of demand on which the effect on the Spanish economy of slower global growth and heightened international uncertainties will most strongly be felt. Growth of this component of demand will also be more moderate in 2017 at 4%.

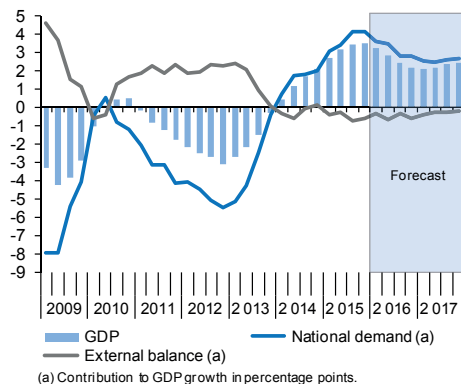
Exhibit 8

Economic forecasts for Spain, 2016-17
Change y-o-y in %, unless otherwise indicated

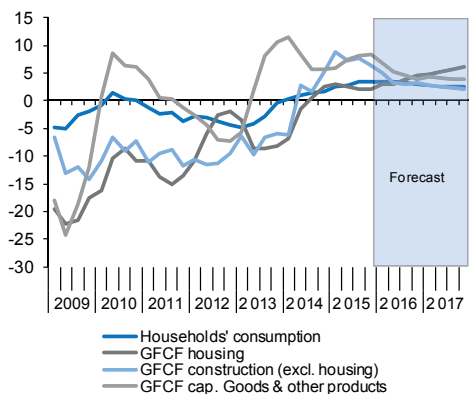
8.1 - GDP



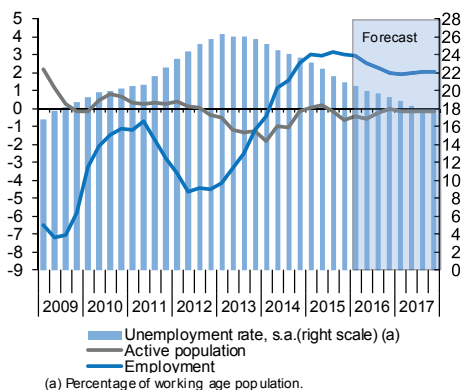
8.2 - GDP, national demand and external balance



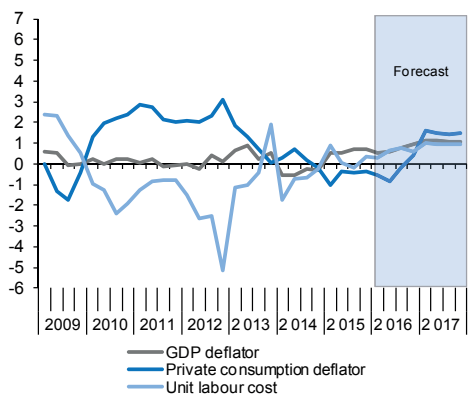
8.3 - National demand aggregates



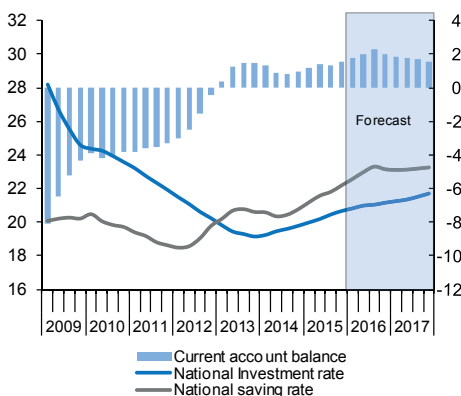
8.4 - Employment and unemployment



8.5 - Inflation



8.6 - Saving, investment and c/a balance (% GDP, 4qt moving averages)



Source: INE (Quarterly National Accounts) and Funcas (forecasts).

Table 1

Economic forecasts for Spain, 2016-2017

Annual rates of change in %, unless otherwise indicated

	Actual data				Funcas forecasts		Change forecast (a)
	Average 1996-2007	Average 2008-2013	2014	2015	2016	2017	2016
1. GDP and aggregates, constant prices							
GDP	3.8	-1.3	1.4	3.2	2.7	2.3	-0.1
Final consumption households and NPISHs	3.6	-2.2	1.2	3.1	3.3	2.6	0.1
Final consumption general government	4.3	0.7	0.0	2.7	2.0	1.3	0.6
Gross fixed capital formation	6.4	-7.0	3.5	6.4	4.3	3.9	-1.0
Construction	5.9	-9.8	-0.2	5.3	3.6	3.8	-0.9
Residential construction	7.8	-11.2	-1.4	2.4	3.6	5.5	-1.8
Non-residential construction	4.2	-8.2	0.8	7.5	3.7	2.4	-0.2
Capital goods and other products	7.5	-2.4	7.7	7.5	5.1	4.0	-1.0
Exports goods and services	6.6	1.7	5.1	5.4	3.8	4.8	-1.3
Imports goods and services	8.7	-4.1	6.4	7.5	5.7	6.0	-1.2
National demand (b)	4.5	-3.0	1.6	3.7	3.2	2.5	-0.1
External balance (b)	-0.7	1.7	-0.2	-0.5	-0.5	-0.3	-0.1
GDP, current prices: - € billion	--	--	1,041.2	1,081.2	1,118.0	1,155.8	--
- % change	7.4	-0.8	1.0	3.8	3.4	3.4	-0.4
2. Inflation, employment and unemployment							
GDP deflator	3.5	0.5	-0.4	0.6	0.7	1.1	-0.2
Household consumption deflator	3.1	1.8	0.2	-0.5	-0.3	1.5	-1.2
Total employment (National Accounts, FTEJ)	3.4	-3.3	1.1	3.0	2.4	2.0	0.0
Productivity (FTEJ)	0.4	2.1	0.3	0.2	0.3	0.3	-0.1
Wages	7.5	-1.1	0.9	3.9	3.5	3.4	0.1
Gross operating surplus	6.9	-0.2	0.4	3.1	2.8	2.8	-0.8
Wages per worker (FTEJ)	3.3	2.4	-0.6	0.5	0.8	1.3	0.0
Unit labour costs	2.9	0.3	-0.8	0.3	0.6	1.0	0.2
Unemployment rate (LFS)	12.5	20.2	24.4	22.1	19.9	18.2	-0.3
3. Financial balances (% of GDP)							
National saving rate	22.4	19.9	20.8	22.2	23.1	23.2	0.4
- of which, private saving	18.6	23.1	24.3	25.0(c)	24.9	24.0	0.5
National investment rate	26.9	23.2	19.8	20.7	21.2	21.7	-0.1
- of which, private investment	23.0	19.4	17.7	18.5(c)	19.0	19.6	-0.2
Current account balance with RoW	-4.5	-3.3	1.0	1.5(c)	2.0	1.6	0.6
Nation's net lending (+) / net borrowing (-)	-3.7	-2.8	1.6	2.2(c)	2.7	2.2	0.7
- Private sector	-2.8	5.8	7.5	7.2(c)	6.6	5.1	0.7
- Public sector (general governm. deficit)	-0.9	-8.6	-5.9	-5.0(c)	-4.0	-2.9	-0.1
- General gov. deficit exc. financial instit. bailouts	--	-7.8	-5.8	-5.0(c)	-4.0	-2.9	-0.1
Gross public debt	52.2	66.8	99.3	99.0	99.2	98.9	-0.8
4. Other variables							
Household saving rate (% of GDI)	10.2	10.2	9.6	9.0(c)	9.3	8.9	-0.6
Household gross debt (% of GDI)	82.1	127.2	112.1	106.2(c)	100.7	97.7	1.6
Non-financial corporates gross debt (% of GDP)	80.0	127.9	112.2	104.3(c)	97.5	91.5	-0.7
Spanish external gross debt (% of GDP)	90.2	159.7	166.2	168.3(c)	165.0	160.1	-0.7
12-month EURIBOR (annual %)	3.7	1.9	0.5	0.2	0.0	0.3	-0.2
10-year government bond yield (annual %)	5.0	4.7	2.7	1.7	1.7	2.2	-0.1

Notes:

(a) Change between present and previous forecasts, in percentage points. (b) Contribution to GDP growth, in percentage points.

Sources: 1996-2015 except for (c): INE and Bank of Spain; Forecasts 2016-2017 and (c): Funcas.

The forecast for construction investment in 2016 has also been revised downwards, due to the lower-than-expected growth in the residential component in the last quarter of 2015. Nevertheless, this component's growth will continue to pick up speed in 2016, while growth of investment in other constructions will slow significantly with the end of the effect of the electoral cycle on public investment, which is what stimulated this variable last year. In 2017, it is expected that housing construction will continue to gain strength, while the other constructions component will continue to slow.

Exports will slow to 3.8% in 2016, which is significantly down from the last forecast, as a result of worsening global economic conditions. Imports have also been revised downwards to 5.7%, due to the expected slower growth of final demand resulting from the decline in investment and exports. Both these variables are expected to grow somewhat faster in 2017. Consequently, the external sector's contribution to GDP growth will be somewhat more negative than forecast previously in 2016.

Employment, measured in full-time equivalent job terms, is set to grow by 2.4% this year (unchanged from the last forecast) and 2% next year. In terms of the numbers of people in work according to the labour force survey (LFS), employment generation between the two years will be 794,000, and the unemployment rate will drop to an annual average of 19.9% in 2016 and to 18.2% in 2017 (Exhibit 8.4).

Productivity of the economy as a whole is likely to grow in both years at 0.3%, a similar rate to preceding years. In conjunction with faster growth in compensation per employee, this will lead to a rise in unit labour costs of 0.6% and 1% in 2016 and 2017, respectively. This remains below increases in the GDP price index.

As regards inflation, even supposing the oil price recovers to over 45 dollars a barrel during the year, the headline inflation rate will be negative at

least for the first half of this year. The core rate will be positive throughout 2016 at around 1% and will accelerate slightly in 2017 (Exhibit 8.5).

The general government deficit will drop to 4% of GDP in 2016 solely as a result of the favourable effect of the cycle. In 2017, the deficit is set to drop to 2.9% of GDP. This is basically due to the smaller cyclical deficit, with the improvement in the structural deficit having only a minor impact.

The surplus on the current account of the balance of payments will increase in 2016 despite the negative contribution of external sector growth, thanks to the lower oil price. With regard to 2017, the starting point hypothesis is that this favourable situation will not be repeated, such that the surplus will shrink as imports grow faster than exports (Exhibit 8.6).

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To conclude, the impact of the one-off factors that stimulated growth in 2015 is wearing off, and, at least in 2016, this is being compounded by worsening global economic conditions. The outlook in Spain is therefore for slower GDP growth this year and next. The downside risks are considerable. These derive from the possibility of renewed tensions in financial markets and the possible negative impact of the situation of domestic political uncertainty on investment and employment decisions.

The Spanish economy: The need for restoring growth potential and modernisation

Emilio Ontiveros¹

The Spanish economy's recovery is currently outperforming that of the eurozone average. To achieve sustainable growth over time, it will be essential to modernise the Spanish economic model with a focus on increasing competitiveness through a variety of channels in addition to lower input costs.

Spain's economic recovery has been the most vigorous in the euro area. As was the case in the preceding recession, the strength of the recovery was influenced by temporary external factors, such as cheaper energy commodities and the ECB's monetary policy. This year's projected growth of around 2.7% will depend on the continuation of this recovery, in addition to financial stability and global economic growth. While achieving adequate growth figures is important, modernisation of the economy through strengthening Spain's competitive advantage in areas apart from direct costs is no less so. Restoring growth potential and modernisation will require the resolution of political uncertainty, arising from government formation gridlock at the national level since the end of last year as well as Catalonia's independence movement.

At the end of 2015, Spain recorded GDP growth of 3.2% – twice the eurozone average. Growth was accompanied by job creation and correction of external imbalances. However, the government struggled to reduce the fiscal deficit in line with the agreed EU target. In fact, as the European Commission (2016) has warned, the structural deficit deteriorated significantly in 2015, while public debt reached almost 100% of GDP.

These macroeconomic developments – signs of a clear recovery following a deep recession – are not, however, supported by sufficient normalisation of economic agents' behaviour. Households have not seen a significant increase in income. Firms

are not scaling up their investment decisions at a rate parallel to the expansion of their business, and perhaps most importantly, in line with the need to strengthen competitive advantages other than lower input costs. The general government, for its part, remains constrained by the application of austerity programmes, forcing a contraction of its spending and investment plans.

At present, indicators also fail to confirm that the Spanish economy will be able to ensure sustainable growth over the medium-term. This is primarily because capital, in all its forms, has yet to recover from the erosion suffered during the crisis, but also because there are insufficient signs

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of a transformation in the growth model towards one in which the quality of factors and institutions takes precedence over keeping costs relatively low. The need for this change is particularly pressing in the political context resulting from the recent general elections. On top of the risks deriving from a deterioration in the international economic environment, less favourable than it was during the recovery, there are the contingencies associated with more complex and less stable political governance. And all of this is taking place in a complex international context, in which the year has started off dominated by severe financial instability, which has hit European bank shares particularly hard.

In what follows, this article aims to identify the existing damage to Spain from the crisis and options for remedying it. It then goes on to describe certain measures to reduce the vulnerability of the Spanish economy to shocks, such as those caused by the 2007 crisis, highlighting the priority decisions needed to encourage a more knowledge-based growth model. The article concludes with consideration given to the constraints deriving from the international environment and the political situation following the general elections in December 2015.

Remedying the damage

Unevenly distributed impacts

Spain was more severely affected by the 2007 crisis than the Eurozone average. Despite the recent recovery, at the end of 2015, GDP was still below 2007 levels. The unemployment rate remains over 20% (compared with 8% in 2007), with a relatively large long-term component, and many households with all members unemployed.

The imbalance that played the largest part in exacerbating the consequences of the crisis was household and non-financial corporate debt with the domestic banking system. The public finances

were comparatively healthy: at the end of 2007, the government's fiscal surplus was 2% of GDP, and public debt stood at 35.5% – among the lowest in the OECD.

The imbalance that played the largest part in exacerbating the consequences of the crisis was household and non-financial corporate debt with the domestic banking system.

The slump in activity, and – of course – in residential construction, led to a sharp drop in government revenues, driving up the deficit and public debt. This coexisted with increased vulnerability of the banking system, which was the first to be affected by the collapse of global credit markets. The economy's heavy reliance on bank finance meant that financial system disruption was passed on more quickly and more powerfully to the real economy. This in turn intensified the vicious cycle between the tensions in public debt markets, the deepening recession, and worsening bank balance sheets, which included a substantial portion of public debt, and, of course, mortgages.

Applying pro-cyclical fiscal austerity, which Paul de Grauwe (2015) termed “panic-induced austerity”, was somewhat counterproductive to facilitating a recovery in economic growth. As de Grauwe points out, against the backdrop of a recession, these policies reduced the effectiveness of automatic stabilisers, making the drop in activity more intense. There was a manifest erosion of all forms of capital – physical, human, technological – and, consequently, of the economy's potential growth rate.

Basis for the recovery

Spain suffered a significantly worse slowdown in growth than the eurozone average, and external drivers have subsequently played a bigger role in the recovery than in most euro-area economies.

The first driver was the change in the European Central Bank's stance as of summer 2012, when it showed it was willing to act against the collapse in government bond prices which reflected expectations of a break-up of the euro. Spain was particularly affected by falling bond prices and worsening bank balance sheets. This led to the need for European financial assistance to recapitalise the banks in June 2012, which was the first form of support for the economic recovery, alleviating the harm caused by austerity. From then on, the ECB's adoption of monetary policies modelled after those of the Federal Reserve and the Bank of England enabled further progress on restoring households' and firms' balance sheets to health, and reducing interest on public debt.

Exceptionally expansionary monetary policy adopted by the ECB, the consequent depreciation of the euro and the cheapening of raw materials and consumables, in particular hydrocarbons, represented a bigger stimulus for the Spanish economy than for the eurozone average. This was due to the higher level of debt and the vulnerability of the banking system, along with the higher level of dependence on oil and gas imports. The strength of exports also played a major role in the recovery. Export growth was largely driven by Spanish firms' increased propensity to export in order to compensate for lacklustre domestic demand, and it was also boosted by cheaper input costs, including labour.

Expansionary monetary policy adopted by the ECB, the consequent depreciation of the euro and the cheapening of raw materials and consumables, in particular hydrocarbons, represented a bigger stimulus for the Spanish economy than for the eurozone average. The big question is whether these drivers will endure over time.

The big question raised by this pattern of recovery is whether these four drivers will endure over the

longer term. In the absence of a strengthening of other, more lasting, competitive advantages, it is highly likely that growth will be insufficient to continue reducing unemployment and shrinking the considerable debt burden. This was pointed out by the IMF's latest Article IV report (2015), which warned of Spain's low medium-term growth potential. The IMF forecast growth of 1.8% for the Spanish economy in 2020. Unless there is further deterioration in the international environment, beyond that already witnessed, the Spanish economy could maintain solid growth over the next two years, of 2.7% and 2.3%, in 2016 and 2017, respectively (Table 1). Although not as strong as in 2015, growth drivers include favourable monetary conditions, a gradual recovery in credit and relatively low commodity prices, which are helping keep Spain's growth above its potential rate. However, unless investment picks up and productivity rises, it will be difficult to reduce structural unemployment and thus raise potential growth.

Despite strong job creation in 2015, there are clear risks of further deterioration in most people's living standards, given the trends in average wages, job quality, the number of unemployed receiving no benefits whatsoever, and the widening income and wealth gaps.

These limitations, and the uneven distribution of income generated during the recovery, help explain why last year's macroeconomic figures have not translated into more optimistic perceptions among economic agents. Despite strong job creation in 2015, there are clear risks of further deterioration in most people's living standards, given the trends in average wages, job quality, the number of unemployed receiving no benefits whatsoever, and the widening income and wealth gaps. Reducing inequality is a necessary condition for stability, particularly political stability. However, it is also a prerequisite for economic growth.

Table 1

Economic forecasts

Macroeconomic data on the Spanish economy				
	AFI			
Annual rate (%)	2014	2015	2016	2017
Real GDP	1.4	3.2	2.7	2.3
Consumer spending	0.9	2.9	2.6	1.9
Households	1.2	3.1	2.9	2.1
General govt.	-0.0	2.5	1.6	1.3
GFCF	3.5	6.2	5.0	4.9
Capital goods	10.7	9.7	7.0	6.1
Construction	-0.1	5.6	4.6	4.9
Housing	-1.3	3.0	4.6	5.5
Domestic demand (*)	1.5	3.4	2.9	2.5
Exports	5.1	6.0	5.5	4.7
Imports	6.4	7.8	6.8	6.1
External demand (*)	-0.2	-0.3	-0.2	-0.2
CPI (annual average)	-0.2	-0.5	0.2	1.1
GDP deflator	-0.4	0.6	1.0	1.3
Nominal GDP	1.0	3.8	3.7	3.6
Employment (LFS)	1.2	3.0	2.5	2.0
Unemployment rate (LFS)	24.4	22.1	20.1	18.9
Public sector balance (% GDP)	-5.8	-4.7	-3.7	-2.7
Private sector balance (% GDP)	99.3	100.7	101.3	100.5

Note: (*) Contribution to GDP growth.

Source: AFI, the author.

Modernising the economy

Restoring lost capital, increasing investment, and raising productivity are necessary conditions for the Spanish economy to maintain sustainable medium-term growth. However, they are not sufficient conditions. The pace of modernisation of the economy, which experienced a slowdown as a result of the crisis, must also increase. Long before the crisis, there was already a need to shift the competitive advantage of sectors of the Spanish economy towards increased reliance on knowledge-based factors and to reduce vulnerabilities typical of less advanced economies.

There are a number of priority areas on which it should be possible to reach agreement, regardless of the ultimate distribution of political power. These may be summarised as follows:

Strengthening technological capital and education

The Spanish innovation system was one of the biggest victims of the crisis. Spain was already near the bottom among advanced economies in terms of R&D investment before the crisis, and now its position has further worsened. In 2008,

Spain devoted 1.35% of GDP to R&D, 0.45 points less than the EU average, and by 2013 this had dropped to 1.23% of GDP. Elsewhere in the EU, investment in R&D has risen steadily during the crisis, such that Spain's investment effort has dropped by 60% in relative terms since 2004. The distance by which Spain lags behind the leaders in innovation has widened even further (Mulet, 2016).

Although the economy grew in 2014, public and private R&D investment dropped significantly compared to the previous year, and consequently, with respect to the start of the crisis. Another feature that differentiates Spain from the rest of the EU is the source of this investment. In Spain, almost half comes from public sources, whereas the EU average is just 32%. This means that this form of technological capital is highly dependent on the willingness of governments to invest, and on the priority given to R&D in any budgetary adjustment decisions taken. Whereas in other economies, the allocation of public funds tends to be fairly stable, in Spain it is highly volatile, suggesting a lack of a consistent strategy in this area.

This is an area in which there needs to be a long-term strategy, with sufficient political backing to ensure it is not at the mercy of future budget cuts.

Closely linked to better budgetary support for technological capital is education funding. As pointed out by Serrano and Soler (2015), young people's basic skill level prior to joining the labour market is insufficient. From compulsory to higher educational levels, Spain's position relative to other countries is not in line with the size of its economy.

Spain has not been able to devise a policy guaranteeing sufficient stability of adequate standards to enable school-leavers' skills to match the needs of today's society and economy. At the same time, continual changes to education policy have done little to achieve the other basic goal of reducing persistent and marked social stratification.

Businesses and entrepreneurship

The quality of management is crucial to ensuring good economic performance. Society needs to generate the necessary incentives to ensure top talent devotes its abilities to entrepreneurship. It is also necessary in order to ensure efforts are productive, and to clearly distinguish entrepreneurs from profiteers, as John Maynard Keynes put it.

However, while creating the right conditions and removing barriers for new start-ups is important, taking the comprehensive parameters of the World Bank's Doing Business Report as a reference, it is no less important to encourage business growth, so as to ensure that businesses are better able to adopt innovation. Micro-enterprises (those with fewer than nine employees), of which there are 3.1 million in Spain, continue to account for a disproportionate share of firms (96%).

In short, there are undoubtedly gains to be made by encouraging the emergence of business structures that operate more efficiently. And this inevitably entails increasing the average size of firms, so they are able to assimilate trends in innovation and introduce appropriate improvements to the management of business subsystems. Both boosting the economy's potential growth rate and achieving productivity gains depend on these general improvements in business functioning.

Institutional quality and social inclusion

The loss of trust in Spain's institutions is one of the reasons for the major shift that has taken place in the country's political landscape. There is a pressing need for renewal, to bring institutions closer in line with economies undertaking best practice, and to break the ties of political influence that pervade the economy.

As stated by the European Union, it is also worth progressing towards diversification of the financial

system, reducing the reliance on banks and laying the foundations for assimilating the proposed changes to support Capital Markets Union.

No less important when defining growth strategies and growth sustainability is social inclusion. Michael Spence (2016) recently underlined the risks of those patterns of growth that systematically exclude population subgroups, leading to weak political and social cohesion, and ultimately, undermining growth prospects. Again, the provision of good quality education and health services is crucial to the necessary equality of opportunities and intergenerational mobility.

Support from the international environment

The extent to which the international environment will be conducive to achieving these two essential goals – restoring and modernising the economy – in the short and medium term is currently unknown. As was discussed in the first section, temporary external factors have made the biggest contribution to the Spanish economy's recovery and continued growth depends on the

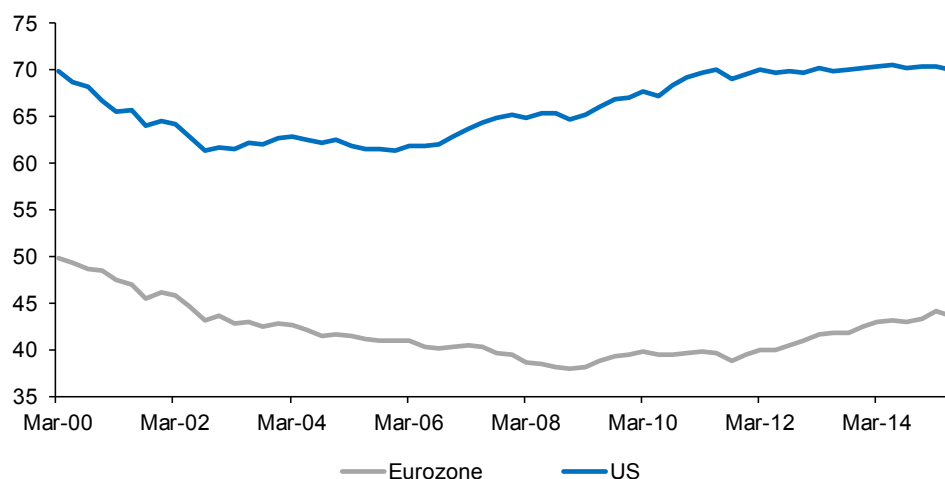
persistence of these factors. Various factors may alter the expansionary momentum with which the Spanish economy entered 2016 and slow the rate of investment.

The expansion of the global economy and international trade will be less favourable to Spain's growth than in 2015. Apart from the deceleration observed in emerging economies, there are renewed risks of financial instability deriving partly from the explicit divergence in monetary policies between the main economic blocs, with a differential impact on highly indebted energy companies. Another potential source of risk is the uneven capacity of financial systems in less advanced economies to facilitate deleveraging decisions by private-sector actors that often have high levels of dollar-denominated debt.

Irrespective of the underlying causes and the analysis of the factors triggering the slump in stock markets in the opening weeks of 2016, the resulting loss of financial wealth could have an adverse impact on growth in advanced economies. This will, of course, rein in expectations and limit the propensity to consume and invest. With the caveats that apply to specific estimates of the wealth

Exhibit 1

Households' financial wealth (% of total wealth)



Source: AFI, the author.

effect depending on the economy (assumed to be greater in the United States than in Europe, given the greater share of financial wealth in the U.S., as shown in Exhibit 1), it is highly likely that drops of more than 15% in share prices, over such a short period, will cause aggregate demand in the U.S. and Europe to contract. Moreover, given that banks' shares have been the hardest hit, it may also slow the normalisation of intermediation activity, and thus, in particular, hold back lending in the euro area.

Developments affecting China's economy and financial system have been a powerful driver of financial instability registered in the early part of the year. The perception that the world's second largest economy has entered a phase of slower growth and is struggling to stabilise and normalise its financial system and currency regime remain disruptive factors for global financial stability. Even though the direct commercial and financial links between Chinese and Spanish economies are relatively insignificant, there is clearly capacity for contagion, whether through links with major euro-area economies or through emerging economies with which Spanish firms have more direct ties.

Concerns over China's growth and financial stability remain disruptive factors. Even though direct commercial and financial links between China and Spain are relatively insignificant, there is capacity for contagion through links with major euro-area economies or through emerging economies with which Spanish firms have more direct ties.

The impact of the slowdown in Chinese import demand, particularly in the case of commodities, is one of the factors contributing to the more acute difficulties being faced by economies of relevance to Spain, such as Brazil. Spain's direct investment in Brazil is fairly significant, and it generates substantial income and profits for some of Spain's

largest firms, which have a key place in Spanish stock market indices.

Additionally, the complexity of the geopolitical context, with falling energy and commodity prices, also does little to favour economic and financial stability. The tension between Saudi Arabia and Iran is just one illustration of this.

Within the euro area, growth has been weak since the start of the public debt crisis in 2010. GDP at the end of 2015 had still not returned to its end-2007 level, and economic players' confidence levels also remain low. Inflation has as yet failed to respond to monetary stimuli, suggesting, as some authors argue (Roubini, 2016) that the traditional causal link between money supply and price changes may have been broken. Despite low capital costs, investment is scant, as is productivity growth, while the export sector is unable to make a significant contribution to growth owing to the weakness of the emerging economies. It will not be easy either for the euro area to free itself from the obstacles to increasing its potential growth, as highlighted by the various academics working together under the title of Rebooting Consensus Authors (2015). Some of the imbalances making the crisis more acute in the euro area have yet to be corrected. These include the quality of bank assets or banks' exposures to home-country public debt, and the general vulnerability in those economies with high levels of private debt to the normalisation of ECB monetary policy. Shrinking financial margins and increased regulatory pressure are a bad combination for some European banking systems, as stock markets have recently noticed.

Banks' shares were hit hardest as prices slid in the first few weeks of 2016, particularly in the euro area. Concerns over the banking sector seem to be predicated on the assumption that near-zero interest rates, lacklustre economic growth, high default rates and greater regulatory pressure will be irreconcilable with adequate margins and returns on equity. This is particularly relevant in the case of retail banking. Fears became more acute when it became apparent that the ECB had

limited room to manoeuvre through reliance on extra stimulus without generating more financial instability.

Concerns over the banking sector seem to be predicated on the assumption that near-zero interest rates, lacklustre economic growth, high default rates and greater regulatory pressure will be irreconcilable with adequate margins and returns on equity.

This has all contributed to a renewed focus on the concept of “secular stagnation.” On November 8th, 2013, at the IMF’s Economic forum, Larry Summers “resuscitated”, as he himself put it, Alvin Hansen’s idea of the possibility of a secular stagnation in advanced economies. This is an idea that is particularly applicable to the euro area. Since then, events have done nothing to refute this hypothesis. Investment decisions are far from expansionary, despite real interest rates being at record lows. At the end of another IMF conference, Olivier Blanchard (2015) took up Summers’ position, arguing that in a context in which there was a chronic excess of saving relative to investment, keeping the economy at its potential rate would require extremely low, or even negative, interest rates. This is a situation, however, that as well as involving low medium-term growth, also implies frequent episodes of financial instability.

Against this backdrop, the effectiveness of monetary policy is constrained not just by the level of interest rates or decisions to implement quantitative easing, but also by the difficulties that are becoming apparent in the monetary policy transmission mechanism. In this context, a more active fiscal policy is therefore needed. As evidenced by the Juncker Plan – to be implemented by mobilising pan-European investments to counteract the risks of stagnation and encourage improvements in business productivity. European

institutions need to be aware of the damage caused by the approach to the crisis adopted from mid-2010 onwards, which, while falling short of stabilising public finances, seriously eroded the euro area’s potential growth. The resulting loss of welfare fuelled public discontent with the process of EU integration and heightened nationalist tensions in certain countries. Bringing plans for common investments in technology and energy networks to fruition should not only make it feasible to achieve growth just below that of 2016 levels, which most analysts estimate at 2.7%, but also facilitate a necessary improvement in the pattern of growth as well as bolstering productivity.

Concluding remarks: The role of political uncertainty

In the current international context, which in no way guarantees adequate growth rates, the Spanish economy is in the midst of its own internal transition owing to the break with the prevailing pattern of government.

The results of the recent general elections have not eliminated the traditional parties, but have enabled new parties to emerge that will need to

So far, financial variables, particularly government bond prices, have not reflected the country’s current political uncertainty, but this situation could change.

be taken into account in the future. New scenarios now exist that make equally novel outcomes possible in the Spanish political scene. However, Spanish and foreign economic agents are justifiably sceptical over the stability of such scenarios, and this is having a negative impact on the investment climate.

So far, financial variables, particularly government bond prices, have not reflected the country’s

current political uncertainty, but this situation could change. The ECB's public debt purchases are undoubtedly significantly moderating the potential negative impact of the difficulties of building a sufficiently stable coalition government. The same obstacles make it difficult to find solutions to the complex dynamics of the situation in Catalonia or adopt decisions to agree new deficit and public debt targets with the authorities in Brussels. The prolongation of these situations may end up producing significant economic and financial impacts, in the event they result in the freezing of investment decisions by Spanish and foreign firms.

It would therefore be desirable for an outcome to emerge in which there was a sufficient majority, notwithstanding its duration, to be able to manage three crucial issues: the situation in Catalonia,

The difficulties in building a sufficiently stable coalition government are also obstacles to finding solutions to complex situations, such as that of Catalonia or the adoption of decisions as regards new deficit and debt targets with EU authorities.

negotiation with the European Commission to relax the 2016 public deficit target and lift the sanctions imposed for breach of the 2015 target, and improve the quality of the country's institutions. A willingness to act on these three fronts is essential to address the other medium-term objective mentioned earlier – modernising the Spanish economy's growth model, which is closely linked to the sustainability of its growth rate and the generation of better quality jobs.

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The European Investment Fund: Challenges and opportunities for Spain

Carmen López Herrera¹

The rollout of the European Fund for Strategic Investments (EFSI), also known as the Juncker Plan, creates attractive investment opportunities for Spain. Taking advantage of these opportunities to support business projects, in collaboration with public authorities, can help boost growth and job creation.

In Europe, the crisis has had a significant, negative impact on investment, which over the medium-term could lead to decreased competitiveness and growth potential. Despite the region's economic recovery, investment remains well below pre-crisis levels, with some countries, such as Spain, particularly affected. Reduced public and private investment funding are hampering development of large-scale projects and growth and innovation efforts of SMEs. In response, the European Commission has launched the European Fund for Strategic Investments (EFSI), or the Juncker Plan, as a tool for reducing this output gap and increasing growth potential. The three pillar strategy is based upon: mobilisation of investment funding through the EFSI, creation of an investment-friendly environment; and, implementation of reforms to support investment in the real economy. The EFSI represents an important opportunity for European growth through allowing for the possibility to leverage private funds with contributions from national governments and European institutions, while allowing for project identification and ownership at the firm level. Spain should continue to take advantage of these facilities as part of its effort to change the economy's growth model and foster sustainable job creation.

The impact of the crisis on investment and loss of competitiveness in the medium-term

The economic crisis has led to job losses and has eroded income in the European Union, particularly along the periphery. Unquestionably, this has an impact on well-being in the short-term; however, it is also important to monitor the impact over a medium-term horizon. Indeed, the crisis has generated a significant investment gap, which

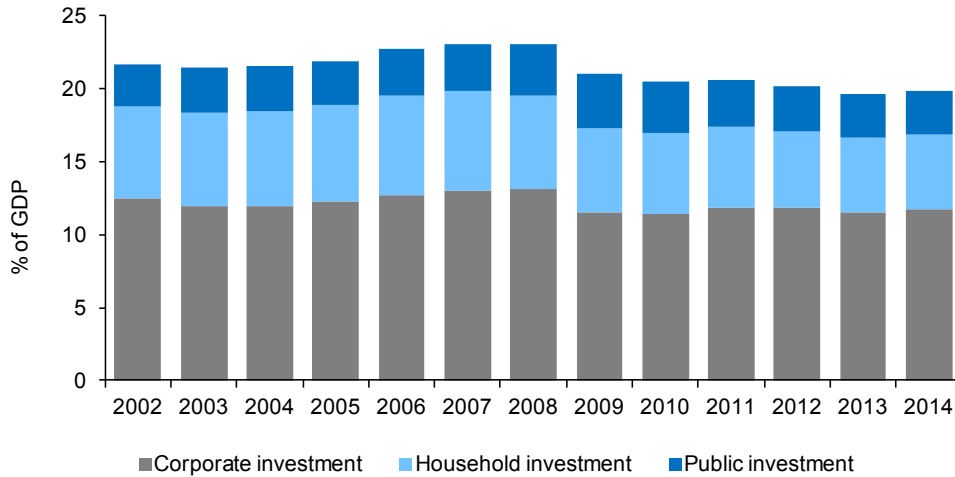
undermines Europe's competitiveness and growth potential.

Despite the fact that the European economies are already staging a recovery, investment remains well below pre-crisis levels and the gap with respect to its potential remains very wide. Spain is the nation, in which investment has contracted the most relative to its closest peers (France and Germany). Between 2008 and 2014, investment has gone from representing 29% of gross domestic product to 20%. However, in Italy, the

¹ A.F.I. - Analistas Financieros Internacionales, S.A.

Exhibit 1

Investment trends in the EU-28



Source: Eurostat.

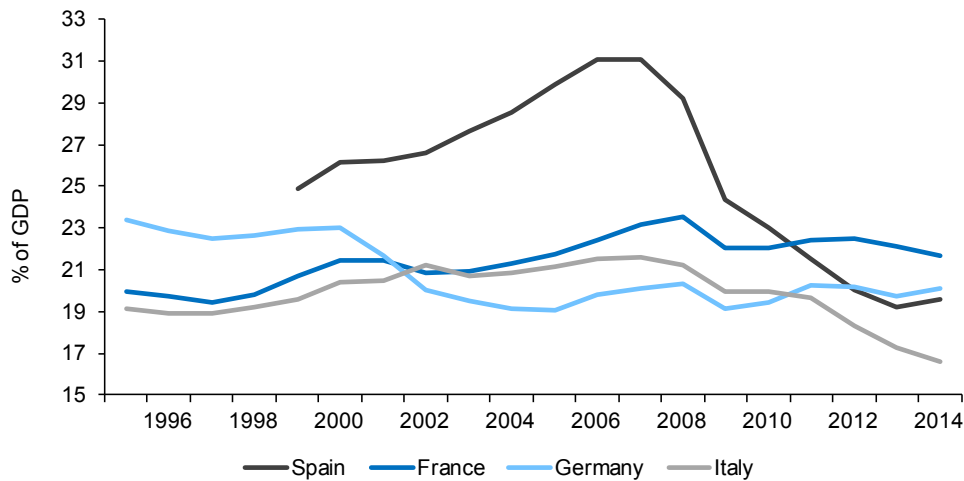
correction in gross capital formation has meant that investment as a percentage of GDP fell to an even lower 17% in 2014.

The drop in investment volumes has been driven by both the fiscal restrictions imposed, particularly

in peripheral nations in an attempt to curb public deficits (public investment has corrected by over 20% in the EU-28 since 2009), as well as lower investment by households and companies due to weak demand, income stagnation and deleveraging.

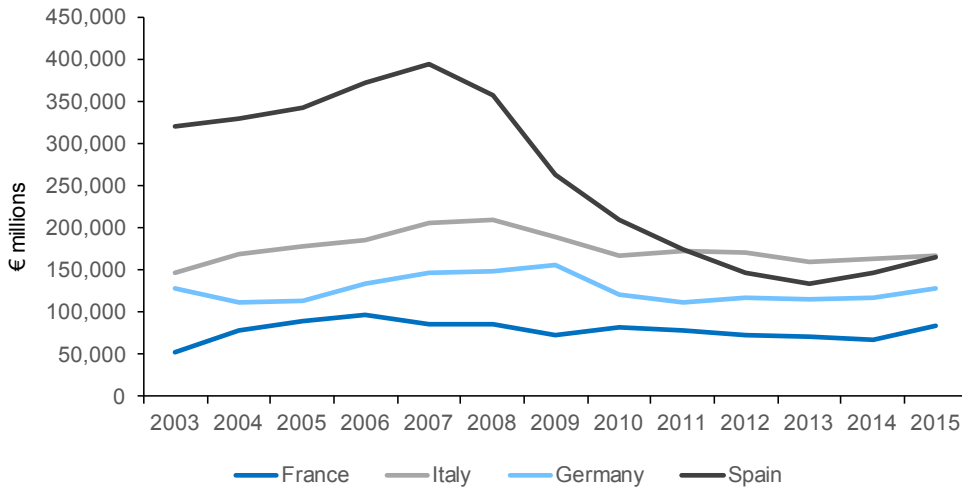
Exhibit 2

Investment trends in the main EU economies



Source: Eurostat.

Exhibit 3

New credit to SMEs

Source: ECB.

The lack of financing has hampered the development of large-scale projects (whether public or private) but has also eroded small and medium sized companies' ability to grow and innovate, given their

Despite the fact that the European economies are already staging a recovery, investment remains well below pre-crisis levels.

dependence on bank financing. The European economy lacks alternative financing sources capable of channelling funds into higher-risk projects, in contrast to Anglo-Saxon markets where incentives for R&D, job creation and entrepreneurship are greater.

Looking at the prospects for credit growth over a longer timeframe, we see that the volume of new loans granted to SMEs by banks, according to the data released by the European Central Bank (ECB), has been stagnant since 2010. Although this trend would appear to be reverting in recent months, marked by an increasingly-evident

recovery in the granting of new loans, the burden borne by the banking sector by the provisioning effort and regulatory requirements is impeding more robust credit growth and therefore dragging down growth.

This dynamic, to the extent long-lasting, would jeopardise delivery of the targets of the Europe 2020 strategy for smart, sustainable and inclusive growth, which is why it is crucial to break, by stimulating demand in true Keynesian style, the vicious circle which could trap the eurozone economy if these conditions were to prove to be protracted.

EFSI structure: Main characteristics

Faced with this situation, in 2014, the President of the European Commission (EC) presented the outline of the roadmap for setting up a fund for stimulating investment and job creation to the European Parliament. This gave rise to the European Fund for Strategic Investments (EFSI), alternatively known as the Juncker Plan, an attempt to redirect the growth model and

conceived of as a tool for delivering a sustained reduction in the output gap as well as an increase in growth potential.

With the aim of achieving these objectives, the Plan was articulated around three pillars:

- Creation of an investment fund (namely, the EFSI).
- Generation of an investment-friendly environment via the European Investment Advisory Hub and the European Investment Project Portal (EIPP).
- Implementation of regulatory reforms in a bid to support investment in the real economy and eliminate non-financial regulatory barriers in key sectors.

The hope is that this public support will facilitate financing in the amount of 315 billion euros (or 2% of EU-28 GDP) over a three-year period, with two-thirds of this sum earmarked to infrastructure and large-scale investment projects and the remainder to SME funding.

As a result, the beneficiaries will be public and private borrowers, in the broadest sense, the following qualifying to apply for funding:

- ✓ entities of all sizes, including SMEs and mid-cap companies;
- ✓ national promotional banks or institutions or banks acting as financial intermediaries;
- ✓ equity/fixed income funds and any other form of collective investment undertaking;
- ✓ investment platforms; and,
- ✓ public-sector entities.

48 Mobilisation of financing for investments via the EFSI

The European Fund for Strategic Investments has been set up in collaboration with the EC and the European Investment Bank (EIB), the Plan's financial arm. The onus is on companies and other organisations looking to raise funding to present their projects to the EIB.

The fund's approach is similar to that of other financial instruments backed by the European Union insofar as it is based on the provision of a public guarantee in order to leverage private resources.

The fund's approach is similar to that of other financial instruments backed by the European Union insofar as it is based on the provision of a public guarantee – funded from the budget of the European Union and by the EIB itself in the order of 21 billion euros – to leverage private resources.

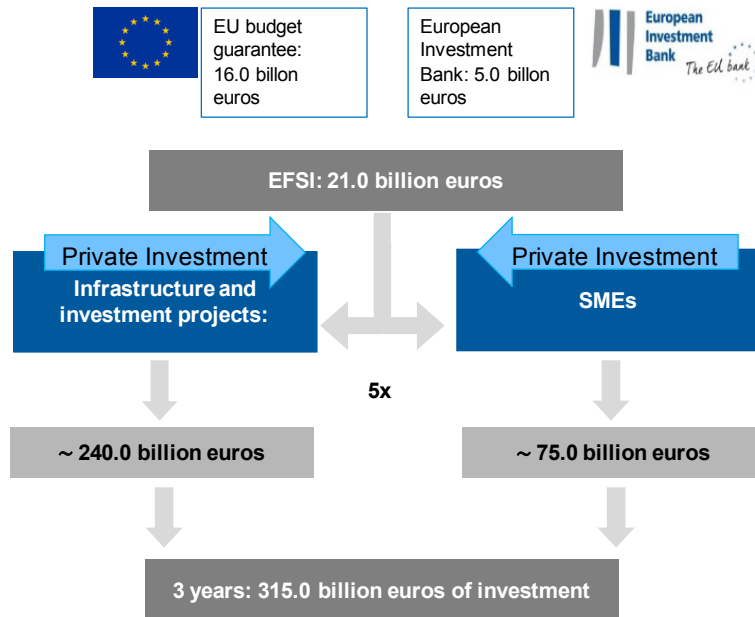
The idea of EFSI is not to have public investment substitute private market finance, but rather to act as a catalyst for collaborative projects that otherwise would not get funded by private investors.

The idea is not, therefore, to have public investment substitute private market finance or products, but rather to act as a catalyst for collaborative projects that otherwise would not get funded by any private investor.

The funds will go to a large number of sectors, albeit emphasising those related to the Europe 2020 strategy: energy efficiency and independence; transport infrastructure; innovative transport equipment and technology, ICT-related projects and companies with fewer than 3,000 employees (particularly SMEs and small mid-cap companies).

Exhibit 4

EFSI financing scheme



Source: AFI, based on EC figures.

In terms of how the EFSI will invest in qualifying projects, the EC has sought to take a flexible approach, which can be tailored for the various projects' individual needs. The products for which support can be provided include:²

- EIB loans, guarantees, counter-guarantees, capital market instruments, any other form of funding or credit enhancement instrument, equity or quasi-equity participations, including in favour of national promotional banks or institutions, investment platforms or funds;
- EIB funding or guarantees to the EFSI enabling it to undertake loans, guarantees, counter-guarantees, any other form of credit enhancement instrument, capital market instruments and equity or quasi-equity

participations, including in favour of national promotional banks or institutions, investment platforms or funds;

- EIB guarantees to national promotional banks or institutions, investment platforms or funds under a counter-guarantee of the EU guarantee.
- Lastly, the EFSI is also structured to contemplate the possibility of investing in European Long-Term Investment Funds³ (ELTIFs).

Creation of an investment-friendly environment

For all the measures being championed under the scope of the current EC mandate to take effect,

² Instruments eligible for coverage by the EU guarantee in accordance with article 10 of EFSI Regulation (Regulation (EU) 2015/1017).

³ Investment vehicles marketed to professional and retail investors in order to fund long-lived financial investments in unlisted European companies and long-term assets, such as real estate and infrastructure projects.

it is crucial to support Europe's companies and publicise the new financing channels put in place. To this end, the EC has created, again together with the EIB, the European Investment Advisory Hub, a platform managed by the EIB to provide access to a series of advisory and technical support programmes and initiatives.

In parallel, work is ongoing on the development of a portal – the European Investment Project Portal (EIPP) – which was slated to be up and running by the beginning of 2016. The portal will publish project details at the request of their developers with the aim of publicising them vis-à-vis potential investors.⁴

Support for investment in the real economy

The Commission has established the objectives of removing barriers to investment and creating a more favourable corporate financing environment. To overcome market failures, it is driving the creation of a Single Digital Market, Energy Union and Capital Markets Union.

All three projects constitute important initiatives for mitigating the fragmentation characterising the European market, which is often signalled by investors as one of the biggest obstacles to investing in the region. Against this backdrop, it is expected that the EFSI will be able to make progress on these aspects by financing cross-border projects and projects implemented by multiple countries in collaboration.

Potential impact for the Spanish economy

Although the cyclical upturn and the expansive monetary policy measures rolled out by the ECB have begun to fuel liquidity and credit supply, Spanish companies continue to call for institutional support to facilitate access to financing.

Since the EFSI has been set in motion, support totalling 5.7 billion euros for 42 projects has been unlocked for infrastructure & innovation, while backing for 84 transactions valued at 1.8 billion euros will be channelled towards SMEs. In both cases, the projects have attracted very significant sums of additional funds ('additionality') – these funds are expected to reach 50 billion euros in aggregate –, implying leverage ratios of 4x for the infrastructure and innovation arm and of 13x for SMEs.

Spain is filing an acceptable number of applications, ranking behind France, Italy and the UK.

Most of the support granted to infrastructure and innovation projects has gone to the energy sector and, to a lesser extent, to transport and RDI projects. In a nutshell, target sectors in terms of shaping a more productive growth model and boosting innovative sectors that strengthen European market union.

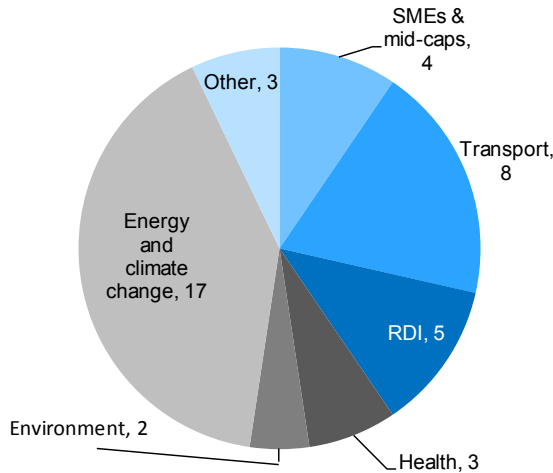
In Spain, the pace of applications is acceptable, albeit trailing that of France, Italy and the UK. Although the amount applied for in the infrastructure and innovation segment is similar to that requested by the above-listed countries, there is room for improvement in terms of applications by or on behalf of SMEs. Compared to funding deals for six infrastructure projects (for 515 million euros, expected to generate an aggregate investment volume of 1.6 billion euros), just three SME agreements have been entered into with financial intermediaries via the European Investment Fund (EIF) for 72 million euros (expected to generate ultimate investment of 731 million euros).

It is worth noting that there are no country quotas; this could lead to more competitive countries

⁴ Publication of project details on this website does not guarantee receipt of EFSI funding.

Exhibit 5

Use of proceeds granted by the EFSI to February 2016



Source: EC.

taking up a disproportionate share of the financing, a development that would be counter-productive in term of fostering convergence across countries and regions. This should be taken into account in Spain, particularly with respect to the funding earmarked for SMEs given their small average size (53% of Spanish SME's have no employees and just 0.1% have more than 250).⁵

Lastly, recall that EFSI support can be complemented by other existing funds (whether or not derived from structural funds) devoted to stimulating corporate investment, particularly those targeted at small and medium-sized enterprises, such as:

- At the national level: The enterprise, entrepreneur and guarantee credit lines offered by Spain's public credit institution, ICO, (such as FOND-ICO Pyme, ICO Innovación Fondo Tecnológico and Línea JEREMIE) and the facilities granted by the Centre for the Development of Industrial Technology (CDTI) for research, development and innovation projects.

- At the community level: the SME Initiative (financing aimed at the provision of guarantees to financial intermediaries consisting of the provision of partial coverage of portfolios of loans extended to eligible SMEs), the InnovFin lines (with two tranches, depending on project size, which can take the form of loans or guarantees) and financing under the scope of the COSME programme for competitiveness of enterprises and SMEs.

Conclusions

There is a broad spectrum of facilities already on offer in the marketplace which complement the EFSI. Spain should take advantage of these facilities as part of its effort to change the economy's productive model and foster sustained job creation in the wake of the collapse of the real estate bubble. Although the scale of the so-called Juncker Plan is limited relative to the size of the European economy, it is probably the most ambitious initiative on the horizon in terms of breaking the pattern of sluggish growth. All the more so considering the fact that the budget restrictions imposed by the fiscal consolidation effort, still incomplete in most countries, will curb large-scale public investment.

Against this backdrop, the EFSI creates the chance to leverage private funding with contributions from national governments and European institutions, while allowing for project identification and ownership at the enterprise level. It is clear that this strategy marks a change in the role of public fund managers and calls for a welcome assessment, using impact and return criteria, of infrastructure projects so that they successfully draw investor interest.

The existing paradox, shaped by abundant liquidity in Europe coupled with investors' inability to identify sufficiently attractive projects (to justify reallocation of money held in risk-free assets

⁵ The INE's *Central Company Directory* (DIRCE). Data as of January 1st, 2014.

carrying negative interest) must be reverted. In this context, the role of the public sector, in concert with the financial sector, should be redirected towards signalling priorities from an economic and social optic with a view to boosting productivity and social cohesion. From this perspective, it will be far more important for the authorities to facilitate project structuring in collaboration with the private sector by designing vehicles and platforms capable of channelling the interests of various investors as a function of the risk they are willing to assume than to devote funds directly to gross capital formation.

This is the chance to revitalise public-private partnerships by innovating, studying success stories and drawing lessons from the numerous experiences which have ultimately ended up frustrating private backers and government authorities alike. Particularly the latter, which have seen their debt burden increase (causing unanticipated imbalances) as a consequence of inaccurate demand estimates and/or ill-advised allocation of risks. The Plan is not targeted at member states' central governments, but rather at regional and local governments, together with enterprises, which must attract the interest of investors to fund projects with the capacity to stimulate the economy and creating stable, quality employment.

Challenges ahead for the banking industry

Carlos Ocaña¹ and Alice Faibishenko²

A unique macro environment, stricter regulation and technology-related disruptive change represent the main actual and forthcoming challenges for the banking industry. Banks' adaptation strategies in response to these challenges will likely forge a new industry structure.

A unique macro environment, characterized by a prolonged period of low interest rates, pressing regulation mainly based on higher capital requirements and technology-related disruptive change are the main actual and forthcoming challenges for the banking industry. Some of these pressures, low interest rates for instance, are especially intense in the case of the Spanish banking sector, given its high degree of reliance on the traditional banking model. Meanwhile, the negative implications arising out of increased capital requirements appear to be more manageable for most Spanish banks. Both global and Spanish banks' adaptation strategies in response to these challenges will likely forge a new industry structure and financial innovation technologies should be an important part of it.

Financial crises are not uncommon. In the event that they occur, they are usually accompanied by restructuring and regulatory reform in the financial sector. However, in their wake, the sector generally returns to a pre-crisis equilibrium. After the latest financial crisis, however, we are looking at a very different future for banks, the banking business model and their industry structure.

Pressure on the banking industry today is increasing considerably due to a combination of three main forces acting across different time dimensions:

- In the short-run, a unique macro environment, characterized by very low interest rates, negatively affecting banks' profitability,
- In the medium-term, new and notably more stringent regulation and supervision, intensifying

profitability challenges, and possibly reducing lending; and finally,

- Over the long-run, technology-related disruption, such as the rise of alternative lending and distributed ledger technology (*i.e. Blockchain*), which is increasingly obligating banks to adapt their business models and allowing for new competitors to enter the traditional banking scene.

All of this is taking place in an environment where banks are rebuilding their reputation following the damage it has suffered during the crisis. Reputation building post-crisis is an area where banks will have to continue to focus if they want to overcome the negative impact the financial crisis has had on their public image, as well as

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² Funcas.

capture next generation (Millennial) clients, who are increasingly in favour of by-passing traditional banking.

In this context, the banking industry is devoting significant attention to the profitability pressures arising from the unique macroeconomic environment. However, more consideration should also be given to the potential implications of regulatory and technology related changes, which are equally important and permanent. It is precisely these future challenges that have the potential to be much more disruptive than what we have seen in recent history and could change the structure of the financial industry. This implies that, among other things, to improve its outlook, the banking sector must increase efficiency and new technologies should be an important part of this process.

The remainder of this article will focus on each of the three forces outlined above and on how they will likely affect the banking industry in general, with the final pages paying particular attention to the situation in Spain.

Unique macro conditions are affecting profitability in the short-term

The banking industry's most pressing concern is how to increase profitability in an environment of persistently low (in some cases zero or negative) interest rates observable across the majority of advanced economies.

One factor often blamed for lower profitability levels today relative to before the crisis is the current low interest rate environment under the so-called 'New Normal'. In the wake of the financial crisis, the global economy remains in a period of uncertainty often referred to as the 'New Normal' – initially defined as a time of low, but predictable growth. Economists have many differing views about the 'New Normal'. In general, however, where there is consensus is on the fact that low real interest rates are likely to persist for some time into the future, creating a series of economic policy challenges.

Current low interest rate conditions have a particularly negative impact on the profitability of smaller banks. Smaller banks are typically more reliant on traditional lending, making it harder for them to compensate for lower interest margins through other activities, *i.e.* M&A and trading.

Nevertheless, historical evidence suggests that banks are more sensitive to overall economic conditions than to monetary policy. Improvement in unemployment levels, GDP growth, the housing market and other asset prices in response to monetary easing are determining factors for bank

Improvement in unemployment levels, GDP growth, the housing market and other asset prices in response to monetary easing are determining factors for bank profitability and could ultimately compensate decreased margins resulting from a QE style monetary approach.

profitability and could ultimately compensate decreased margins resulting from a QE style monetary policy approach (Genay and Podjasek, 2014).

At the same time, the low interest rate environment has had other noteworthy implications on the banking industry as banks adopt strategies to offset lower interest margins. Some banks have attempted to increase profits through decreased provisions, higher commissions and trading gains, while other banks have become more selective in their lending. The low growth, low interest rate environment is also fueling a search for yield, inciting financing entities to take on greater risk.

Stricter regulation will likely affect profitability and lending capacity in the medium-term

The adoption of stricter financial regulation, largely in the form of increased capital, leverage,

and liquidity requirements, is expected to place additional strains on profitability and lending as banks struggle to fall in line with new obligations. At the same time, additional pressures will likely arise from new resolution (bail-in) rules at the EU and G20 level. Ultimately, banks' adaptation strategies to comply with new regulation will likely entail significant changes to industry structure.

Regulators require more solvency and more capital, while investors seek to maximize profits and policy makers want more credit flowing to the economy. These objectives are not entirely compatible.

Regulators require more solvency and more capital, while investors seek to maximize profits and policy makers want more credit flowing to the economy. These objectives are not entirely compatible. The new measures do not come free of cost, bringing with them consequences for the financial sector, and depending on banks' responses in terms of credit supply, potential impact on the real economy – although most studies show that at Basel III stipulated capital levels (a minimum of 7% relative to the 2% required under Basel II), benefits outweigh costs.

Such a conclusion is presented in recent studies by the Basel Committee on Banking Supervision (BCBS) and the European Commission, which provide a cost-benefit analysis of the increase in regulatory capital. Complementary studies which identify optimal capital ratios, defined as those which maximize the benefits in relation to costs, point to ratios above those of Basel III (Peña, 2015).

There will likely be unintended consequences of multiple capital, liquidity, leverage requirements, together with other regulatory changes, on bank profitability and the provision of long-term financing as banks either increase capital or reduce activity to comply with new obligations.

Stricter regulation will likely impact banks on three levels: profitability, credit growth and business model/industry structure.

Impact on profitability

Increased capital requirements and high return on equity (ROE) objectives do not appear to be compatible. The principal objective of any bank is to maximize shareholder value and profitability. ROE is a good proxy of return on shareholder investment. Under higher capital requirements, most analysts believe that there will be a reduction in ROE as the cost of capital increases. There are two reasons for the increased cost of capital under the new regulatory regime. Even at constant prices, increased capital requirements would translate to a higher overall cost of capital. At the same time, investor concerns over bank profitability are increasing pressures on banks' funding costs, making capital more expensive. Compliance with liquidity target ratios may also reduce bank profitability, requiring balance sheet changes aimed to increase holdings of higher quality (*i.e.* lower yielding), more liquid assets, as well as longer-term, more stable wholesale and retail deposits.

Impact on credit growth

As noted above, the estimated benefits of Basel III implementation are anticipated to outweigh the costs. However, the additional costs are expected to have an impact on the availability and conditions of credit to the private sector.

Under more stringent capital requirements, many banks may become more selective lenders or even reduce their lending activity in order to comply with regulatory demands. According to preliminary IMF studies, higher capital requirements in response to Basel III would raise the marginal funding costs for banks, leading large banks to increase lending rates and in turn reducing loan growth over the longer term - although results may vary

considerably between countries. (Cosimano and Hakura, 2011). As an example, American banks spent \$70.2 billion (as of the end of 2013) to comply with the new regulation (Peña, 2015). All of this is expected to impact credit recovery.

Impact on business models and industry structure

The new regulatory requirements are changing the business model of banks as they adopt strategies to cope with the impact of the new measures. These include a revision of the types of products and services offered, cost reductions, balance sheet reductions, moving certain activities to the “shadow-banking” sector and divestiture of non-strategic activities.

Other responses include ring-fencing (as in the case of HSBC in the UK, prior to the entry into force of regulatory measures addressing this issue in 2019. At the European level, proposals including some form of ring-fencing are under consideration but have not yet been approved.) Finally, some banks may shift their geographical mix, trying to take advantage of different calendars for Basel III implementation across different regions.

Disruptive technological change will present opportunities and threats in the longer term

In addition to the complexities of operating in a low interest rate environment with increased regulatory burden, today’s banks face an additional

Already significant, in the future, FinTech is expected to have profound transformational impacts on the way banks do business.

challenge – how to confront the emergence of new, disruptive technological changes. Digitalization and the penetration of non-bank financial service providers is on the rise globally. New financial

innovation technologies (FinTech) all pose distinct opportunities and threats to the traditional banking sector, as new competitors emerge on the scene. Already significant, in the future, FinTech is expected to have profound transformational impacts on the way banks do business. Banks’ will have to adjust quickly to the digital age or risk finding themselves behind the competition.

Some of the fastest growing financial innovation technologies, presenting both opportunities and challenges, include alternative lending channels, such as P2P lending and DLT. Peer to Peer lending (P2P) connects lenders and borrowers directly at lower costs, presenting both challenges and opportunities for traditional financial intermediation. Distributed Ledger Technologies, or DLTs (*i.e. Blockchain*, the technology behind cryptocurrency *Bitcoin*) allow for decentralized transactions and a reduction of infrastructure costs.

It is worth pointing out that these new platforms are only examples of the range of emerging FinTech innovation, some of which is already more broadly in use across the financial sector, such as mobile or Internet banking. At present, nobody knows what will be the ultimate impact or speed at which these technologies will be implemented, but competitive pressures are forcing banks to invest in them. Moreover, as the process of bank digitalization accelerates, we may expect a decreased demand for physical and human banking resources, such as branches and/or employees.

Technology-driven industry changes

As the digital age becomes an ever increasing reality for the banking sector, structural changes can be expected as banks try to keep up with non-bank competition. We are already seeing and should continue to see greater cooperation between banks with digital partners, through acquisitions or integration of new technologies; increased investment in digital initiatives, such as mobile or online banking; and, integration of FinTech innovation with traditional business to improve customer services and products.

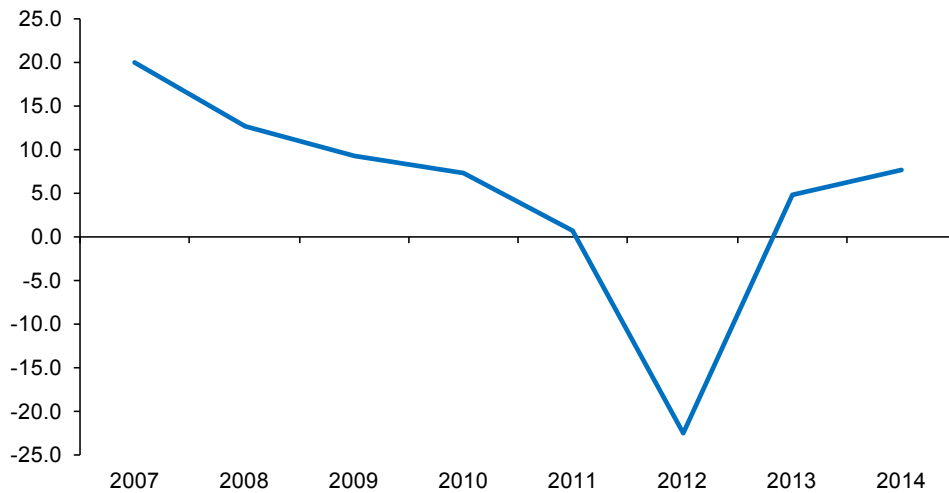
Perspectives on the Spanish banking sector

As expected, the low interest rate environment, stricter regulatory requirements and the rise of

new technologies in the banking industry will have implications on profitability, lending and the future landscape of the Spanish banking sector. Challenging macroeconomic conditions, together with the need to clean up banks' balance sheets

Exhibit 1

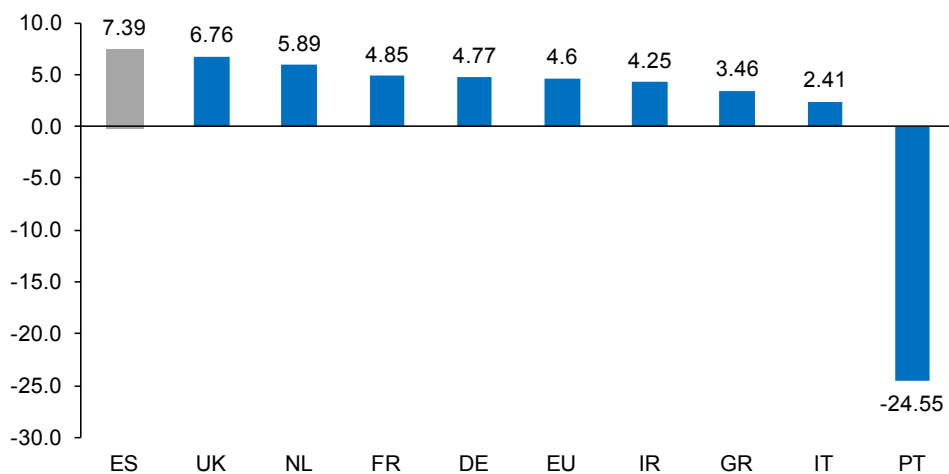
Historical ROE for Spain, Consolidated groups (Percentage)



Source: Bank of Spain.

Exhibit 2

Comparative ROE data for EU and Spain, June 2014 (Percentage)



Source: ECB.

in the wake of the crisis, catalyzed an intense adjustment process with the objective of improving the financial health and efficiency of Spanish financial entities. The results of this process include: a series of mergers and acquisitions within the sector; divestiture or reduction in assets and/or activities deemed non-profitable, in particular, a reduction in installed capacity most acute in the area of retail branches; a largescale provisioning effort (according to the Bank of Spain, since the beginning of the crisis, in 2008, the Spanish banking sector allocated more than 200 billion euros in provision, that, if combined with other resources assigned to provisions, add up to 330 billion, equivalent to slightly above one third of Spain's GDP); and, recapitalizations, in some instances through reliance on private investors, while in others (as in the case of nationalized institutions) through reliance on public funds.

The question that remains is – how far along is the Spanish financial sector in the adjustment process and what remains to be done. The following sections provide some insights on the state of play.

Profitability improving but bumpy road ahead

After suffering notable declines during the crisis years, as shown in Exhibit 1, Spanish banks' profitability indicators through the end of 2014 confirm a modest recovery. Profitability returned in 2013, after suffering losses in 2011 and 2012, and has since remained in positive territory.

On a comparative basis, Exhibit 2, based on the latest available data from the ECB through June 2014, shows Spain's ROE is currently above most large EU banking sectors, as well as the EU average.

This relatively high profitability may seem surprising, given that the sector was one of the more severely affected by the crisis. Moreover, repeated claims by the Bank of Spain and the ECB highlighting profitability concerns also point to the

contrary. However, this apparent paradox can be explained by a number of factors. For instance, in addition to benefitting from better domestic economic conditions, the improvement in Spanish banks' profitability is largely attributable to the decline in provisions, together with cost savings through lower funding costs and efficiency gains.

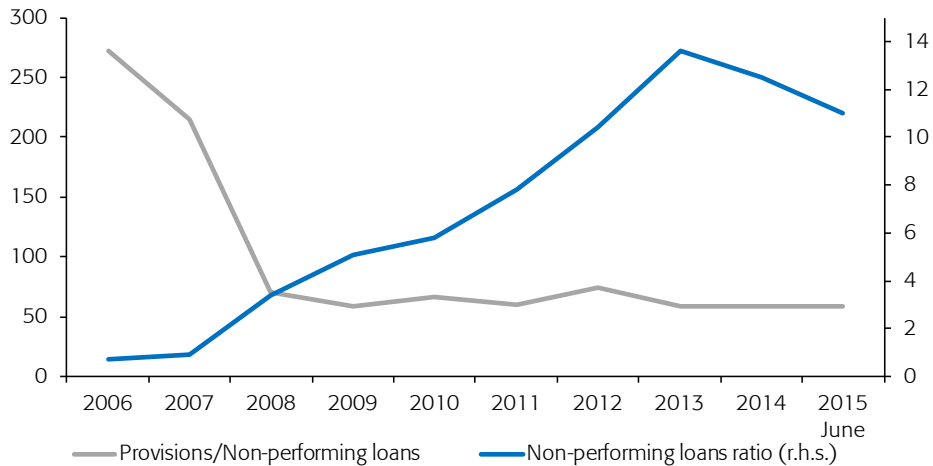
Asset disposals and improvement in NPL ratios have resulted in a significant decrease in provisions. According to several analysts, including Standard

The relatively high profitability of the Spanish banking sector as a whole may seem surprising, given that it was among the more severely affected by the crisis. Moreover, repeated claims by the Bank of Spain and the ECB highlighting profitability concerns also point to the contrary.

and Poor's, *unlike some other EU banking sectors, Spanish banks frontloaded their provisioning effort as a means of restoring confidence to the Spanish financial system at the height of the crisis, allowing them to reap the benefits of this strategy in the following years until today* (See Exhibit 3). This, in turn, has reduced the cost of risk, and helped to somewhat ease profitability pressures. Additionally, banks' funding has also become less expensive, more stable and more diversified than at the peak of the crisis, in part due to deposit and wholesale costs having come down and access to both types of funding having improved.

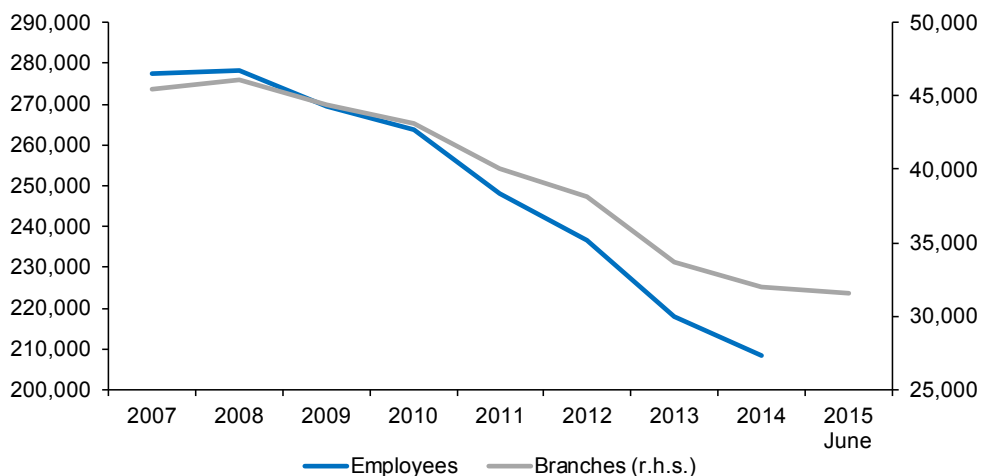
As shown in Exhibit 4, efficiency gains throughout the consolidation process, the reduction of employees and branches, for example, have also helped to secure further cost cuts to compensate for compression of interest margins. According to the Bank of Spain, since the start of the crisis, there has been a reduction in branches, employees, and banking groups of 30%, 25%, and 40%, respectively (Bank of Spain, 2015b). As

Exhibit 3

Provisions in the banking system

Source: Bank of Spain.

Exhibit 4

Employee and branch reductions

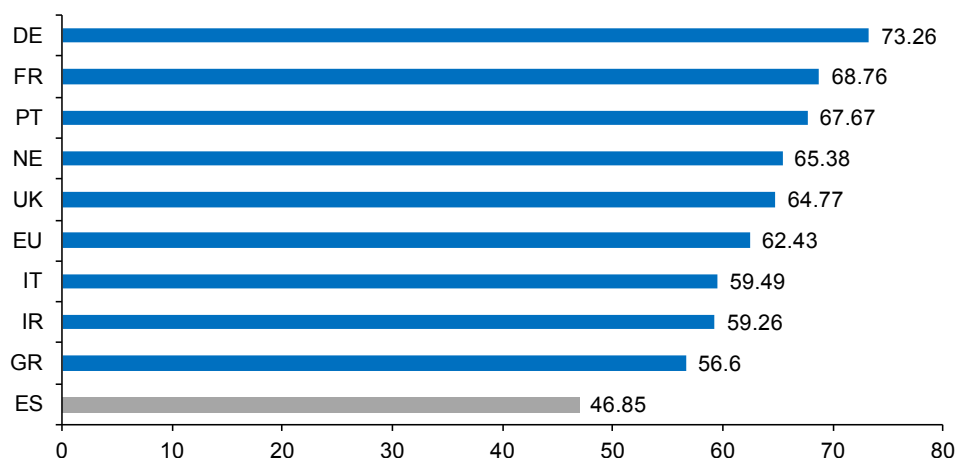
Source: Bank of Spain.

a result of a combination of these factors, as we see in Exhibit 5, Spanish banks' cost to income ratios today are among the lowest in Europe (Maudos, 2015).

Despite the improvements mentioned above, Spanish bank profitability remains below levels needed to secure long-term sustainability and should continue to improve over the medium-term.

Exhibit 5

EU comparative cost to income ratio, June 2014 (Percentage)



Source: ECB.

Under improved prospects for the sector, Spanish banks are well-positioned to benefit from euro depreciation and the economic cycle. However, future profitability of the Spanish banking system faces major challenges and risks.

Low interest rates, weak credit demand and concerns over the quality of Spanish banks' loan portfolios constitute some of the key challenges for profitability over the coming years.

The low interest rate environment poses a particularly relevant threat to Spanish banks' profitability given their high exposure to retail lending and to floating rate mortgages. Under the falling interest rate scenario, the latter are being reset at lower rates simultaneously with the elimination on interest rate "floors clauses" on some mortgage loans (IMF, 2014). Moreover, as recently pointed out by the Bank of Spain, despite improvement, low interest rates are reducing Spanish banks' profitability as they result in ROE below estimated cost of capital. Furthermore, the sustainability of margins depends on sufficient banking activity to compensate for the reduction in prices. While activity is increasing, it

remains today at reduced levels. Finally, although the economic recovery has helped bring about a reduction in NPLs, NPL ratios and the volume of foreclosed and impaired assets on banks' balance sheets remain high (Bank of Spain, 2015b). The European Commission (EC) raises further attention to this issue in its ex-post evaluation of Spain's financial assistance program. According to the EC, despite the significant reduction in the absolute value of NPLs, the quality of banks' loan portfolios remains weak as reflected in NPL ratios above 10% of total loans (EC, 2016).

The recent profitability improvement also masks remaining weaknesses in some of the banks and there is wide variation across entities. Recent data show several banks recorded ROE close to 3%, while others, among them the larger, more internationally diversified banks, recorded levels significantly above the sector average. As highlighted by the Bank of Spain in its latest Financial Stability Report, profitability for the sector as a whole has also been supported by the international activity of some of the larger banking groups (Bank of Spain, 2015a). At the same time, as the IMF points out, the deteriorating

outlook for EM may cause some instability for banks' with significant exposure to these markets, in particular in Latin America, although exposures elsewhere should provide some diversification against these risks (IMF, 2014).

Finally, banks were also able to record capital gains from earnings obtained from the carry trade, where lower interest rate ECB funds were used to finance public debt purchases – a strategy that will be difficult to repeat in the context of expected sovereign spread compression.

Regulatory burden appears manageable

The level of capitalization of the Spanish banking system has significantly improved. Nevertheless, solvency levels remain below the majority of European peers and some banks may tap capital markets in the near-term to compensate for the anticipated phasing out of certain instruments currently still qualifying as regulatory capital.

Capital injections and loan-loss provisions (in 2012 and 2013 in the case of the former and since

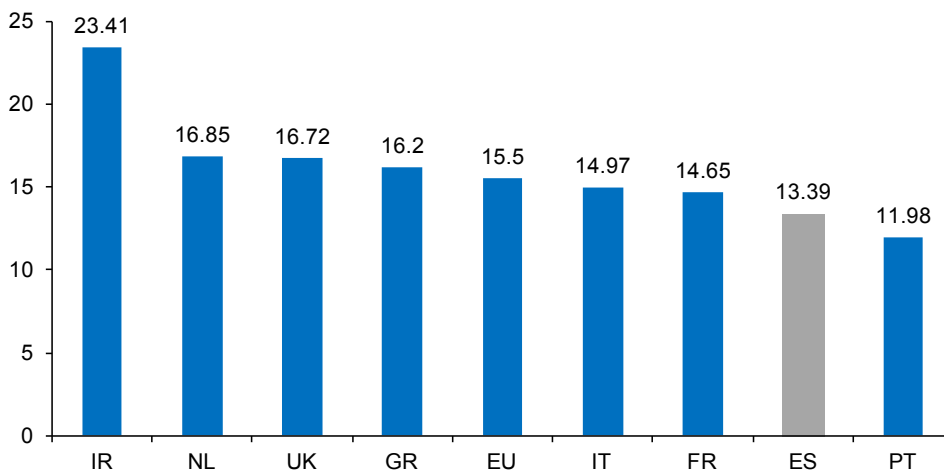
2008 in the case of the latter), together with other balance sheet adjustments, allowed the Spanish banks to pass the 2014 stress tests conducted by the ECB and EBA.

As of June 2015, latest available data confirm that the Spanish banking sector's solvency levels are above the minimum regulatory levels required. At June 2015, the common equity tier 1 (CET1) of Spanish deposit institutions stood at 12.4%, over 80 basis points above the June 2014 level, above the minimum regulatory requirement of 4.5%. The total capital ratio stood at 14.3% at June 2015, increasing similarly to the CET1 ratio from June 2014 and also above the 8% required level (Bank of Spain, 2015a). As regards the ECB's solvency requirements for the coming year, most banks that have published their results appear to be in line with stipulated ratios.

While capital ratios across the Spanish banking sector have improved, they remain below most of their European peers (See Exhibit 6). Also, as in the case of profitability, the sector average covers up lower CET1 ratios recorded by some

Exhibit 6

Comparative EU and Spanish solvency, June 2014



Source: ECB.

entities, which for example have levels near 10%, or notably below the 12.4 average (EC, 2016).

Moreover, the Bank of Spain just set requirements at end-December of a 0% countercyclical buffer and between 0-0.25% for systemically important institutions. In addition, European regulators seem to be more eager for EU banks to increase capital requirements closer in line with the new Basel III ratios than their US counterparts. These considerations, together with anticipation that regulators will continue to phase out from capital

The impact of Basel III on the Spanish banking system, at least over the near to medium term, is expected to be less burdensome than for some other financial systems due to the typically lower risk profile of most Spanish banks and their reliance on a more traditional banking model.

considerations assets currently still considered high quality capital, could mean that some Spanish banks may choose to boost capital ahead of the end of the Basel III implementation period. This will probably take place this year through some banks tapping Additional Tier 1 (AT1) markets. Further capital increase may also take place should some of the former *Cajas* raise fresh capital in an effort to dilute the controlling stake of the banking foundations that own them (Standard and Poor's, 2016).

On the whole, the impact of Basel III on the Spanish banking system, at least over the near to medium term, is expected to be less burdensome than for some other financial systems due to the typically lower risk profile of most Spanish banks and their reliance on a more traditional banking model. The challenges they will face for profitability and credit growth will be more related to economic conditions and the impact of deleveraging on new credit flows.

Digitalization not far away from most European peers but room for improvement in penetration of alternative finance

Digitalization trends

Over the next few years, the implications of the digital disruption on banks' bottom lines are going to be huge. McKinsey estimates that at present, only 10 percent of the revenues of a typical European bank are subject to digital disruption, defined as a majority of new revenue being derived from either online or mobile channels. As shown in Exhibit 7, by 2018, this figure is expected to rise to above 50% in many major geographic areas, with products such as loans and payment services particularly affected (McKinsey, 2015).

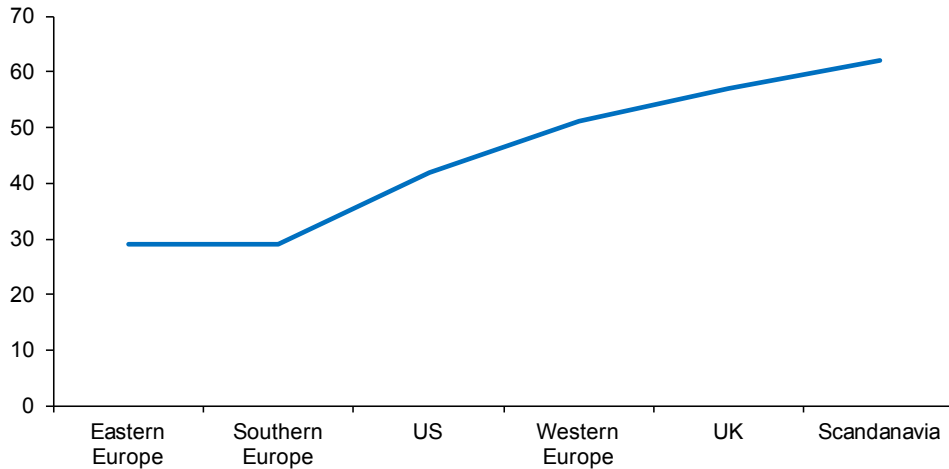
In Europe, however, many retail banks have digitized only 20 to 40 percent of their processes; 90 percent of European banks invest less than 0.5 percent of their total spending on digital (McKinsey, 2014).

Although there is not a great deal of reliable information allowing us to quantify the level of digitalization in Spain, industry experts agree that outside of some of the Nordic countries and the UK, Spanish banks' level of digitalization is in line with most of its European counterparts. Nevertheless, there are obvious differences among the level of digitalization among the smaller Spanish banks relative to larger institutions, who are generally more innovative in this space. Despite the fact that the costs of digitalization are typically scalable and cost-efficient for small institutions, smaller banks appear to be lagging behind their larger competitors, in part due to cultural differences and less flexibility in management of existing resources.

According to a recent survey report published by IESE Business School and Synpulse management consulting firm, which surveyed 40% of the Spanish banking population in the first quarter of 2015, many banks appear to have planned and begun executing a digital strategy. However, there are some identified gaps between

Exhibit 7

Estimated global digital revenue penetration by 2018 (Percentage)



Source: McKinsey & Co.

Spanish banks' intentions on the one hand and transformation readiness on the other, such as: still heavy reliance on physical branches rather than automated channels to manage customer relationships; complex, outdated IT platforms that lack the required agility for digital IT transformation; and, too great a focus on digitalization of back-end operations, rather than front-end customer operations and services (IESE, Synpulse, 2015). Finally, regulatory uncertainty and lack of regulatory coordination across the EU is further complicating the transition to a digital financial services economy in Spain and in Europe as a whole. In the meanwhile, as regards adoption of new technologies, taking as an example the case of DLT, in the words of a former central banker, *they must be allowed to develop and industry players able to experiment without risk. In a country like Spain, where the administrative burden is high, DLT could be very important.*

Penetration by non-bank financial service providers

In Spain, empirical evidence reveals that penetration of non-financial services players is still

quite low. According to BBVA Research, *whether a factor of the regulatory climate, customer profiles (distrust or lack of awareness over alternative financing sources), or a combination of all of these factors, Spain remains primarily reliant on traditional banking intermediation services to a higher degree than many of its EU peers.*

In sum, the process of bank digitalization in Spain appears in line with most of its EU counterparts, although UK and Nordic countries are perceived to have more highly digitalized banking services. At the same time, non-financial service providers' penetration levels in Spain appear to be below that of other EU peers, mostly as a function of the competitive advantage maintained by Spanish banks, together with customer preferences.

Conclusion

The current pressures on the global and Spanish financial system are intense. At the macro level, the principal challenge for the financial industry remains the unique macro environment, characterized by a prolonged period of low interest rates and the implications for banks' profitability.

At the regulatory level, in the wake of the crisis, the need for stricter financial regulation, largely in the form of higher capital requirements and supervision, is adding pressures to banks' bottom lines, and could restrict lending.

Finally, technological change, such as the rise of alternative finance and distributed ledger technologies are also playing a disruptive role by increasing competition against the traditional banking model, introducing both threats and opportunities.

All of these factors combine with the fact that financial entities today are fighting to reestablish their public image.

For the case of the Spanish banking sector, some of these pressures, such as low interest rates, are particularly intense, given reliance on the retail focused, traditional banking model. At the same time, the traditional model works in favour of the Spanish banking system as regards reducing negative implications on profitability from increased capital requirements.

In the current environment, Spanish banks will have to reassess, rethink, and reshape their business models to further increase profitability and face regulatory challenges, in part by taking advantage of their competitive position to break into new areas, such as alternative lending and other financially innovative technologies.

The strategies adopted by banks should include additional efficiency gains, and changes to their existing business models through, among other things, the divestiture of non-profitable assets/activities and the adoption of new technologies and strategies to counteract some of the pressures to which they are currently being subjected.

Although the recent restructuring process has resulted in a considerable consolidation of the Spanish banking sector, low profitability levels could prompt another round of consolidations – in

line with recommendations from both Spanish and European regulators. Nevertheless, under current circumstances, these changes are unlikely to be imminent nor do we expect their impact on the sector to be particularly transformational.

Moreover, as pointed out by Carbó y Rodríguez (2016), *at the geographical scale at which retail financial services compete, the degree of concentration is not as important as the contestability or competitive intensity between rivals at the provincial or regional level.*

This suggests that banks should contemplate alternatives in addition to consolidation as a means of improving their profitability as well as addressing other outstanding challenges.

Finally, Spanish banks must not fall into complacency. They must maintain their competitive advantage within the Spanish retail banking system, but at the same time move forward on initiated deep structural reform, maximize recovery value from the sale of entities still under control by the FROB, complete the restructuring process and continue with efforts to improve the overall quality of their balance sheets. In parallel, the SAREB should continue to move forward with its objective of management and selling of distressed assets. This should allow for the emergence of a stronger, more efficient and more resilient financial sector for the future.

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The Spanish banking sector in the financial turbulence of 2016

Santiago Carbó Valverde¹ and Francisco Rodríguez Fernández²

In the context of a difficult start to 2016, the Spanish banking sectors' recent performance on profitability and solvency indicators has been positive and transparency has improved. As the outlook ahead remains equally complex, banks in Spain and in Europe will have to adopt transformational changes across key areas to remain competitive.

The markets got off to a somewhat turbulent start in 2016, with the European banking sector among the worst affected. Doubts have arisen about the quality of assets held by some of Germany's systemically important institutions, and countries, such as Italy, have had to take steps to address a spiralling default rate. Although the loss in value in early 2016 was spread across Europe, there have been some noteworthy positive developments for the Spanish banking sector. Spanish banks' profits have risen –the six largest Spanish banks increased their joint profits in 2015 by 8.1% relative to the previous year. Their solvency has improved – banks' fully-loaded core tier 1 capital (CET1) ratio rose from 10.9% in 2014 to 12.2% in 2015. Private sector credit growth is expected to return to positive figures in 2016. Finally, Spanish banks may benefit in the medium-term relative to their peers elsewhere thanks to the enhanced transparency exercises undertaken. The outlook remains challenging and both the European and Spanish banking sectors will have to adopt transformational changes across key areas to realign themselves with the new paradigm.

A difficult start to the year: Market and regulatory pressure

European financial markets got off to a fairly tough start this year and the banks were among the worst affected. Against this backdrop, other factors arose that were unfavourable to the sector's outlook, such as the threat of the United Kingdom's leaving the European Union, or doubts about the situation and solvency of certain

financial institutions in Italy and Germany. In January alone, the European sector index for the continent's banks registered a loss of value of 350 billion euros.

The unique macroeconomic situation further complicated matters. While expansionary monetary policy has undoubtedly made it easier for banks to obtain liquidity, the sharp drop in interest rates –with some inter-bank rates even

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turning negative— has put interest margins under intense pressure, heightening European banks' difficulties, although shared in part by banks elsewhere.

In January alone, the European sector index for the continent's banks registered a loss of value of 350 billion euros.

In any event, as Benoît Cœuré, Member of the Executive Board of the European Central Bank, recently noted, interest rates are not the only challenge the banks are facing. Non-performing loans and the sector's lack of consolidation are the main factors creating uncertainty for the banks.³

Moreover, market volatility is a response to a series of factors beyond banking activity, including uncertainty over China and emerging markets and the upheaval in energy markets, with the slump in oil prices.

Doubts also persist as to the European economy's ability to take off in an environment in which monetary policy is running out of room to manoeuvre and there is little sign of any political will for coordinated expansionary policies. As regards the factors intrinsic to the banking market, the quality of some systemic European banks' balance sheets is still questionable, while in some countries, such as Italy, a new asset management company has even been created (a "bad bank"), given the aggregate scale of its non-performing loans.

The crisis also highlighted the existence of excess capacity in the European banking industry. Restructuring thus became the main mechanism for rebalancing supply and demand. However, these processes have been very uneven and in many countries there is still a lot to do. What is

more, it has become apparent that the major bail-outs in 2008, not being accompanied by significant restructuring, have delayed many institutions' return to profitability, resulting in these institutions ended 2015 with significant losses. Some of these institutions now face significant adjustments to be realized through branch closures and staff cuts.

An additional factor significantly impacting market perceptions of European banks' is regulatory pressure. Regulatory pressure can only be expected to increase, given the supervisory shortcomings and inadequate solvency requirements uncovered during the financial crisis. However, the impact that these requirements may be having on the banking sector's capacity to increase credit flows and stimulate productive investment has perhaps not been sufficiently gauged. Although this issue deserves more thorough analysis – beyond the scope of this article – there is no doubt that the discussion of how strict regulatory requirements should be is back at the top of the agenda.

It is also worth asking to what extent the European Banking Union, in its current design, is functioning. On February 22nd, 2016, with the help of competent national authorities, the Single Resolution Mechanism (SRM) began to collect data with which to determine the minimum requirement for own funds and eligible liabilities (MREL). In order for the SRM to be able to draw up resolution plans for each entity, it needs to know about specific aspects of their solvency and leverage. These data are collected by means of exhaustive questionnaires. This is undoubtedly an important task, but the decentralisation and multiple layers of bureaucracy involved in the current banking union are such that regulatory compliance is absorbing a vital part of the banking sector's human resources. In recognition of this effort, the SRM's timetable for completing these questionnaires has been spread over 2016.

³ Talk given at the "Süddeutsche Zeitung Finance Day 2016," Frankfurt am Main, March 2nd, 2016: <https://www.ecb.europa.eu/press/key/date/2016/html/sp160302.en.html>

In this context of decentralisation and a multiplication of regulatory requirements, the European Banking Authority (EBA) has also designed an EU-wide stress test exercise for 2016. It published the methodology for these tests on February 24th, 2016, and two points stand out. The first is that the EBA aims to publish the results in the first quarter of the year. The second is that, somewhat controversially, the EBA has said that it will not set a minimum capital requirement. On the one hand, it seems logical given that the EBA aims to gather information for this year's supervisory evaluation and review process (SREP), which is when decisions on capital levels will be made. But on the other hand, such an evaluation dilutes

The EBA's decision not to set a minimum capital requirement in the EU-wide stress tests for 2016 dilutes their essence and weakens their ex-ante and ex-post disciplinary character.

the essence of the stress tests and weakens their *ex-ante* and *ex-post* disciplinary character, particularly in comparison with other similar tests, such as those conducted in the United States. On the whole, they do not seem likely to help reduce current market uncertainty.

As regards regulation from Spain, on February 9th, 2016, the Governing Council of the Bank of Spain approved the circular on supervision and solvency, which completes the adaptation of the European rules deriving from the Basel III Accord. The Circular lays down the regulations for branch offices and the freedom of credit institutions based in non-EU countries to provide services in Spain, and it spells out the capital buffer requirements. It also includes various provisions on credit institutions' internal organisation and remuneration policies, along with the internal capital adequacy assessment process entities are to undertake, as well as covering other points,

such as the rules on the transparency of credit institutions, and their reporting obligations to the Bank of Spain.

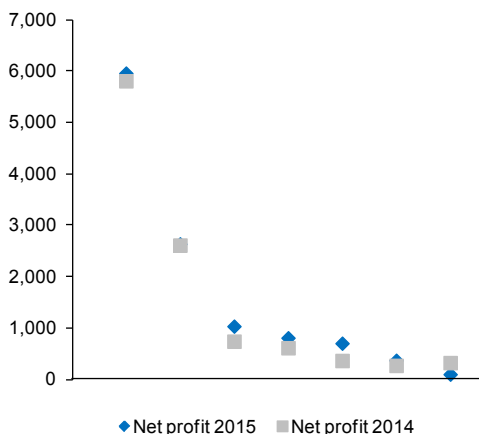
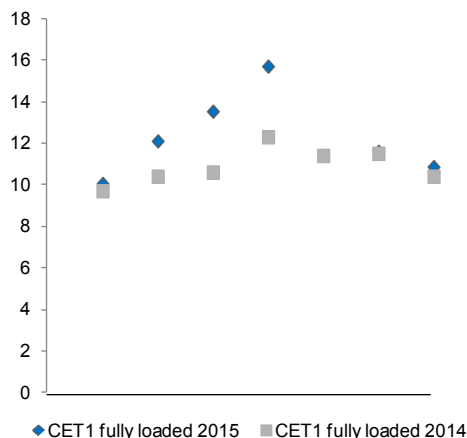
The Spanish banking sector: Results and expectations for credit

In the context of the situation described in the preceding section, the Spanish banks' year-end 2015 results (presented in February 2016) can be viewed as positive. Particularly when compared with the huge losses suffered by large institutions in the United Kingdom, Germany and Italy.

Exhibit 1 aims to give a single snapshot of the two main elements for market scrutiny: profitability and solvency. In the case of the former, the six largest Spanish banks increased their joint profits from 10.8 billion euros in 2014 to 11.7 billion euros in 2015, an increase of 8.1%. The variability in the magnitude of the results is due to the differences obtained from extraordinary operations and the uneven impact of insolvency provisions. In particular, these were reduced sharply in 2015.

The second panel of Exhibit 1 shows how solvency has progressed, from a fully-loaded core tier 1 capital (CET1) ratio, which shows the highest quality capital the entity would currently be deemed to hold if it were obliged to meet today the Basel III regulations envisaged for 2019. Averaged across these six large banks, CET1 rose from 10.9% in 2014 to 12.2% in 2015. This is a significant increase. In general, a degree of confusion has arisen as to the extent to which it is advisable to raise the own funds ratio above the regulatory minimum. The academic literature has for a long time illustrated various aspects of the – entirely logical – existence of the opportunity cost of capital, namely that higher capital requirements mean less lending. In recent years, it has been said that Spanish financial institutions started out from lower solvency levels than their European counterparts, the reasons including the fact that some components of this capital in Spain, such

Exhibit 1

Profits and solvency of Spain's six largest financial institutions in 2014 and 2015**1a) Profitability (EUR million)****1b) Solvency (%)**

Source: Financial institutions' consolidated accounts and authors' calculations.

as tax credits, would not be recognised as own funds by Basel III in 2019. Nevertheless, the banks have shown their capacity to increase other components of CET1. The “value” of the capital ratios also depends on the transparency of the assets in the denominator. If any European banking sector has really undergone an enhanced transparency exercise it is Spain's. This also

The Bank of Spain's decision on January 11th, 2016, to set the counter-cyclical capital buffer applicable to credit exposures in Spain at 0% was an explicit recognition of Spanish financial institutions' solvency and the opportunity cost of excessive regulatory requirements.

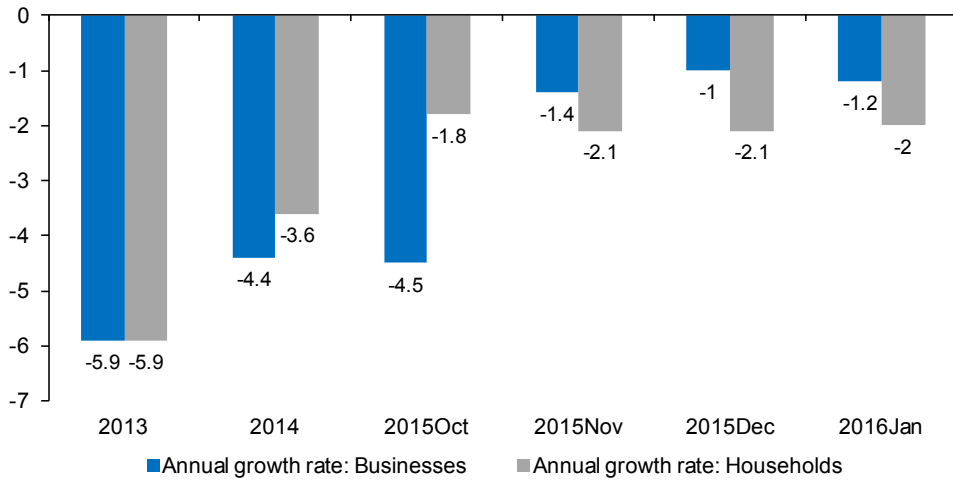
reduces the uncertainty as to the value of the buffer between the demonstrated and minimum regulatory solvency.

The Bank of Spain's decision on January 11th, 2016, to set the counter-cyclical capital buffer applicable to credit exposures in Spain as of January 1st, 2016, under Basel III regulations, at 0% was an explicit recognition of Spanish financial institutions' solvency and the opportunity cost of excessive regulatory requirements. As the supervisory authority pointed out, “the decision is based on the fact that all the information analysed yields consistent and sufficiently uniform signals against activating the counter-cyclical capital buffer at this time. In particular, the credit/GDP gap in June 2015 was -58%, which is still a long way from the 2% threshold established as the reference by the Basel Committee on Banking Supervision.”

Specifically, as regards the progress of credit – and SEFO's monitoring of it – the most recently published data suggest that year-on-year rates of change in financing to the Spanish private sector remained negative in January 2016 (Exhibit 2). Positive rates of change are anticipated in 2016,

Exhibit 2

Year-on-year change in lending to the Spanish private sector



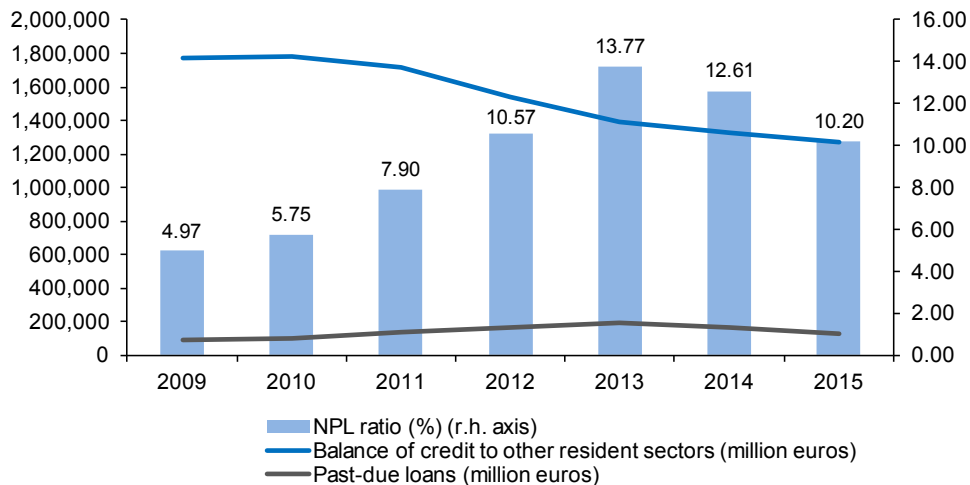
Source: Bank of Spain and the authors' calculations.

however, at around 3%, although this recovery is subject to the uncertainty deriving from the political deadlock and its actual and potential impact on investment projects.

The quality of the credit balance also continues to improve, as shown in Exhibit 3. The most recent data, from December 2015, show the ratio of doubtful credit to total private sector credit to have

Exhibit 3

Non-performing loans in Spain



Source: Bank of Spain and the authors' calculations.

fallen to 10.2% from a peak of 13.77% in 2013. As total credit increases (the ratio's denominator)

The most recent data show the ratio of doubtful credit to total private sector credit to have fallen to 10.2% from a peak of 13.77% in 2013. As total credit increases and the balance of non-performing loans continues to decline, the drop in the ratio will accelerate.

and the balance of non-performing loans continues to decline (as has been observed in recent months), the drop in the ratio will accelerate.

Fresh doubts about European banks?

Recent doubts have resurfaced over European financial stability. The problems were particularly acute in February, when concerns arose over Deutsche Bank's ability to meet its debt maturities. The systemic character of this German bank lies not only in its size but also in the fact that it holds derivatives worth over 50 trillion euros, 17 times Germany's GDP. This is not to say that these derivatives are putting the bank at risk, but that its leverage could potentially drag down a significant number of other European banks. The bank bought back part of its debt and brought payments forward to calm investors, but the doubts could resurface at any time, as since 2008 there has been a persistent problem of transparency affecting part of the European banking system's exposure to structured products.

Specifically, the doubts arising again now are related to the failed resolution framework existing in 2008, which has since been reformulated in the context of banking union. New European banking supervision and resolution mechanisms have been proposed, in which bondholders, as well as shareholders, are to face losses before taxpayers. What is more, bondholders cannot be

paid a dividend if the bank has not made a profit. Deutsche Bank was the first entity to face this restriction on paying bond dividends, specifically affecting its CoCos (contingent convertible bonds). However, it is not the only European entity to have issued CoCos, and the market has consequently punished bank bonds, and ultimately, the shares into which they may be converted. This explained a large share of their loss of market capitalisation.

This uncertainty coincides with the undeniable evidence that inter-bank interest rates are falling to negative levels, putting even more pressure on banks' margins. Indeed, the catalyst for these fears was the Bank of Japan's decision to set negative official rates, although the banks were offering deposits with positive rates. This mismatch across jurisdictions gives rise both to regulatory arbitrage and disparity in bank securities on different markets.

The doubts have also spread to Italy's banks. The latest analysis suggests that Italy's irrecoverable debts amount to 200 billion euros, i.e. 16.7% of total credit, compared with 7% in Spain and 4% in France. Other Bank of Italy estimates suggest that there could be a further 160 billion euros of doubtful loans. Italy's authorities have responded by setting up an asset management company (or "bad bank"). However, somewhat surprisingly, this company remains under the control of the Italian supervisory body, without the involvement of the European SRM. This treatment is in sharp contrast with that seen in other jurisdictions, such as Spain.

Instead of cohesion on the subject of transparency, Europe appears to be caught up in a regulatory dispute that could even be considered "diversionary tactics." Thus, for example, Germany has repeatedly insisted that holdings of government debt on bank balance sheets should be penalised. One of the longer-term effects of repeated bouts of increased sovereign risk is that government bonds are no longer an instrument for coverage and balance sheet diversification,

but are marked with a degree of stigma. However, in reality, these exposures, which are more or

As a result of repeated bouts of increased sovereign risk, government bonds have been marked with a degree of stigma. However, in reality, these exposures, which are more or less guaranteed by the ECB's expanded asset purchase programme, are highly transparent.

less guaranteed by the ECB's expanded asset purchase programme, are highly transparent.

Transformation under way

As a conclusion to the discussion of trends in European and Spanish banks, one might ask - what are the main lines of transformation for the Spanish banking system in 2016? These are summarised in Exhibit 4.

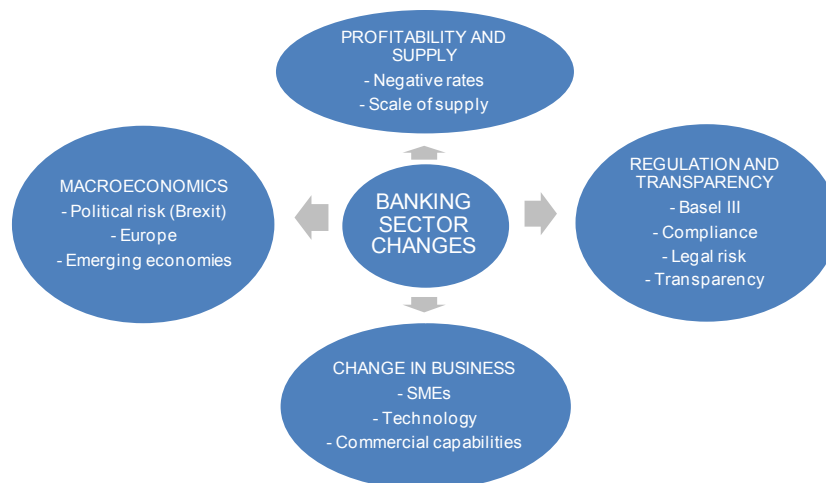
Firstly, banks continue to face the challenge of profitability, particularly in the current context of negative interest rates. There are those who argue that there are a number of reasons why these negative rates may have undesirable effects. First of all, with such low rates, there is little leeway for monetary policy and its impact on the market is diminished. Moreover, with high levels of public and private debt, it is difficult to envisage an easy path back to higher interest rates. The banks' need to make a profit rules out products and services based on negative rates, at least on a widespread basis, in the case of either deposits or credit.

When margins tighten, the response seems to lie in consolidation (*i.e.* competitors tend to merge so as to get a bigger share a smaller market "pie"). Significant progress has been made in this direction in Spain, but there is still a long way to go. In Europe, this is particularly fertile ground for corporate activity over the coming years.

The challenges of regulation and transparency are critical. Although the main aspects have been dealt with in previous sections of this note, it is worth highlighting that there are significant

Exhibit 4

Main lines of transformation for the banking sector in 2016



Source: Authors' own elaboration.

differences in transparency (observable balance sheet quality) among European banks, and neither the Single Resolution Mechanism nor the planned stress tests seem able to solve this issue satisfactorily.

From the macroeconomic viewpoint, the weakness of certain emerging economies stands out. This could have a negative impact on some Spanish entities, but the long-term effect should be viewed as positive, as the recent historical perspective shows geographical diversification to have clear benefits. Political risks, and Brexit in particular, could also have impacts on the macroeconomic level. It should come as no surprise that the City of London's banks are strongly against the UK's leaving the EU. The gains from financial integration and interaction are clear, and any scenario of disintegration would have serious negative consequences.

Finally, there is the change in the banks' business. The unavoidable correction in the property sector has led many European banks to rethink their business and focus more on SMEs. This is a complex strategy, as it requires a change in the competences of banks' human capital – to take a more proactive approach and offer more tailored services – because this type of financing is particularly penalised by solvency regulations. Technology remains part of the answer, but there are a whole host of initiatives, and it is difficult to distinguish which will emerge victorious and what their true impact will be.

Regulations on banks' sovereign bond holdings: Assessing the impact of potential changes

Victor Echevarria Icaza and Francisco J. Valero López¹

The increase in banks' public debt holdings has raised concerns from regulators over the current treatment of such holdings on banks' balance sheets. Potential changes to existing risk weightings and the introduction of limits on holdings could bring both positive and negative implications for sovereigns and banks and should be accompanied by further progress on banking union.

The significant weight of government debt on banks' balance sheets in several European countries, including Spain, has been fuelling ongoing debate about the regulatory treatment of these bond holdings. Their inclusion within risk-weighted assets, in the leverage ratio and in the large exposure limit are some of the alternatives presently under debate. A reduction in sovereign bond holdings could weaken the link between banks and sovereigns and free up funds for private sector lending. However, penalising these holdings would also reduce banks' ability to stabilise the sovereign bond markets and could exacerbate financial fragmentation in the event of stress in the EMU. Although the introduction of outright monetary transactions (OMTs) allows the ECB to act as lender of last resort to eurozone sovereign issuers, further progress on banking union may prove even more important in preventing bank stress from being passed on to sovereigns.

Since the start of the global financial crisis, there have been many changes to financial regulations that have had an impact on much of the banking business.

In the face of these changes, despite being a permanent focus of debate, the regulatory treatment of sovereign debt holdings for capital adequacy purposes remains unchanged. Since the crisis, banks across several European countries have sharply increased their public debt holdings in terms of both outstanding balances

and balances relative to total bank assets. The collateral effects of this trend on efficient allocation of banks' resources and on strengthening sovereign – bank linkages have renewed interest over the current treatment of such holdings.

To date, in practice, the regulatory framework exempts sovereign debt issued by EU states in local currency from having to be included in banks' risk-weighted asset calculations. However, the stress experienced by certain countries during the euro crisis changed the underlying tenet that

¹ A.F.I. - Analistas Financieros Internacionales, S.A.

advanced economies' sovereign bonds should be necessarily considered risk-free assets.

This article analyses the various regulatory proposals currently on the table for sovereign bond holdings and their potential effects. Specifically, the article highlights the fact that the proposed regulations could have counter-productive effects if not accompanied by other measures to provide the monetary union with better tools for managing crises, whether bank or sovereign in origin.

The first section analyses the existing regulatory framework and the recently-proposed reforms. The following section contemplates the potential effects of the new regulations on banks' activities and on the functioning of the monetary union.

Regulatory framework

The relationship between public debt portfolios and banks' business activities is shaped by banking regulations in general and accounting regulations in particular, insofar as this debt, which is traded on official exchanges, is subject to supply and demand, which may or may not be driven by interest rates.

These swings can be significant even in the absence of an economic or banking crisis. In Spain, and other European countries, we need only to cast our minds back to the bond market crisis of 1994, which triggered a massive sell-off in the European markets, driving yields substantially higher and causing considerable losses for banks.

The most notable solution taken at that time was the addition of a kind of portfolio immune to these swings for accounting purposes: the held-to-maturity portfolio, albeit subject to significant restrictions related to its financing.²

More recently, against the backdrop of the economic crisis which began in 2007, the above-

mentioned relationship has taken on greater proportions, affecting sovereigns' and banks' risks at a higher level, as is expressed in the vicious circle illustrated in Exhibit 1.

Indeed, the banking union effort was set in motion precisely to break this circle. Although banking union is not yet complete, it is far enough along to understand and assess its possibilities and limitations.

The 1994 bond market crisis and the recent crisis revealed that banks' sovereign bond exposures have entailed far greater risks than anticipated.

What both of these episodes —the 1994 bond market crisis and the recent crisis— have in common is that banks' sovereign bond exposures have entailed far greater risks than anticipated. Some of these risks include potentially significant implications for the real economy by impeding corporate and household financing or at least making it more expensive.

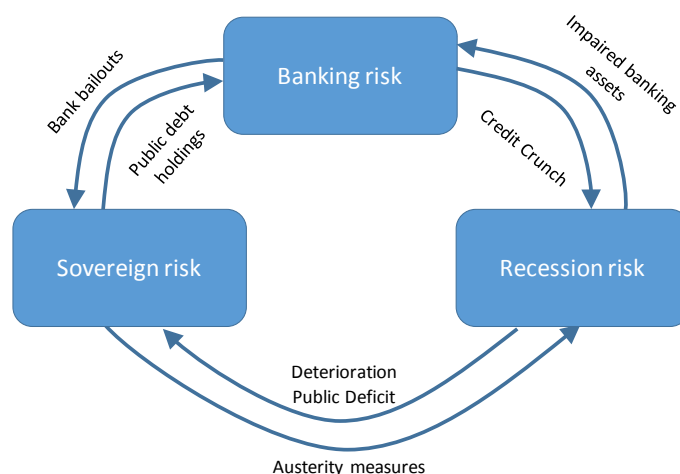
It is hardly surprising, therefore, that the authorities are proposing solutions for reducing these risks, preventively if possible. This is what the European Commission (EC) has proposed in its Document COM(2015) 587,³ which accompanied the EC proposal to complete Banking Union with the creation of a European deposit insurance scheme (COM(2015) 586), whose absence has been flagged in different arenas as an important gap if the aim is to decouple bank risks from sovereign risks as much as possible.

Among the risk-mitigation measures proposed by the EC in the above-mentioned document,

² See Bank of Spain Circular 6/1994, of September 26th, 1994, on credit institutions, amending Circular 4/1991, of June, 14th, 1991, on accounting rules and financial statement templates.

³ Towards the completion of the Banking Union.

Exhibit 1

The three vertices of the current vicious circle

Source: AFI.

those affecting banks' solvency along either of the following two dimensions stand out:

- Treatment (weighting) of sovereign exposures.
- Limits on such exposures.

The EC notes that such initiatives would emerge first within the Basel Committee on Banking Supervision Committee (BCBS), from where they would be transposed into European law. At any rate, it is meaningful to analyse the current situation.

Debt weightings

Given that Basel III has not modified in substance the treatment of the various classifications of credit risk, we need to go back to Basel II to see how these exposures are weighted (in theory in accordance with their credit ratings,⁴ regardless of the fact that a process is underway to reduce the importance of these ratings in respect of banking

regulations). For simplicity purposes, we refer exclusively to the standardised approach. As it is more recent and also more general in scope, here we echo Regulation EU no. 575/2013 (the Capital Requirements Regulation or CRR).

If this modus operandi were used, a sufficient impairment of the creditworthiness of a sovereign bond would imply a higher capital allocation on the part of the bank holding that asset. Recall, however, that Basel II contemplated the following: "at national discretion, a lower risk weight may be applied to banks' exposures...denominated in domestic currency and funded in that currency. Where this discretion is exercised, other national supervisory authorities may also permit their banks to apply the same risk weight to domestic currency exposures to the sovereign funded in that currency." Both elements remain intact in the current CRR.

However, in the EU, this situation is superseded by the principle of equal treatment of the various

⁴ The process of approving the correspondence, or 'mapping', between the credit rating assessments and the specific credit ratings awarded by each agency is pending completion. The most recent document available is: <http://www.eba.europa.eu/documents/10180/1269185/Final+Draft+ITS+on+ECAIs%27%20Mapping.pdf>

Table 1

Creditworthiness and risk weights

Credit assessment	1	2	3	4	5	6
Risk weight (%)	0	20	50	100	100	150

Source: Regulation EC No. 575/2013.

member states, which is why article 114.4 of the CRR allocates a weight of 0% to exposures to the central governments and central banks of these states that are denominated and funded in the corresponding domestic currency.

This treatment could be changed by way of opportune regulatory amendments. Any such amendments would likely be opposed by the states believed to have the most to lose, influenced by the weight of domestic investment in their debt (as the higher this is, the less dependent the sovereign will be on foreign investment). At any rate, no specific project has been publicly formulated along these lines at this time.

Limits on exposures to sovereign debt

Another alternative is the imposition of limits on banks' sovereign holdings. Leaving aside other potential formulations,⁵ there are currently two possibilities within the scope of the Basel III framework.

The first, one of the novelties introduced by Basel III, is the leverage ratio,⁶ which, in essence, is similar to the capital adequacy ratio but without applying risk weights; the idea is to use tier 1 capital to calculate the numerator.

Obviously, the leverage ratio would have a greater impact on risks weighted at 0%, such as the debt under debate here, the more demanding the

threshold imposed: the minimum leverage ratio currently contemplated is 3%, albeit subject to final calibration.

The leverage ratio does not have a big impact on the matter at hand, not only because its design is not complete but also because initially it forms part of Pillar II; the idea is to migrate it to Pillar I treatment from January 1st, 2018, which means that all the details will have to be decided in 2017, at the very latest.

The second line of initiatives relates to application to these exposures of the large exposure limits, which are not part of the Basel Capital Accord but also emanate from the Basel Committee on Banking Supervision and have already been incorporated into the CRR. An institution's exposure to a client or group of connected clients shall be considered a large exposure where its value is equal to or exceeds 10% of its eligible capital (article 392 of the CRR). In principle, no large exposure may exceed 25% of eligible capital, although the competent authority may also set an absolute limit of 150 million euros, or an even lower limit (article 395 of the CRR).

Exempted from these limits, among other exposures, are claims on public administrations which are assigned a 0% risk weight for credit risk calculation purposes (article 400.1.a) of the CRR).

Any decision to apply large exposure limits to a public administration, particularly if that administration is a state, needs to consider

⁵ By way of example, in EU banking regulations, there are already limitations on qualifying industrial holdings (currently regulated in articles 89 and 91 of the CRR).

⁶ See Basel III: Leverage ratio framework and disclosure requirements, January 2014.

carefully the fact that many exposures may be inter-related, via companies and other public organisations, without there necessarily being decision-making unity. This circumstance is expressly contemplated in article 4.1.39 of the CRR, defining 'close links'. In this respect, public debt could be viewed as a 'client' which can be differentiated from other claims on the state in question on the basis of its links with the market.

Under the umbrella of Basel III/CRD IV/CRR, it is possible to imagine the incorporation of some form of haircut or limit on investments in public debt by banks, at least in the instances in which these investments reach levels deemed excessive, not so much in absolute terms as in relation to the size of the entities.

Requirements Directive)/CRR, some form of haircut or limit on investments in public debt by banks, at least in the instances in which these investments reach levels deemed excessive, not so much in absolute terms as in relation to the size of the entities.

Effects of penalising sovereign bond holdings

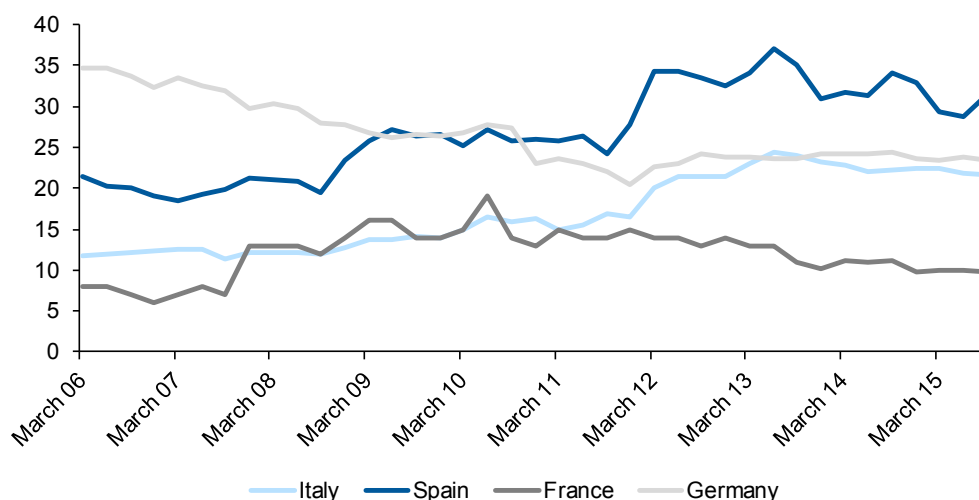
The introduction of some form of haircut on banks' sovereign debt holdings would have an impact on the entities' allocation of resources and on the link between banks and sovereigns. The first impact would be to reduce banks' demand for sovereign bonds. As illustrated in Exhibit 3, the limit on holdings would have a substantial impact on peripheral issuers where the volume of debt held by domestic banks rose considerably during the crisis.

In short, we believe it is possible to incorporate, under the umbrella of Basel III/CRD IV (Capital

Meanwhile, the impact of weighting sovereign bond holdings for capital adequacy purposes would

Exhibit 2

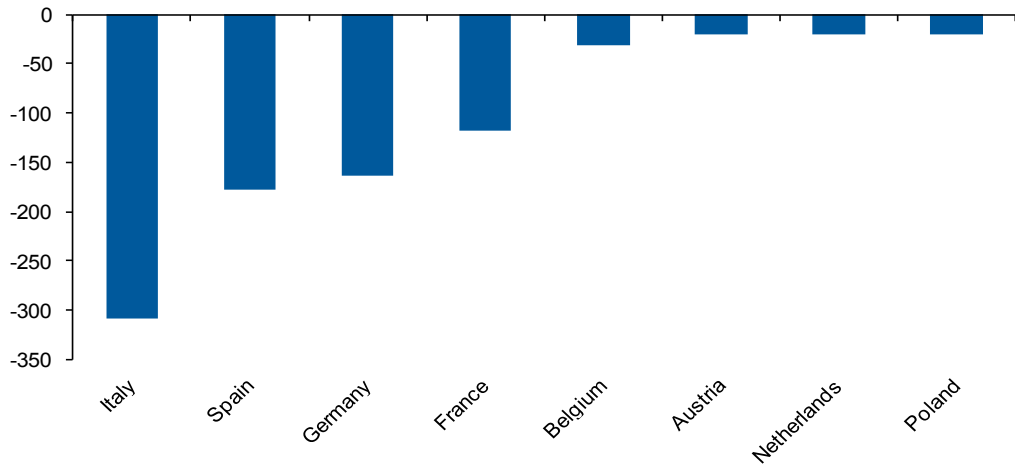
Trend in banks' sovereign bond holdings (As a percentage of total debt)



Sources: Bruegel, Merler and Pisani-Ferry (2012), AFI.

Exhibit 3

Changes in holdings following introduction of a limit of 25% of risk-weighted assets
(In billions of euros)



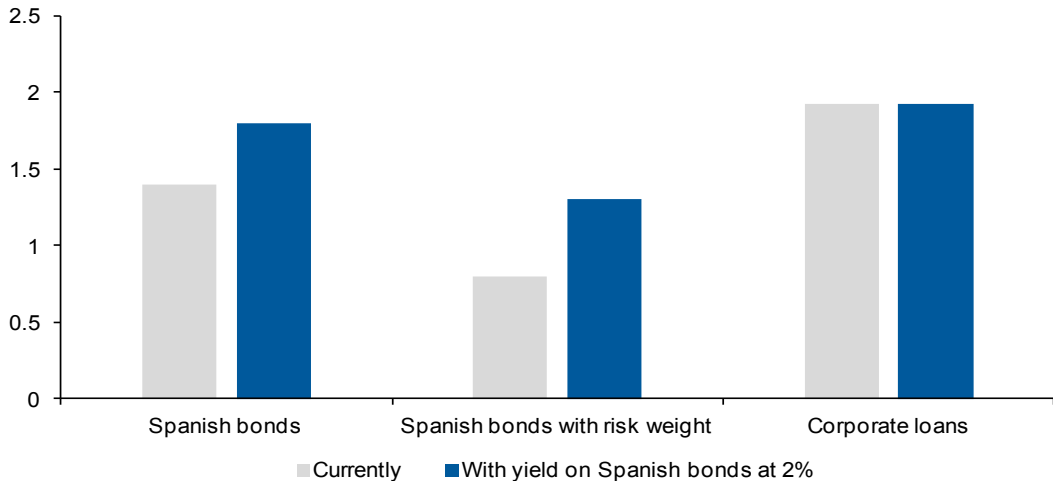
Source: Citi, AFI.

depend on the risk weights assigned. If the weights are in line with sovereign credit ratings, the impact on the cost of capital would exacerbate the scant yields these bonds are currently offering so that their risk-adjusted returns would dip below those offered by corporate loans.

Exhibit 4 illustrates how even in the event of Spanish bond yields rebounding towards the 2% mark, the cost of risk would render this asset less attractive than corporate loans with a similar risk profile, even assuming that the rate on new loans were to stay at current levels of around 3%.

Exhibit 4

Risk-adjusted return assuming different weights
(Percentage of investment)



Source: AFI.

Effects on the sovereign - bank link

Another ramification of a potential decision to penalise sovereign bond holdings would be to reduce the link between banks and their sovereigns. During the crisis, strengthening of these links meant that the episodes of stress sustained by banks had a knock-on effect on their sovereigns and vice versa, ultimately amplifying overall financial stress.

This transmission effect has been amply debated in academic papers. As documented by Singh *et al.* (2016), the transmission of risk from the financial institutions to the sovereigns themselves increased after the latter introduced guarantees with a view to ensuring the solvency of their domestic banks in 2008-2009. In contrast, when uncertainty about the solvency of certain peripheral EMU economies intensified at the end of 2011, there was an observable transfer of risk from the sovereigns to their banks.

Intensification of this link between banks and their sovereigns is particularly harmful when it affects

Intensification of the link between banks and their sovereigns is particularly harmful when it affects countries belonging to a monetary union that does not have the mechanisms needed to handle asymmetric shocks.

countries belonging to a monetary union that does not have the mechanisms needed to handle asymmetric shocks (Abascal *et al.*, 2013). Specifically, if the sovereign does not have the resources required to recapitalise a bank, the central bank does not guarantee coverage of this function and there are no alternative recapitalisation mechanisms, impairment of the entity's solvency may in turn impair the sovereign. As a result, the perceived existence of this risk at a financial institution could trigger financial

fragmentation within the monetary union. This financial fragmentation can in turn limit the ability of solvent companies (and even the sovereign itself) to obtain funding via a credit crunch, ultimately undermining economic activity.

Alternative investment options

The increase in sovereign bond holdings by financial institutions during episodes of stress can reduce the resources available for private sector funding. Theoretically, for this to have an adverse effect on a country, one of the following two conditions has to be met: either, the private sector is more efficient at allocating resources than the sovereign; or, there is some form of bias making the financial institutions demand bonds when it would be more efficient from a risk-reward perspective to lend to the private sector.

Several studies have pinpointed evidence of such a bias, shaped by either impaired solvency on the part of the financial institutions or because banks see a specific appeal in sovereign bonds (Mody, 2012 and Angeloni, 2012). However, Castro and Mencía (2014) do not find evidence of such a bias, while Echevarria (2016) finds that this bias is only observed during short bouts of particularly intense sovereign stress.

Effects when the source of the stress is sovereign in nature

Financial institutions tend to play a stabilising role in sovereign bond markets during episodes of crisis. In times of sovereign stress or spikes in global volatility, investors tend to repatriate their investments (even when the source of the stress lies with a third country), seeking refuge in risk-free assets.

The result is that the prices of risk assets, including the sovereign debt of non-core eurozone countries, fall (the yield rises), so that the country's financial stress intensifies. This can even materialise when

the risk aversion phenomenon is not justified by the trend in the country's fundamentals.

Any decision with the effect of limiting banks' ability to stabilise the sovereign debt market as a result of the introduction of limits or risk weights could potentially generate episodes of sovereign stress that need not necessarily derive from deterioration of the country's fundamentals. This effect would be particularly significant if the weight assigned to sovereign bonds for the purpose of calculating capital ratios depends on the bonds' credit ratings, as this would make these holdings particularly onerous in RWA terms during times of economic weakness (pro-cyclical effect).

Accordingly, banks would pare back their sovereign bond holdings during times of stress and this would drive a bigger increase in yields than if these bond holdings were exempt from haircuts or exposure limits. As a result, the introduction of these risk-mitigation measures would run the risk of amplifying the adverse impact of an increase in risk aversion as investors may perceive that the increase in sovereign bond yields may impede the sovereigns' ability to support their banks, the result of which would be unwanted strengthening of the sovereign-bank negative feedback loop.

To prevent this from happening, the transmission of sovereign risk into bank risk can be reduced by

To be truly effective, the inclusion of sovereign bond holdings for RWA calculation purposes must be accompanied by a genuine lender of last resort, a role the European Central Bank is approaching with the introduction of OMTs.

creating instruments to immunise sovereigns from global risk aversion trends. In a monetary union, these mechanisms include the existence of a central bank that acts as a lender of last resort. Against this backdrop, the evidence

found by Singh *et al.* (2016) and Echevarria and Sosvilla (2016) of a reduction in risk transmission between sovereigns and banks in the wake of the announced creation of the outright monetary transactions (OMT) and the statements made by Mario Draghi in the summer of 2012 (the now-famous "whatever it takes") is consistent with the creation of a lender of last resort figure.

Therefore, to be truly effective, the inclusion of sovereign bond holdings for RWA calculation purposes must be accompanied by a genuine lender of last resort, a role the European Central Bank is approaching with the introduction of OMTs. This instrument would at least mitigate the adverse effect of the introduction of haircuts on sovereign bond holdings.

Effects and solutions when the source of the stress is bank-related

The assessment of the mechanisms rolled out by the EU to manage financial crises prompted by a spike in bank stress is less positive.

When the source of stress is the need to recapitalise the banking system, the haircut on sovereign bond holdings could make matters worse: not only would the system need recapitalising, with the associated cost for the sovereign, banks would have to sell off sovereign bonds to boost their capital ratios. As a result, bank stress would be passed on, with even greater intensity, to the sovereign.

If the source of the stress is a specific institution that is not considered 'systemic', the entities' capital buffers, the loss absorption measures and the established resolution procedures would limit the impact on the sovereign. The difficulty could arise, however, in the event of materialisation of systemic risk that calls into question the sovereign's ability to recapitalise the entity.

The introduction of regulations specifying the portion of debt eligible for absorbing losses in

the event of impaired solvency aims to reduce the link between sovereigns and their financial institutions: in the event of solvency problems, some of the cost of the recapitalisation effort would be borne not by the sovereign but rather by the debt holders. This would reduce the state's financial burden.

All of this leads us to conclude that the best way to prevent the transfer of solvency issues to the sovereign in the wake of an episode of bank stress would be to strengthen banking union. This would enable the sharing of banking sector risks among the banking union participants and would therefore prevent contagion to a specific sovereign and the related increase in financial fragmentation.

Regulations specifying debt eligible with loss absorption capacity in the event of impaired solvency aims to reduce the link between sovereigns and their financial institutions, specifically by shifting some of the cost of the recapitalisation effort to debt holders rather than the sovereign.

The EU has taken some important steps towards the creation of a banking union. However, until this process is complete, the risk of intensification of the sovereign-bank link will continue to exist. Unification of the deposit guarantee schemes and the establishment of a single bank resolution fund represent key milestones in this process.

Conclusions

The foregoing analysis reveals that although the introduction of a capital requirement for sovereign bond holdings would have some advantages, its ultimate impact would depend on the existence of other mechanisms designed to mitigate possible negative effects.

The decision to include sovereign debt in the RWA calculation would introduce a more procyclical bias to capital regulations via both the introduction of a capital requirement in respect of these positions and limits on exposures to sovereign debt.

Elsewhere, to achieve the objective of reducing the sovereign-bank link in the eurozone, the introduction of haircuts on sovereign bond holdings could be counter-productive. Although the OMTs seem to have worked as a mechanism for converting the ECB into a de facto lender of last resort for the sovereigns, culmination of the banking union process is a vital step in reducing the sovereign-bank link.

Lastly, the timelines for introducing the various measures are a crucial variable in the current environment. Banks' returns are currently being eroded by increased regulatory requirements coupled with the adverse impact on profitability of curve flattening and the existence of negative rates at the short end of the curve. Before penalising sovereign bond holdings, it might be a good idea to make progress on banking union to prevent the erosion of banks' profitability from causing financial stability issues. The idea would be to include the haircuts on sovereign bond holdings as part of a broader package of measures, allowing for an improved assessment on their overall impact on financial stability.

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Regional concentration of the Spanish banking market

Joaquín Maudos¹

The profound restructuring of Spain's banking sector has resulted in a significant increase of concentration across almost all provinces. Despite the much needed correction of installed capacity in response to the crisis, the resulting situation may warrant assessment of its potential implications for competition.

The deep restructuring undergone by the Spanish banking sector to correct the imbalances built up during the preceding expansionary phase has led to significant branch reduction, largely as a consequence of mergers within the sector. In parallel, there has been a notable increase in market concentration – now much higher than the European average. While the level of concentration at the national level is important, it conceals major differences at the regional level. Using information at the provincial level of the network of branches as a proxy for bank business, results show that concentration varies greatly across the provinces, although increasing substantially during the crisis and almost across all of Spain. The increase in concentration has been so intense that in some provinces it exceeds the threshold that in some countries would require an assessment of potential impact on competition.

The profound restructuring of the Spanish banking sector has resulted in a smaller number of competitors and increased market concentration. Specifically, by September 2015, the number of deposit-taking institutions had fallen by 24% (from 286 to 198) since the start of the crisis in 2008. In parallel, the market share of the five largest entities grew by 37% (from 42.4% to 58.3%) between 2008 and 2014, and the Herfindahl-Hirschman Index (HHI)² of market concentration

rose sharply (69%) from 497 to 839. This decrease in the number of competitors and rise in concentration has been much more pronounced than the European average, revealing the deeper restructuring undergone by the Spanish banking system during the crisis.

The thorough restructuring has completely changed the relative position of Spain's banking market concentration vis-à-vis the European context.

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² The Herfindahl-Hirschman Index (HHI) is defined as the sum of the squares of the market shares of all the banks operating in the market analysed. The HHI has certain advantages over absolute indices such as CR_i (market share of the "i" biggest banks): it takes into account the total number of competitors and its results are not sensitive to the number of banks included (1, 3, 5, 10, etc.).

Since 2008, it has risen from a level below the euro-area average to concentration indices that exceed the average for European banks in late 2014. This situation could have implications for the strength of competition.

However, national indicators may not be the most relevant when it comes to judging the intensity of competition, at least for those banks for which the significant geographical dimension for competition is the regional market rather than the national market. And this may be the case of many Spanish entities, whose business is concentrated in regional markets rather than covering the country as a whole.

It should also be remembered that bank restructuring has had an uneven impact across the country, at least in terms of the adjustment to installed capacity. As explored in this article, the intensity of the reduction in the branch network has varied across Spain's provinces and is more pronounced in those where entities that received public aid have a stronger presence, and on which the Memorandum of Understanding (MoU) imposed harsher restrictions in terms of cutting their installed capacity. The differing intensity of the adjustment goes hand in hand with a differing intensity of increase in market concentration, such that concentration rose more in those provinces with the most branch closures.

Against this backdrop, this article aims to analyse the regional dimension of the Spanish banking market, constructing concentration indices at the provincial scale based on the distribution of each deposit-taking institution's branch network (including banks, savings banks, and credit unions). Specifically, indices have been constructed for 2008 and 2014, to allow for an analysis of the impact of restructuring on banking market concentration.

The results of the analysis have significant economic policy implications. In some provinces, the increase in concentration exceeds thresholds

that in other countries would be considered worrisome, currently reaching levels high enough to affect the strength of competition. This is a situation which therefore needs to be monitored.

Along with this introduction, this article is divided into four sections. The first section analyses the progress of bank concentration in the European context. The second focuses on an analysis at the provincial level of bank concentration in Spain, after analysing the differences in intensity of the adjustment that has taken place in the branch network. The following section analyses the possible impact of the current levels of concentration in terms of competition, based on the concentration indices constructed, taking the thresholds used in the United States as a benchmark. Finally, the article sets out some of the conclusions of the analysis performed.

Trends in bank concentration in Spain in comparison with the European context

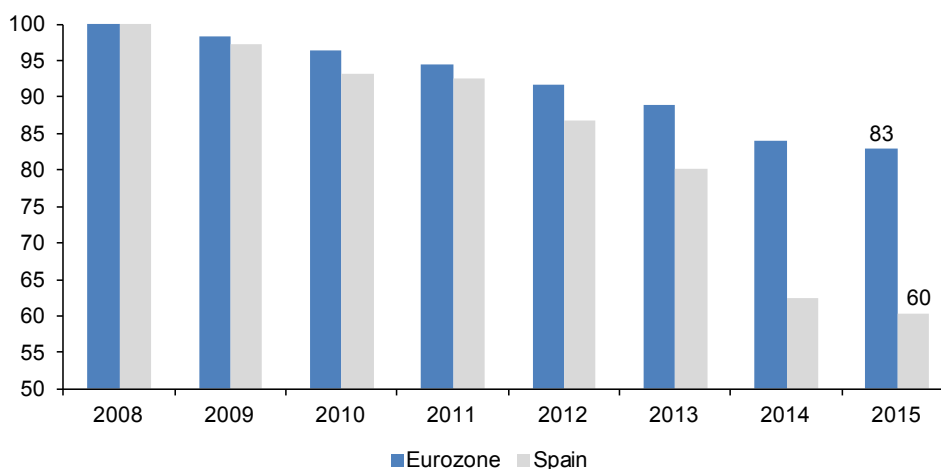
In the years since the start of the crisis in 2008, the number of credit institutions has fallen by 40% in Spain, compared with a drop of 17% in the euro area. The decline has been so intense that Spain ranks second in the euro area in terms of the

In the years since the start of the crisis in 2008, the number of credit institutions has fallen by 40% in Spain, compared with a drop of 17% in the euro area. However, Spain remains second on the EU ranking in terms of branch network density.

contraction, behind only Cyprus and Greece. The number of banks has also fallen in the largest European economies, but with differing intensities: 36% in France, 20% in Italy and 11% in Germany.

Exhibit 1

Number of credit institutions (2008=100)



Source: ECB.

Table 1

Market concentration in the EU-27 banking sectors

HHI				CR ₅			
2008		2014		2008		2014	
Germany	191	Germany	301	Germany	23	Luxembourg	32
Italy	307	Luxembourg	329	Luxembourg	30	Germany	32
Luxembourg	309	Austria	412	Italy	31	Austria	37
United Kingdom	431	Italy	424	United Kingdom	38	United Kingdom	39
Austria	454	United Kingdom	462	Austria	39	Italy	41
SPAIN	497	France	584	SPAIN	42	Ireland	48
Poland	562	Poland	656	EU-15	44	EU-15	48
EU-15	642	Ireland	677	EU-27	44	France	48
EU-27	650	EU-15	703	Poland	44	EU-27	48
Ireland	661	EU-27	710	Ireland	50	Poland	48
France	681	Romania	797	France	51	Hungary	53
Hungary	819	Bulgaria	836	Romania	54	Romania	54
Bulgaria	834	SPAIN	839	Hungary	54	Bulgaria	55
Romania	922	Sweden	880	Bulgaria	57	Slovenia	56
Sweden	953	Hungary	905	Slovenia	59	SPAIN	58
Czech Republic	1,014	Czech Republic	949	Sweden	62	Sweden	59
Cyprus	1,019	Belgium	982	Czech Republic	62	Czech Republic	61

Table 1 (*continued*)**Market concentration in the EU-27 banking sectors**

HHI				CR ₅			
2008		2014		2008		2014	
Portugal	1,114	Latvia	1,001	Cyprus	64	Cyprus	63
Greece	1,172	Slovenia	1,026	Denmark	66	Latvia	64
Slovakia	1,197	Portugal	1,164	Portugal	69	Belgium	66
Latvia	1,205	Denmark	1,190	Greece	70	Denmark	68
Denmark	1,229	Slovakia	1,221	Latvia	70	Portugal	69
Malta	1,236	Cyprus	1,303	Slovakia	72	Slovakia	71
Slovenia	1,268	Malta	1,648	Malta	73	Finland	80
Lithuania	1,714	Lithuania	1,818	Belgium	81	Malta	82
Belgium	1,881	Netherlands	2,131	Lithuania	81	Netherlands	85
Netherlands	2,167	Greece	2,195	Finland	83	Lithuania	86
Estonia	3,120	Estonia	2,445	Netherlands	87	Estonia	90
Finland	3,160	Finland	3,310	Estonia	95	Greece	94

Source: ECB and author's calculations.

The reduction in the number of credit institutions has taken place in parallel with a cut in installed capacity, leading to an increase in the ratio of the population to branches. Specifically, from 2008 to 2014, in Spain the ratio has risen by 47%, from

The concentration of the Spanish banking market was below the European average in 2008 although by the end of 2014 had risen above it.

991 to 1,454. Although this growth is more than twice the EU15 average in terms of the sharp cuts in the branch network, Spain remains second on the EU rankings in terms of branch network density. The gap with the euro area is huge: 1,454 vs. 2,111.

The reduction in the number of competitors has led to an increase in the concentration of the European banking market. Thus, for the EU-27 (weighted) average, the market share of the five largest credit institutions (CR₅) rose by 7.5%, from 44% in 2008 to 48% in 2014 (Table1). In the case

of the HHI, the concentration has risen by 9%, from 650 to 710.

In Spain, bank concentration has increased more intensely: 38% on the CR₅ and 69% on the HHI. This stronger increase explains how, although the concentration of the Spanish banking market was below the European average in 2008, by the end of 2014, had risen above it: 22% higher in terms of CR₅ and 18% in terms of HHI. On the EU27 ranking, Spain has gone from having the 6th lowest CR₅ in 2008 to 11th in 2014, and from 6th to 13th in terms of HHI.

Concentration of provincial banking markets

As mentioned in the introduction, the existence of significant differences across regions means that analysing banking market concentration at the national level alone may reveal only a partial picture. As a result, it is important to complement the results of the national analysis with one that has a narrower scope. This is particularly so given that many Spanish entities do not operate

nationally, but only within certain regions or even just a handful of provinces. Moreover, as will be discussed below, the average national market concentration value masks huge differences between provinces.

The limitation of the analysis of Spanish banking market concentration at the regional scale is that there is only public information on the provincial distribution of the network of branches of each deposit-taking institution. Data referring to 2014 is available from the most recently published annual reports for banks (AEB), savings banks (CECA) and credit unions (UNNAC).³ No information is available for other relevant business variables (such as total assets, credit, deposits, etc.).

In any event, the provincial distribution of the branch network is valuable information with which to approximate and quantify the regional concentration of the banking system in Spain, which explains why it has been used in a number of studies. Based on this information, it is possible to construct provincial concentration indices, in terms of both market share of the largest entities (CR₄) and HHI.

As a preliminary analysis of the evolution of provincial banking markets, it is worth analysing the changes that have taken place in the provincial distribution of the network of branches in Spain, as, as will be discussed below, there are significant differences between provinces, affecting changes in concentration.

To this end, Table 2 shows the change taking place in the number of offices in each province between 2000 and 2008 (expansionary phase) and between 2008 and September 2015 (crisis).

Since the start of the crisis, Spain's branch network shrunk in all of Spain's provinces, without exception, returning to the number of branches that existed 31 years earlier, in 1984.

The first thing that stands out is that whereas over the period 2000-2008, the branch network grew by 17% (6,776), between 2008 and

Table 2

Number of branches in the Spanish provinces

	2000	2008	2015 (September)	Variation		Percentage	
				2000-2008	2008-2015 (September)	Variation 2000-2008	Variation 2008-2015 (September)
Álava	281	350	250	69	-100	25	-29
Albacete	317	350	299	33	-51	10	-15
Alicante	1,358	1,748	1,126	390	-622	29	-36
Almería	538	709	486	171	-223	32	-31
Asturias	893	978	805	85	-173	10	-18
Ávila	199	217	138	18	-79	9	-36
Badajoz	660	753	645	93	-108	14	-14
Balearic Islands	1,060	1,261	918	201	-343	19	-27
Barcelona	5,204	5,866	3,439	662	-2,427	13	-4
Burgos	524	550	384	26	-166	5	-30
Cáceres	483	452	385	-31	-67	-6	-15

³ Although the Bank of Spain's *Boletín Estadístico* (Statistical Bulletin) publishes data on the distribution of credit and deposits by province, the information is not disaggregated to the level of individual entities.

Table 2 (*continued*)**Number of branches in the Spanish provinces**

	2000	2008	2015 (September)	Variation 2000-2008	Variation 2008-2015 (September)	Percentage Variation 2000-2008	Percentage Variation 2008-2015 (September)
Cádiz	635	807	523	172	-284	27	-35
Cantabria	485	509	428	24	-81	5	-16
Castellón	574	683	395	109	-288	19	-42
Ciudad Real	445	477	407	32	-70	7	-15
Córdoba	608	696	526	88	-170	14	-24
Coruña, A	924	994	697	70	-297	8	-30
Cuenca	248	254	230	6	-24	2	-9
Girona	769	863	506	94	-357	12	-41
Granada	713	852	639	139	-213	19	-25
Guadalajara	211	274	208	63	-66	30	-24
Guipúzcoa	538	597	510	59	-87	11	-15
Huelva	367	450	309	83	-141	23	-31
Huesca	383	359	240	-24	-119	-6	-33
Jaén	600	635	519	35	-116	6	-18
León	488	551	428	63	-123	13	-22
Lleida	550	590	415	40	-175	7	-30
Lugo	373	336	257	-37	-79	-10	-24
Madrid	4,829	6,104	3,965	1,275	-2,139	26	-35
Málaga	918	1,406	915	488	-491	53	-35
Murcia	1,064	1,364	918	300	-446	28	-33
Navarra	707	719	571	12	-148	2	-21
Ourense	420	375	222	-45	-153	-11	-41
Palencia	228	225	152	-3	-73	-1	-32
Las Palmas	510	776	501	266	-275	52	-35
Pontevedra	775	829	543	54	-286	7	-34
Rioja, La	426	497	341	71	-156	17	-31
Salamanca	369	408	294	39	-114	11	-28
Sta.Cruz de Tenerife	556	716	516	160	-200	29	-28
Segovia	192	210	143	18	-67	9	-32
Seville	1,237	1,530	1,004	293	-526	24	-34
Soria	165	150	114	-15	-36	-9	-24
Tarragona	712	836	516	124	-320	17	-38
Teruel	239	236	198	-3	-38	-1	-16
Toledo	590	674	560	84	-114	14	-17
Valencia	2,176	2,663	1,617	487	-1,046	22	-39
Valladolid	529	613	408	84	-205	16	-33
Bizkaia	899	1,059	773	160	-286	18	-27
Zamora	247	256	199	9	-57	4	-22
Zaragoza	1,047	1,212	735	165	-477	16	-39
Ceuta and Melilla	37	46	39	9	-7	24	-15
Total	39,300	46,065	31,356	6,765	-14,709	17	-32
Foreign	91	102	73	11	-29	12	-28
Total	39,391	46,167	31,429	6,776	-14,738	17	-32
Max	5,204	6,104	3,965	1,275	-7	53	-9
Min	37	46	39	-45	-2,427	-11	-42

Source: Bank of Spain.

September 2015 it contracted by 32% (14,738), returning to the number of branches that existed 31 years earlier, in 1984. Since the start of the crisis, the network has shrunk in all of Spain's provinces, without exception.

However, the provincial-level analysis reveals important differences in the intensity of the adjustment during the crisis, with a range of variation which goes from a minimum of -9% (in Cuenca) to a maximum of -42% (Castellón). In four provinces the branch network has contracted by more than 40% (Castellón, Barcelona, Girona and Ourense).

The data show that, in general, the biggest number of office closures has taken place in those regions in which the network grew most during the years of expansion. This is the logical consequence of the correction of the imbalances that had built up. Specifically, there is a 90% correlation between the changes in the branch network between 2000 and 2008 and those taking place between 2008 and 2014.

In terms of the population served by a bank branch, network density has declined over the course of the crisis, with a rise in the number of inhabitants per branch from 998 in 2008 to 1,481 in September 2015 (a 48% increase).

Nevertheless, there are significant differences between provinces in terms of network density, with a range of variation that goes from a minimum of 690 inhabitants per branch in Teruel to a maximum of 2,386 in Cádiz (see Exhibit 2). In general, those provinces with the densest networks are the most densely populated (a 90% correlation using 2015 data), which shows the importance of population density in explaining the differences in network density between provinces.

In order to look at market concentration, Table 3 contains the values for the market share of the 1, 3 and 5 largest deposit-taking institutions in each province in 2008 and 2014 and shows the

changes taking place between the two years. In the case of CR_1 , with just a few exceptions, the value of the index rose between 2008 and 2014, varying between a minimum of 19% (Badajoz) and a maximum of 46% (Teruel) in 2014. It is noteworthy that in seven Spanish provinces, a single deposit-taking institution accounts for more than 35% of all branches, and there are two provinces in which a single institution has a share of 40% or more (Teruel and Cáceres). By contrast, in 2008, in just four provinces, one entity accounted for more than 35% of branches and in no province did a single entity account for more than 40%.

The number of competitors tends to be small in those provinces with a low population density and high concentration. Specifically, in 2014, in six of these provinces (Huesca, Teruel, Segovia, Soria, Ceuta and Melilla) fewer than 10 deposit-taking institutions had branches. Conversely, in provinces such as Madrid, Barcelona, and Valencia, the number of competitors exceeded 40 (over 80 in Madrid).

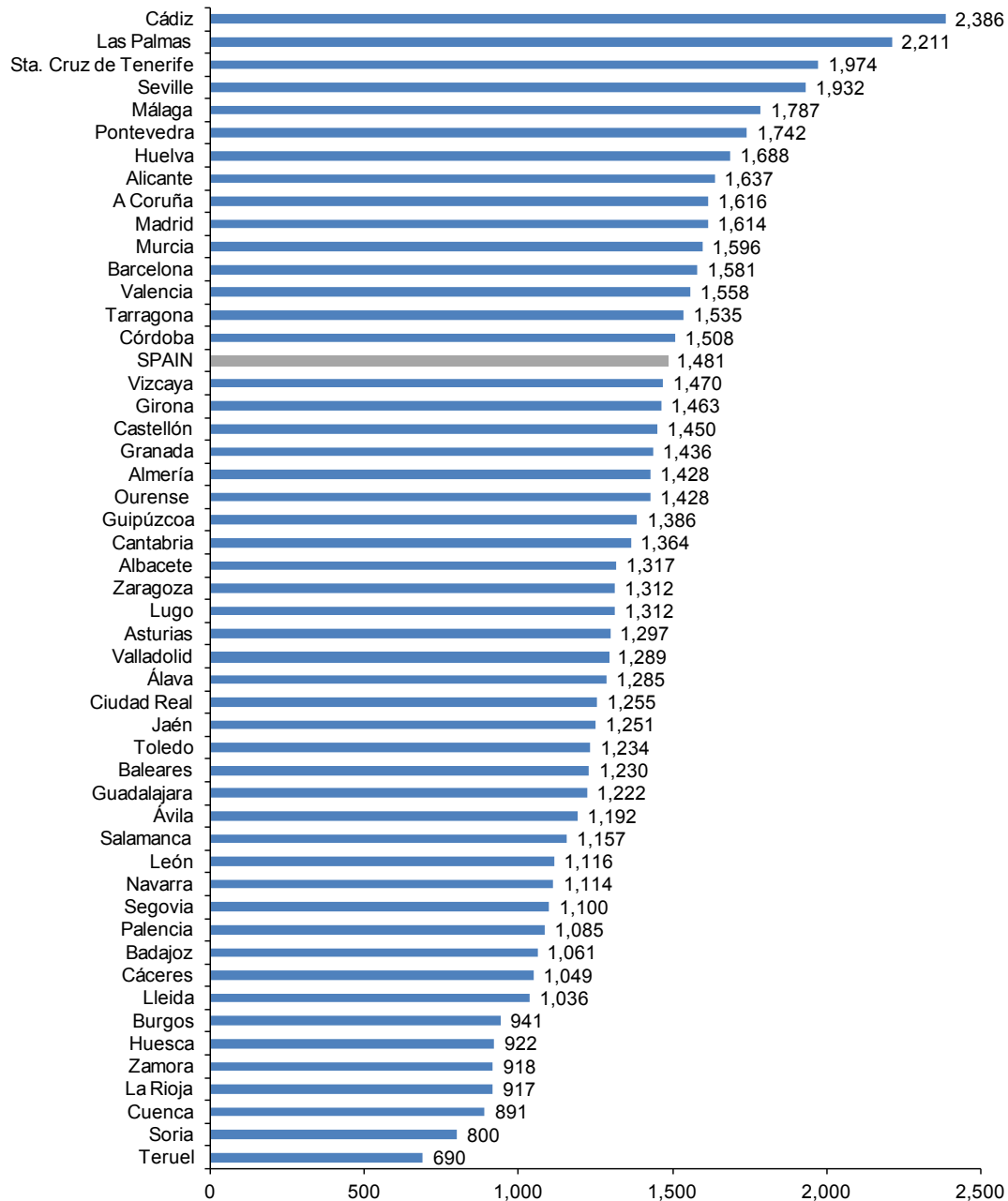
Taking CR_5 as the reference (as is usually done at national level) all Spain's provinces saw an increase in concentration during the crisis, with a maximum increase of 31.6% (Barcelona) and a minimum of 0.6% (Ciudad Real). In eight provinces, CR_5 rose by more than 20%. In 2014, the highest concentration in terms of this indicator was again in Teruel (not taking into account the autonomous cities of Ceuta and Melilla) and the lowest was in Badajoz.

Analysis of HHI is more interesting given its advantages over CR_i absolute concentration indicators. In this case, there are again significant differences between provinces, with a range of variation in 2014 of between a maximum of 3,421 (Teruel) and a minimum of 1,122 (Badajoz).

Between 2008 and 2014, HHI increased in all provinces but one (Ávila), more than doubling in Zaragoza. In 16 of the total 52 provinces, concentration rose by more than 50%.

Exhibit 2

Population per bank branch in the Spanish provinces. September 2015



Sources: Bank of Spain, INE and author's calculations.

Table 3

Market share in terms of bank branches of the 1,3 and 5 largest deposit-taking institutions

	CR ₁			CR ₃			CR ₅		
	2008 (%)	2014 (%)	Variation (pp)	2008 (%)	2014 (%)	Variation (pp)	2008 (%)	2014 (%)	Variation (pp)
Álava	28	31	3.3	47	68	20.9	65	76	10.7
Albacete	26	25	-1.1	60	61	0.9	66	80	14.7
Alicante	19	25	6.4	37	53	16.8	50	76	26.1
Almería	26	34	8.5	52	59	6.5	62	77	15.2
Asturias	22	24	2.0	49	56	6.9	67	77	10.2
Ávila	40	33	-6.5	61	58	-3.2	74	76	2.6
Badajoz	19	19	-0.6	41	46	5.6	56	66	9.8
Balearic Islands	20	23	3.3	50	56	6.4	65	73	7.8
Barcelona	22	28	6.6	40	59	19.4	52	83	31.6
Burgos	28	33	4.2	61	68	7.6	71	82	11.0
Cáceres	37	40	3.3	58	63	4.9	71	76	5.3
Cádiz	19	30	10.4	44	56	12.6	59	76	16.9
Cantabria	29	32	3.1	60	70	10.1	74	84	10.2
Castellón	18	21	3.6	41	52	10.5	57	72	14.3
Ciudad Real	23	23	0.0	54	51	-3.0	73	73	0.6
Córdoba	28	29	1.1	53	59	6.5	66	77	11.6
Coruña, A	23	30	6.8	44	58	13.7	61	83	22.0
Cuenca	31	31	0.1	68	73	4.8	78	87	9.7
Girona	21	34	13.3	47	62	15.4	60	84	23.9
Granada	31	29	-2.1	62	68	6.3	71	81	9.5
Guadalajara	24	30	5.4	58	68	10.6	67	82	15.1
Guipúzcoa	22	25	2.9	46	52	5.3	63	70	7.4
Huelva	33	34	0.7	55	68	13.1	68	83	15.0
Huesca	28	39	10.9	65	80	14.9	77	91	14.2
Jaén	22	27	5.1	48	69	21.1	68	80	11.7
León	23	26	3.5	45	49	4.3	62	71	9.2
Lleida	27	32	4.2	48	60	12.3	63	79	16.8
Lugo	24	30	6.4	45	56	10.9	63	80	17.0
Madrid	18	20	1.4	41	53	12.0	55	70	16.0
Málaga	22	27	5.4	39	50	10.6	50	68	17.4
Murcia	18	25	6.2	48	61	13.4	63	80	17.0
Navarra	26	31	4.9	54	64	10.0	69	89	19.7
Ourense	30	39	8.7	58	65	6.8	70	86	16.2
Palencia	21	35	13.7	47	67	20.0	67	86	18.1
Palmas de Gran Canaria, Las	21	22	0.8	43	59	16.1	60	81	21.7
Pontevedra	26	31	5.2	45	58	13.4	63	80	17.6
Rioja	23	30	7.1	51	58	6.9	62	78	16.8
Salamanca	25	31	6.5	53	70	16.5	77	79	2.0
Santa Cruz de Tenerife	28	37	8.7	50	82	32.2	71	90	19.0
Segovia	39	39	-0.1	61	70	8.6	76	89	13.5
Seville	25	31	6.3	46	58	11.9	60	77	16.5
Soria	32	33	0.6	73	72	-0.9	79	85	5.7
Tarragona	23	32	9.2	51	68	17.7	66	87	21.2
Teruel	37	46	9.1	76	89	13.2	90	95	4.7

Table 3 (continued)

Market share in terms of bank branches of the 1, 3 and 5 largest deposit-taking institutions

	2008 (%)	CR ₁ 2014 (%)	Variation (pp)	2008 (%)	CR ₃ 2014 (%)	Variation (pp)	2008 (%)	CR ₅ 2014 (%)	Variation (pp)
Toledo	26	29	2.2	58	56	-2.0	72	79	6.3
Valencia	16	21	5.2	37	52	15.0	50	71	21.4
Valladolid	18	28	10.3	41	54	12.7	57	76	19.0
Vizcaya	23	27	4.1	46	55	9.6	62	78	16.4
Zamora	26	33	6.7	62	74	12.0	87	92	5.6
Zaragoza	19	37	18.1	46	68	22.3	61	83	22.8
Ceuta	23	27	4.2	58	68	10.5	81	100	19.2
Melilla	24	32	7.8	57	74	16.5	86	100	14.3
Max	40	46	18.1	76	89	32.2	90	100	31.6
Min	16	19	-6.5	37	46	-3.2	50	66	0.6

Sources: AEB, CECA, UNNAC and author's calculations.

Although the results at the autonomous region level are not given here, due to space constraints,

Is the increase in the level of bank concentration in some provinces a cause for concern?

The potential increase in international competition anticipated in the context of banking union is compatible with the existence of certain niches of market power at the regional level. As we have seen, concentration has increased considerably in some provincial markets, and this has undoubtedly contributed to the drop in the number of competing banks as a result of the mergers that have taken place.⁴ Although concentration does not necessarily imply less competition, the levels reached in some cases raise some concerns.

A useful benchmark to help focus attention when monitoring potentially excessive concentration (or any increase thereof) is the 1,800/200 rule used by the U.S. Department of Justice (2000) to assess mergers. According to this rule, a merger needs closer examination to assess its potential effects on competition if the relevant market HHI exceeds 1,800 points after the merger and if it rises by more than 200. For the ECB (2015) an HHI value in excess of 1,800 implies a high

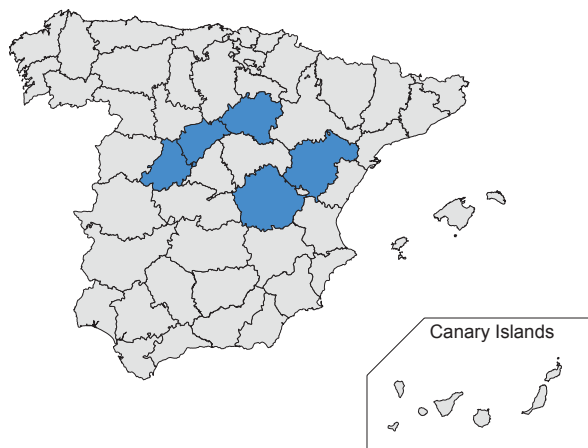
the biggest rise in concentration took place in Aragon, with an increase in HHI of 109%, followed by the Basque Country (103%) and Catalonia (98%). The intense process of branch closures and increase in bank concentration has been driven by the mergers that have taken place between the former savings banks, and the acquisition of banks or savings banks by other entities. In 2014, Aragon was the autonomous region with the highest bank concentration measured in terms of HHI (2,162), followed by Cantabria (2,016). The regions with the lowest concentrations are Andalusia, Extremadura and the Valencia region, with values of below 1,100.

⁴ The number of national banks and savings banks has fallen from 94 in 2008 to 48 in 2014, and the number of credit unions from 81 to 63.

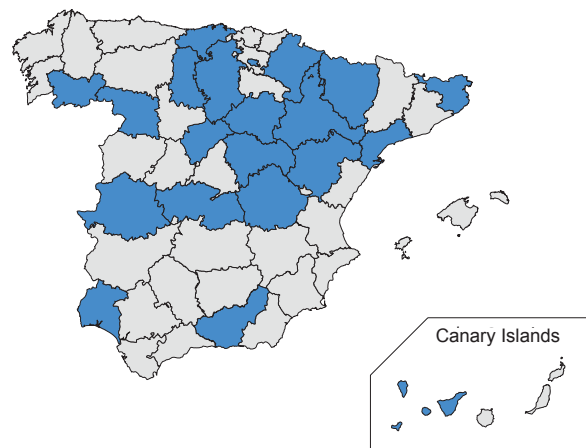
Exhibit 3

Spanish provinces where the HHI exceeded 1,800 in 2014 and the increase between 2008 and 2014 exceeded 200

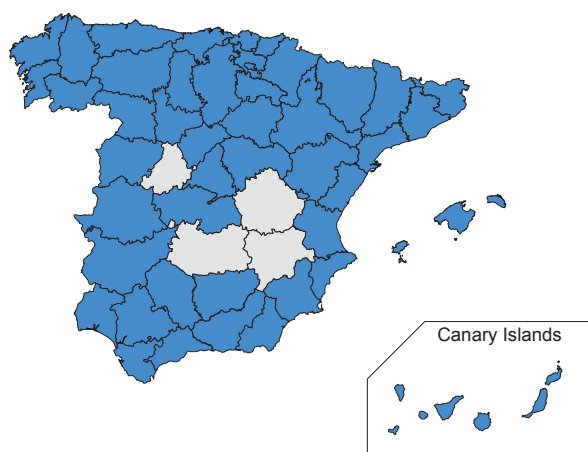
a) 2008: HHI > 1,800



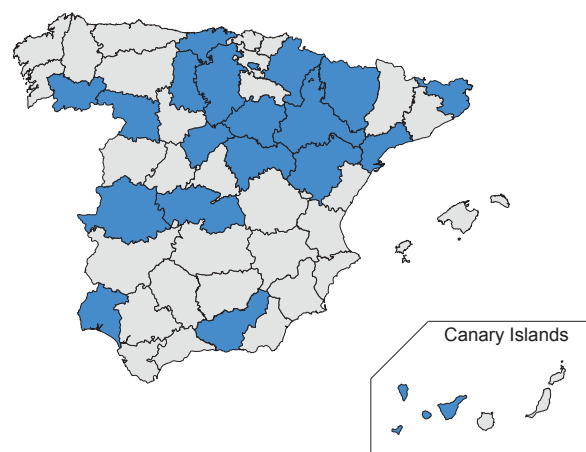
b) 2014: HHI > 1,800



c) Variation 2008-2014 > 200



d) HHI > 1,800 (2014) and variation 2008-2014 > 200



Sources: AEB, CECA, UNNAC and author's calculations.

concentration, while values of between 1,000 and 1,800 imply moderate concentration.

Exhibit 3 shows the application of the 1,800/200 rule more precisely in graphical form. The four panels of the exhibit indicate the provinces in which the increase in concentration between 2008 and 2014 exceeded 200 points, those where it was over 1,800 in both years, and those where it met

both conditions simultaneously in 2014. Based on this rule, from 2008 to 2014, the HHI increased by more than 200 points in 48 of Spain's 52 provinces, and the HHI value in 2014 exceeded 1,800 in 22 provinces. If we consider both thresholds together, the thresholds of this rule are exceeded in 21 provinces. This is the case in Burgos, Cáceres, Cantabria, Gerona, Granada, Guadalajara, Huelva, Huesca, Navarra, Ourense, Palencia, Santa

Table 4

Bank market concentration in the Spanish provinces. HHI

	2008	2014	Variation	Percentage change
Álava	1,184	1,610	426	36
Albacete	1,315	1,497	182	14
Alicante	737	1,280	543	74
Almería	1,240	1,732	492	40
Asturias	1,124	1,424	300	27
Ávila	1,956	1,693	-263	-13
Badajoz	921	1,122	201	22
Balearic Islands	1,089	1,391	301	28
Barcelona	836	1,621	785	94
Burgos	1,622	1,865	243	15
Cáceres	1,764	2,032	269	15
Cádiz	906	1,526	619	68
Cantabria	1,535	2,016	480	31
Castellón	799	1,186	387	48
Ciudad Real	1,298	1,332	34	3
Córdoba	1,286	1,553	266	21
Coruña, A	1,082	1,692	610	56
Cuenca	2,020	2,098	78	4
Girona	1,011	1,862	851	84
Granada	1,577	1,830	253	16
Guadalajara	1,209	1,944	735	61
Guipúzcoa	1,068	1,326	259	24
Huelva	1,538	2,033	495	32
Huesca	1,759	2,633	874	50
Jaén	1,154	1,572	419	36
León	1,055	1,365	310	29
Lleida	1,182	1,710	527	45
Lugo	1,119	1,627	508	45
Madrid	772	1,181	409	53
Málaga	814	1,277	463	57
Murcia	991	1,516	525	53
Navarra	1,328	1,840	512	39
Ourense	1,538	2,016	477	31
Palencia	1,125	1,945	820	73
Palmas de Gran Canaria, Las	956	1,516	559	58
Pontevedra	1,169	1,643	474	41
Rioja	1,192	1,567	375	31
Salamanca	1,275	1,681	405	32
Santa Cruz de Tenerife	1,304	2,089	785	60
Segovia	1,933	2,234	301	16
Seville	1,063	1,584	521	49
Soria	1,873	2,230	357	19
Tarragona	1,154	1,961	807	70
Teruel	2,485	3,421	936	38

Table 4 (continued)

Bank market concentration in the Spanish provinces. HHI

	2008	2014	Variation	Percentage change
Toledo	1,508	1,918	410	27
Valencia	694	1,209	515	74
Valladolid	881	1,436	555	63
Vizcaya	1,029	1,465	436	42
Zamora	1,654	2,285	631	38
Zaragoza	938	2,107	1,169	125
Ceuta	1,391	1,860	469	34
Melilla	1,474	2,078	604	41
Max	2,485	3,421	1,169	125
Min	694	1,122	-263	-13

Sources: AEB, CECA, UNNAC and author's calculations.

Cruz de Tenerife, Segovia, Soria, Tarragona, Teruel, Toledo, Zamora, Zaragoza and Ceuta and Melilla.

As the detailed information in Table 4 shows, in one province (Zaragoza) the increase in HHI exceeds 1,000 points, in five the increase lies between 800 and 1,000 points (Girona, Huesca, Palencia, Tarragona and Teruel) and in seven it is between 600 and 800 (Barcelona, Cádiz, Coruña, Guadalajara, Santa Cruz de Tenerife, Zamora and Melilla). The increase is less than 200 points in just three provinces (Albacete, Ciudad Real and Cuenca). It is worth noting that although in 2008, the HHI exceeded the 1,800 threshold in just five provinces, by 2014 the number had risen to 22.

Conclusions

The profound restructuring undergone by the Spanish banking sector has helped to correct the imbalances that built up in the preceding expansionary phase, making it necessary to resort to mergers as a cost-cutting strategy. Cutting branch networks was a particularly important part of this strategy, given that the number of branches existing at the time of the outbreak of the crisis was incompatible with the deleveraging effort needed by the Spanish economy. As a result of

this correction in installed capacity, the network became less dense, although it remains one of the densest in the EU.

As a consequence of these mergers, the degree of concentration in the Spanish banking market rose sharply, such that although it started at a level below the European average in 2008, it now exceeds it.

The increase in concentration does not necessarily imply a reduction in competition, particularly bearing in mind progress towards banking union. Nevertheless, the relevant geographical dimension when judging competition is often not the national scale, as many entities operate at sub-national levels, being concentrated in one or more regions or even just a few provinces. Moreover, it should be borne in mind that the cuts to the branch network have varied widely between provinces, such that the change in concentration and its current level in provincial markets is also very uneven.

In this context, the construction of banking concentration indices at the provincial level, using the information available on the distribution of the branch network of Spanish deposit-taking institutions at the individual level in 2008 and

2014, allows for an analysis of the impact of restructuring over this adjustment period.

The results yield the following conclusions:

- The restructuring undergone by the Spanish banking sector to correct the imbalances that built up during the preceding expansionary phase has led to a significant increase in market concentration, which is now above the European average. Concentration is much higher than in Europe's largest countries.
- The level of concentration at the national level conceals major differences at the regional level. According to individual information on the provincial distribution of bank, savings bank, and credit union branches, there are now some provinces where the concentration is three times that in others. The differences are bigger still in terms of the increase in concentration that has taken place during the crisis (2008-2014).
- Concentration has increased in almost all Spain's provinces, and in some, the increase has been so intense that it exceeds the thresholds that in other countries would require close examination of the possible consequences for competition. Specifically, in 2014, the HHI value exceeded 1,800 points in 22 of Spain's provinces, a threshold above which concentration is considered high. This substantial number of provinces contrasts with the just five over this threshold in 2008. Moreover, in 21 provinces, concentration has increased by over 200 points and is currently over 1,800, values that, in the United States would require a detailed analysis to assess the potential impact on levels of competition.

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The Spanish banking system: The process of cleaning up property assets

José García Montalvo¹

The recovery of the Spanish economy in 2015 allowed the financial sector to significantly reduce its volume of troubled assets. However, progress was primarily concentrated in a decrease in doubtful loans, as banks continued to accumulate foreclosed assets on their balance sheets.

Various property market indicators point to a recovery in 2015, although below pre-crisis levels – in line with the correction of the sector's imbalances. As in the case of the Spanish economy's overall recovery, the property sector's future remains highly sensitive to global and domestic conditions. Despite current macroeconomic uncertainty, today's interest rate environment may positively impact housing for investment purposes, as current yields represent a profitable alternative to negative returns. As regards banks, there has been a significant drop in exposure to different segments of the property sector relative to pre-crisis levels, but the reduction needs to factor into account the transfer of assets to SAREB. Troubled assets have also been reduced, but this has been due to the fall of NPLs, whereas progress on reducing foreclosed assets has been going very slowly, with the net effect being an accumulation on financial institutions' balance sheets. Finally, latest data reveal a significant reduction in SAREB's portfolio of financial assets; however, the value of its real-estate assets has remained largely unchanged since the initial transfer.

The property market crash and financial crisis affecting the Spanish economy revealed the problems stemming from the Spanish financial system's overexposure to property risk. It is therefore logical that both the speed and the nature of the clean-up process in the financial sector will be very much shaped by trends in the property sector and entities' ability to reduce their exposures. This article reviews recent trends in the Spanish financial sector's property exposures and balance sheet clean-up, and the process of liquidation of property exposures through SAREB.

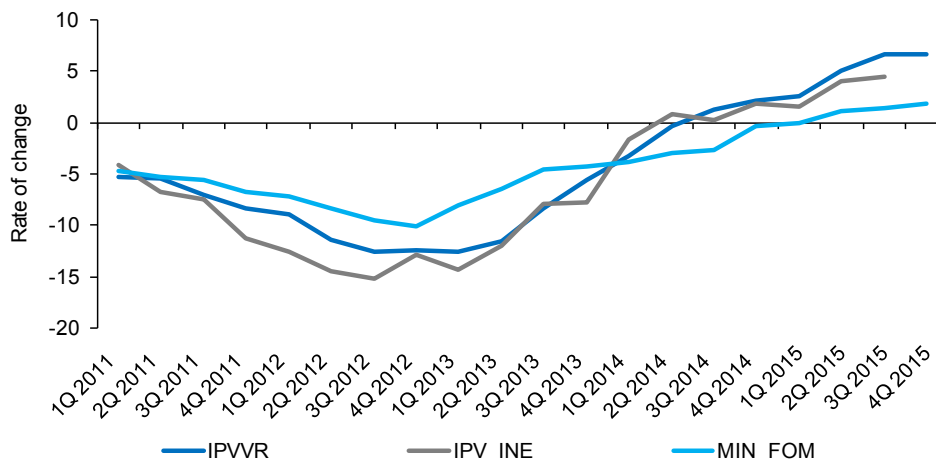
Recent trends in the property sector and lending

The recovery of the property sector is crucial to the financial sector's ability to clean up its balance sheet and the speed of this process. The property sector's figures in 2015 are relatively optimistic, at least when compared to the poor indicators in previous years. Exhibit 1 shows the recent trend in housing prices. Based on the repeat sales indicator, property register statistics situate price growth at 6.6%.

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Exhibit 1

**Recent upward trend in housing prices
(Percentage)**



Sources: Ministerio de Fomento, INE, Registradores de la Propiedad and author's calculations.

National Statistics Institute data show slower progress, although the rate is also significant. Data from the Ministry of Public Works and Transport report an increase of 1.8%, rising to an average of 1,490 euros per square metre. The characteristics of the appraisal prices used by the Ministry of Public Works and Transport for its statistics give less volatile results, as can be seen in Exhibit 1. Appraisal prices dropped more slowly during the decline in prices, which lasted until 2014, and are going up more slowly than property register prices now that property values are rising.

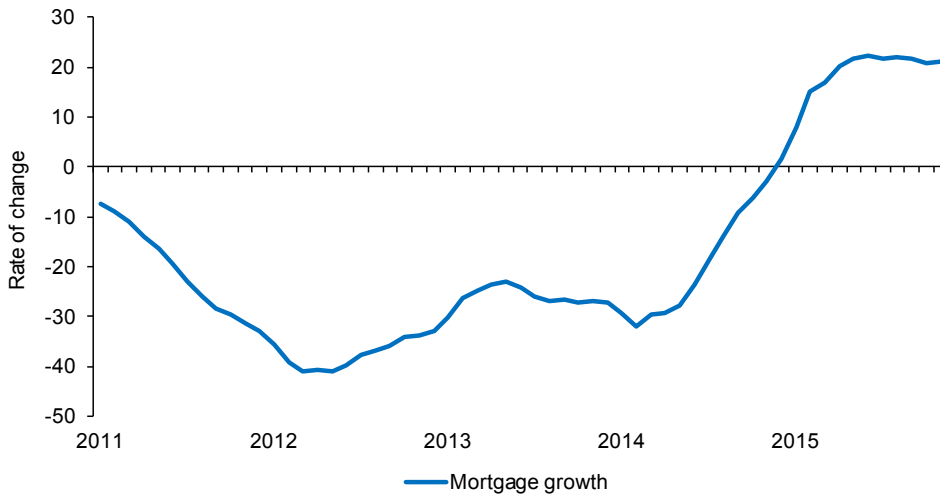
For their part, property registry statistics (Registradores de España, 2016) show that transactions grew by 11.2% in 2015, while new lending to households for home purchases grew by 22.4% in the period to November 2015, while the number of new housing permits rose by the 35.1%. As can be seen, many sector indicators are growing at two-digit rates, although this is a reflection of a property sector returning to a degree of normality after several years of very low activity. Housing transactions still represent just 45% of the 2007 total. New housing starts came to just 7% of the permits issued during

the boom. It is true that the number of workers in the construction sector has grown 12% since the minimum of the first quarter of 2014 until the fourth quarter of 2015, but construction and real estate services had shed 1.7 million jobs since the start of the crisis.

Prices certainly rose significantly in 2015, but property registry prices remain 29% down from the highs reached during the bubble. As Exhibit 2 shows, new mortgages on residential property are growing rapidly, although this is from a low baseline given the small number of mortgages granted in the preceding years. In January of 2016, the growth of new mortgages has gone down to 10.6% from more than 20% at the end of 2015. In view of the double-digit growth of some property-market figures, there has been talk of the possibility of a new bubble forming. However, this is not supported by solid empirical evidence. It could be argued that the battle for the mortgage business is driving rapid growth in new lending, which could push up house prices, as happened during the bubble. However, there are no solid grounds for supporting this hypothesis at this stage. While it is true that there has been intense competition in terms of spreads on mortgages, there has been

Exhibit 2

Mortgages on residential property (Percentage)



Source: INE and authors' calculations.

no relaxation of the requirements for borrowers' ability to pay when granting loans. Relaxing income

In view of the double-digit growth of some property-market figures, there has been talk of the possibility of a new bubble forming. However, there are no solid grounds for supporting this hypothesis at this stage.

requirements and over-appraisals were what caused problems in the past. In fact, to judge from the trend in the Ministry of Public Works and Transport prices shown in Exhibit 1, the over-valuation of the past has given way to under-valuation today.

In any event, like the rest of the economy, the sector's future is highly sensitive to both the global economic conditions and domestic political difficulties in Spain. International geopolitical issues (Syria, Yemen, Ukraine, North Africa, etc.), upheavals in the EU (Brexit and the refugee crisis),

the difficulty of forming a government in Spain, the fall in stock exchanges, or the loss of confidence in China's ability to keep driving the world economy, have all had an impact on Spanish consumers' confidence. The data from the start of the year show a big drop in confidence, driven more by future expectations than the current situation. This loss of confidence will most likely impact general consumption and housing demand. However, for the time being, the economy is still being driven by the momentum from 2015.

Although demand for housing as a durable consumption good may be adversely affected by negative macroeconomic factors, the opposite is true of its performance as an investment. In recent months, assets of all classes have been yielding negative returns. This has been true of equity funds, commodity funds, short-term debt, long-term debt, high-risk corporate debt, and even money-market funds. The only asset class that has yielded positive returns has been housing. Rental yields in Spain's largest cities (Madrid and Barcelona) are around 6.5% and 7%, with capital gains in the past year of 6.6%. This makes

investing in housing an attractive option for many small investors and for some large investment funds. Faced with interest of just 0.2% when their deposits mature, it is not uncommon for customers

The effect of buying as an investment, basically in response to extremely low interest rates narrowing the range of profitable investment alternatives, could act as a counterweight to falling demand for housing bought for the purpose of somewhere to live.

to decide to invest the money in property bought in cash at today's reduced prices. As many as 65% of property purchases have come to be paid in cash in 2014. There was a drop in 2015 as lending for home purchases picked up, although over the last few months, the trend in the number of cash transactions has again tended to be upward. The effect of buying as an investment, basically in response to extremely low interest rates narrowing the range of profitable investment alternatives, could act as a counterweight to falling demand for housing bought for the purpose of somewhere to live.

Meanwhile, the outlook for housing supply is optimistic. Many financial institutions and real-estate platforms have begun to develop highly provisioned foreclosed building land in prime locations. The relationship between banks and developers has also changed. Given the huge problems in the past and the lack of professionalism among some property developers, banks have returned to the standards of the past: before financing a development they require the developer to own the land and to have made a substantial number of sales plans. On this point, word in the sector that some banks have part-financed land purchases could be a cause for concern, as it would represent a return to practices that caused so many problems in the past, when developers did not risk any money of

their own but relied entirely on bank loans to pay for both the land and construction work. However, these practices do not seem to be widespread in the financial sector at present.

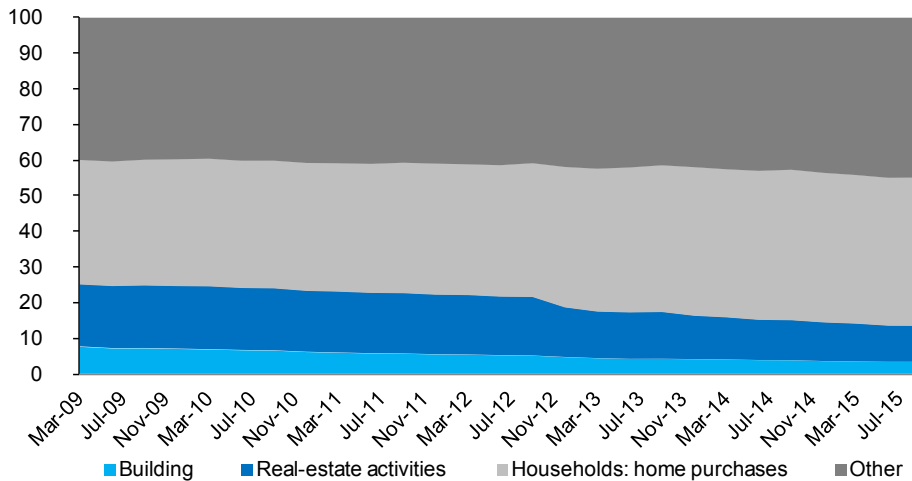
The last question concerns the accessibility of housing. Taking the traditional indicator (mortgage payments as a share of household income) as a guide, the current situation is optimal in terms of low interest rates and the big drop in housing prices in recent years. However, this indicator is not a good measure of a household's effort to buy a home. A better indicator, the ratio of house prices to households' disposable income, remains high by historical and comparative standards (6.3 years of total income to buy an average home), because, although prices have dropped considerably, households' disposable incomes have also fallen in recent years, preventing the indicator from returning to normality (around 4 or 4.5 years). Future adjustment could basically come from increased household incomes, provided the economy does not suffer the negative impact of the current conditions. Prices will also have to slow their rise from the past year's rate, as household incomes seem unlikely to be able to keep pace even if the economy does not lose its momentum.

The banks' property exposure

In the years prior to the property crisis, the Spanish financial sector rapidly increased its exposure to various segments of the property business. In early 2009, the combined exposure to the building industry, the real-estate sector, and lending for home purchases totalled 1.12 trillion euros, or approximately 60% of all lending. Exhibit 3 shows how these three components evolved as a percentage of total credit. A significant drop was observed in the share of lending to the building industry and the real-estate sector, approximately halving from almost 25% of the total to 13.4%. Exhibit 4 shows lending to the building industry and the real-estate sector as a share of total lending for productive activities. It is worth noting

Exhibit 3

Distribution of credit by purpose (Percentage)



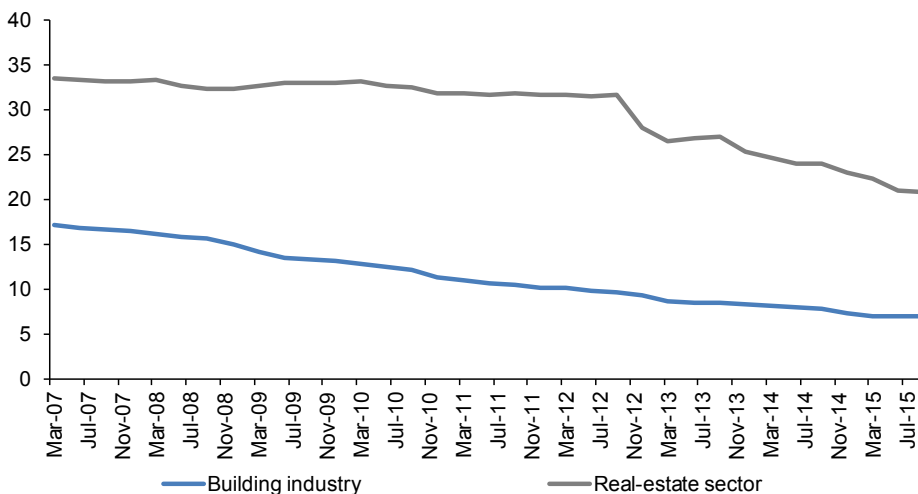
Source: Bank of Spain and author's calculations.

that, as Exhibit 4 clearly shows, part of this drop is due to the transfer of building industry and real-estate sector loans to SAREB in December 2012 and the first quarter of 2013.²

Part of this drop in the share of credit to productive activities relating to the real-estate sector was made up for by the increase in lending to households for home purchases and refurbishment. Their share

Exhibit 4

Credit exposure to the building industry and real-estate sector (Percentage)



Source: INE and authors' calculations.

² Entities in Groups 1 and 2 transferred financial assets for a total value of 39,438 million euros.

of the total went from 35% in January 2009 to 41.6% in September 2015. Obviously, this increase in the share of lending to households for home purchases was accompanied by a contraction in this credit category. However, this was much smaller than the reduction taking place in lending to productive activities in the property sector or in credit in general. Indeed, total lending for housing purchases continued to fall by around 4% at the end of 2015, despite the fact that lending for new home purchases by households rose by over 20%.³ Despite this significant growth, new home loans account for just under 3% of total lending for house purchases, compared with a figure of 31% in 2005. This ratio reveals how low the level of new credit for housing purchases remains in comparison with the situation in the mid-2000s.

Building loans contracted by 14.9% between September 2014 and September 2015, a rate close to that one year earlier (15.1%). The decline in lending to the real-estate sector was similar (13%), although the pace of the reduction was significantly slower than a year earlier (20%).

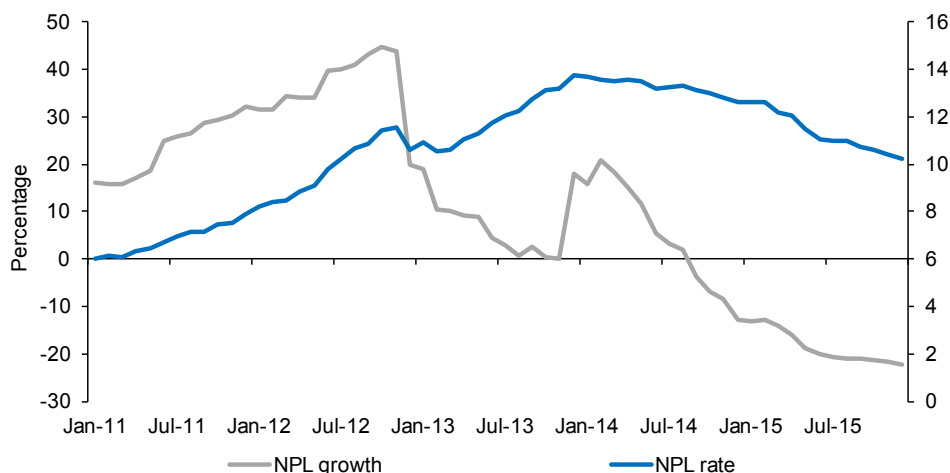
Overall, credit for construction, real-estate activities and housing purchases fell from 1.1 trillion euros in January 2009 to 0.74 trillion in September 2015.

Trends in the NPL rate

The rising non-performing loan rate has been one of the biggest problems the Spanish financial system has faced since the outbreak of the crisis. According to the EC (2016), the NPL rate remains high, but has fallen significantly since 2013. The trend in the NPL rate has passed through several phases. From the onset of the crisis up until end-2012, there was a progressive rise, which was interrupted by the transfer to SAREB in December 2012 and March 2013 of a large share of past-due loans related to the property sector from entities in Groups 1 and 2. The rapid increase up until late 2013 was the result of a reclassification of a large portion of restructured loans as doubtful. In 2015, there was a continuation of the downward trend in the NPL rate that began in 2014. In December 2015, deposit-taking institutions' NPL rate dropped to 10.12%, its lowest level since July 2012 (Exhibit 5).

Exhibit 5

Trend in NPL rate and rate of change (Percentage)

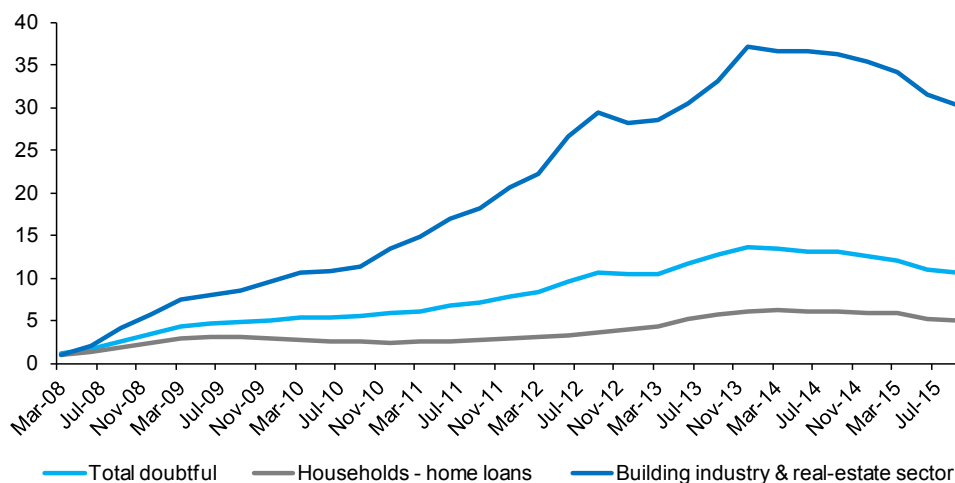


Source: INE and authors' calculations.

³ Only the stock of households' consumer credit is growing.

Exhibit 6

Non-performing loan rate (Percentage)



Source: INE and authors' calculations.

There was a year-on-year reduction of 38,276 million euros in doubtful loans. The NPL rate dropped 3.48 percentage points, down from its peak in December 2013 at 13.6%. The volume of doubtful loans dropped below 130 billion euros for the first time since November 2011. The NPL rate was falling at 22.4% by the end-2015.

Nevertheless, significant differences persist in the NPL rate broken down by purpose of loan (Exhibit 6). Lending to the building industry and real-estate sector continue to present the highest NPL rates and, although they have fallen from their peak of 37% in December 2013, they remain high, at 30%. The NPL rate of households on loans for home purchases or refurbishments has dropped to 5%.

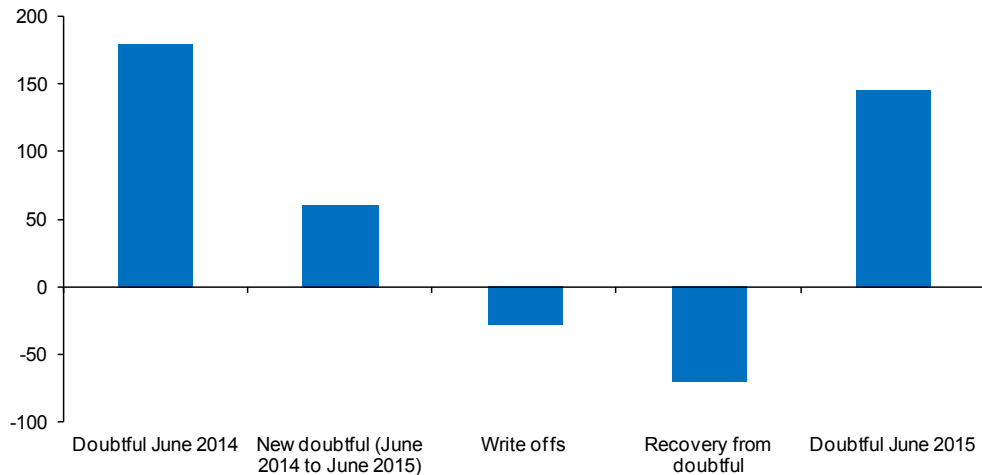
The analysis of the trend in doubtful assets can be deepened by analysing the difference in the volume of doubtful assets at two distinct points in time. Only recently has disaggregated information on flows of loans being classed as NPLs been available, however. Exhibit 7 shows the breakdown in the change in doubtful assets between June 2014 and June 2015. In June 2014, a total of 180

billion euros had accumulated and the following year a further 60 billion euros were classed as non-performing. The writing off of 27 billion euros of bad debt and the recovery of loans worth 69 billion euros (removed from the NPL category) reduced total NPLs to a total of 145 billion in June 2015. Thus, over the period considered, recoveries of doubtful loans exceeded loans newly classified as doubtful, which, in conjunction with the write-off of doubtful loans considered unlikely to be recovered, substantially reduced the NPL balance.

The strength of the various sectors' contribution to reducing the NPL rate has changed over time. Exhibit 8 shows that the lion's share of the drop in the NPL rate between December 2013 and September 2014 (8.4 percentage points) was due to the lower NPL rate on loans for productive activities (almost 80%) - households made a smaller contribution (just 8.6%). The fact that 75% of defaults are concentrated in lending for productive activities undoubtedly explains a significant part of this breakdown. The reduction in the NPL rate between September 2014

Exhibit 7

**Breakdown of changes to doubtful loans
(Percentage)**



Source: Bank of Spain.

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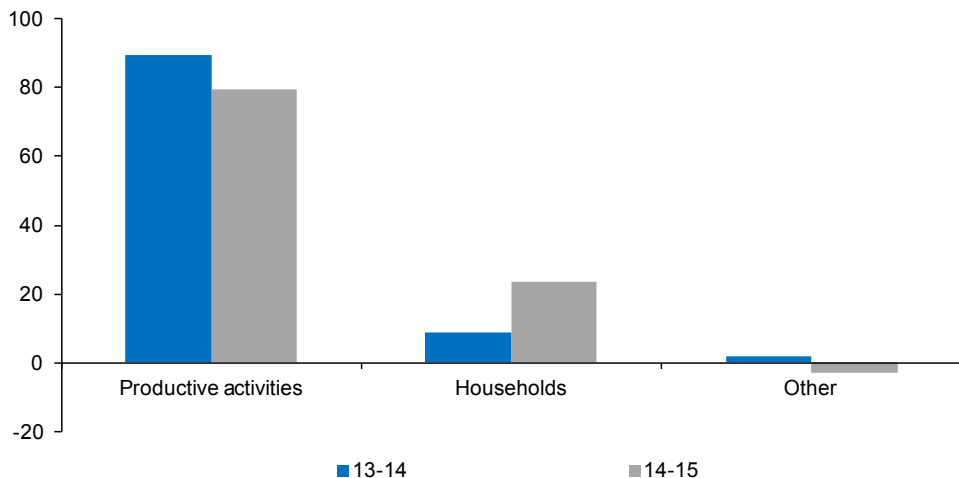
and September 2015 was much bigger (20.8 percentage points) and households accounted for almost 25% of the drop.

Disaggregating the sectors and purposes further to zoom in on lending directly related to the property

sector we find, as Exhibit 9 shows, that almost all of the reduction in the NPL rate between December 2013 and September 2014 was due to lending to the building industry and real-estate sector (94%), while the contribution of lending to households for home purchases and refurbishments was just 5%.

Exhibit 8

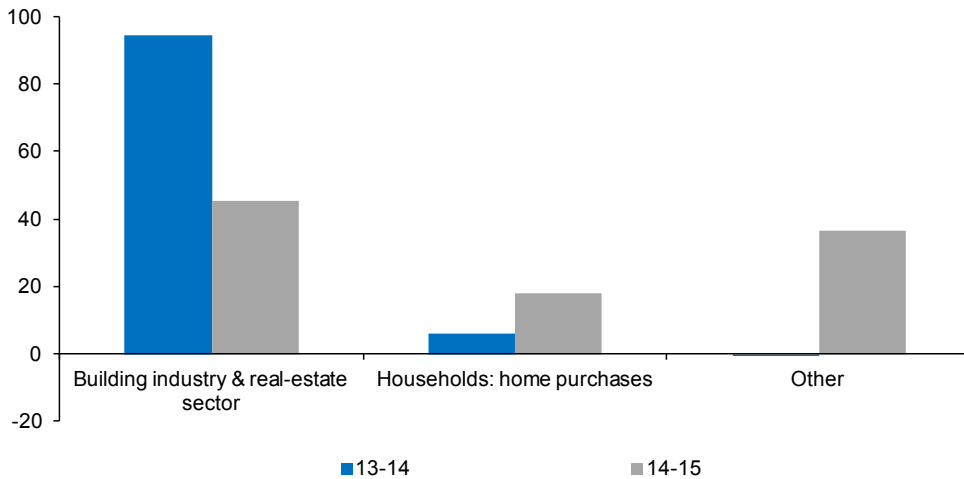
**Contribution to drop in NPL rate
(Percentage)**



Source: Bank of Spain and author's calculations.

Exhibit 9

Contribution to drop in NPL rate (Percentage)



Source: Bank of Spain and author's calculations.

A major part of the significant contribution to the reduction in the NPL rate in the building industry and real-estate sector stems from the way the financial crisis had a more rapid impact on these sectors and the writing off of a significant portion of doubtful loans. Between September 2014 and September 2015 the contribution of firms in the building industry and property services to the reduction in the NPL rate fell to 45%, with the lower NPL rate among households on home loans significantly increasing its share (18%).

The Bank of Spain (2015) has analysed the trend in doubtful loans broken down by company size. The data show that large companies have significantly lower NPL rates than SMEs (14% compared to 23.4%). Indeed, the NPL rate is inversely proportional to company size, reaching 27% among micro-enterprises. The recent fall in the NPL rate was more pronounced among large companies (22%) than SMEs (14.3%).

The NPL rate among businesses in the building industry and real-estate sector is above average, and there is also a significant difference between large companies (24.8%) and SMEs (35.1%).

In the case of these sectors, however, the negative correlation between the NPL rate and size is not always so clear cut: in June 2015, small businesses had a higher rate than micro-enterprises, basically due to the large drop in the NPL rate among micro-enterprises since June 2014. As in the case of non-financial corporations as a whole, the drop in the NPL rate is bigger among large companies than SMEs.

Trends in foreclosures and refinancing

A major part of the Spanish financial sector's non-performing assets are the result of foreclosures or settlement of debts. These represent around 38% of the Spanish financial system's troubled assets in its business in Spain. In this regard, the improvement is not as clear as in the cases of the NPL rate. The volume of foreclosed assets on Spanish financial institutions' balance sheets from business in Spain has stabilised at around 80 billion euros since December 2012 when, following the transfer to SAREB, it dropped from around 100 billion euros. The reduction in foreclosed assets since December 2014 has been proceeding very

slowly, which shows that the sale of property assets from financial institutions' portfolios has been offset by the rising number of foreclosed assets coming onto their balance sheets. Land makes up the largest share of these foreclosed assets, accounting for 35.3% of the total, followed by completed buildings (24.9%) and repossessed homes (21.5%). These proportions have remained fairly stable over time.

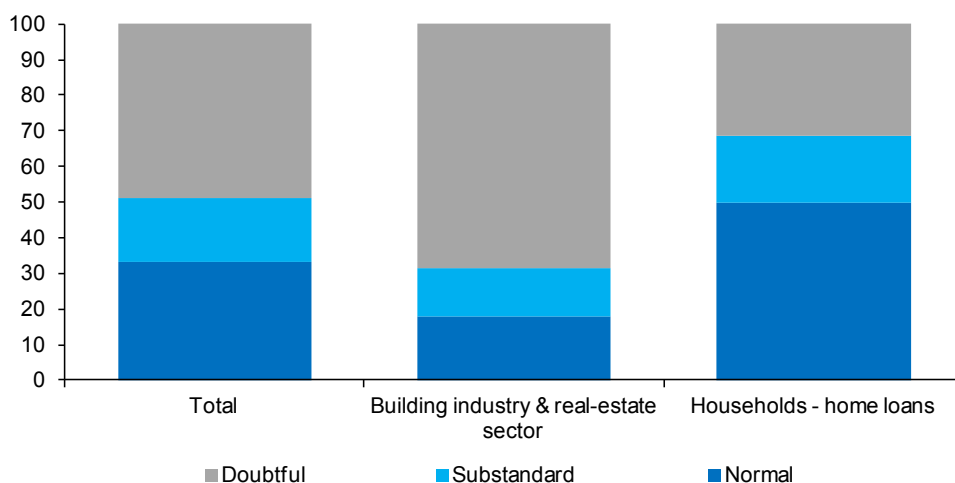
The preview of the major Spanish banks' results at the end of 2015 show no signs of any significant reduction in foreclosed assets. Indeed, several financial institutions show an increase in the number of foreclosed properties, particularly in the segment of real-estate assets from the financing of households for home purchases. This suggests that, despite a slight increase in the sale of properties by most financial institutions, the net effect was a continuing accumulation of properties in 2015. Another trend in the sale of properties by financial institutions, coinciding with

the recovery in property prices, is the reduction of discounts. For example, according to Banco Sabadell, discounts on the sale of its properties dropped from 51% in 2014 to 44% in 2015. For its part, Banco Popular, which saw an increase in the number of foreclosed assets on its books in 2015, reports that online prices have risen by 5% and the capital gain on property sales has gone from -1.8% in the first quarter of 2015 to 2% in the final quarter (with the retail price rising by 2.7%). BBVA indicates that although there has been a reduction in sales of property assets of 9% in 2015, profitability has increased.

The most recent uniform data on refinanced and restructured assets (June 2015) show the volume to stand at 211 billion euros.⁴ There has been barely any improvement with respect to the previous six months, with 49% of these assets being classed as doubtful. 33% of the total refinanced and restructured assets were classed as normal (Exhibit 10).

Exhibit 10

Refinanced and restructured transactions: Classification (Percentage)



Source: Bank of Spain and author's calculations.

⁴ García Montalvo (2015) describes how refinanced and restructured assets have evolved over time.

64% of refinanced transactions concern loans to businesses, while the remaining 36% are loans to households. The breakdown of the refinanced transactions also differs depending on the sector of productive activity and the purpose of lending to households. Among the latter, mortgages for home purchases represent 26% of the total, and approximately 50% of them are classed as normal, while just 30% are classed as doubtful. The situation for construction and property companies is very different, representing approximately 50% of refinanced transactions to companies, and almost 70% of their refinanced transactions are classed as doubtful.

Property risk in SAREB

The transfer of troubled assets to SAREB temporarily reduced the accumulation of these assets on the books of entities formally classed as credit institutions. Nevertheless, bearing in mind the origin of the property risk and the fact that many financial institutions have an equity

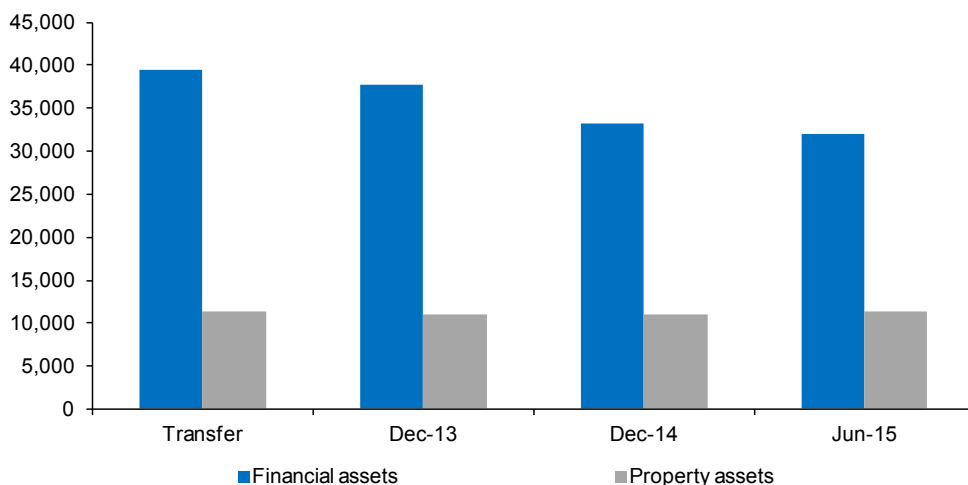
interest in SAREB, it is also worth looking at how it has progressed when considering the property risk facing the economy as a whole. What is more, SAREB is a major player in the market for troubled

The most recent data available reveal a significant reduction in SAREB's portfolio of financial assets. However, the value of its real-estate assets has remained largely unchanged since the initial transfer of assets.

assets (real estate lending and properties) and, as such, its decisions and strategies are relevant to other financial sector agents. The most recent data available reveal a significant reduction in SAREB's portfolio of financial assets.⁵ However, as discussed above, the value of its real-estate assets has remained largely unchanged since the initial transfer of assets. Some of the reduction in financial assets has been due to loans being turned into property assets as a result of foreclosures.

Exhibit 11

Changes in SAREB's assets



Source: SAREB's (2015) financial report.

⁵ García Montalvo (2015) describes the main operations.

Concluding remarks

The reduction in private sector debt in the economy continued in 2015. In particular, lending to the building industry was reduced by 15%, while lending for real-estate activities dropped by 13%. The improvement in the Spanish economy in 2015 allowed the financial sector to significantly reduce the volume of troubled assets. In December 2014, troubled assets (doubtful loans and foreclosed real-estate assets) came to almost 250 billion euros. Non-performing assets were projected to drop below 211 billion euros at the end of 2015. However, the 39 billion euro reduction in troubled assets was concentrated solely in doubtful financial assets. The non-performing loan rate and volume of doubtful loans were falling at a rate of 22.4% at the end of 2015. The most recent data available show that recoveries of doubtful loans are outpacing new non-performing loans, which together with write-offs, explains the substantial drop in the NPL rate.

By contrast, it is foreseeable –based on the 2015 results presented by the major banks– that foreclosed real-estate assets remained stable at the same level as in the preceding half-year periods. Although many financial institutions have pointed to an improvement in the sale of foreclosed assets, properties continue to accumulate on credit institutions' balance sheets, although the prices they are obtaining for them improved over the course of 2015.

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Recent key developments in the area of Spanish financial regulation

Prepared by the Regulation and Research Department of the Spanish Confederation of Savings Banks (CECA)

Bank of Spain Circular on supervision and solvency, completing the adaptation of Spanish legislation to CRD IV and CRR (Circular 2/2016, published in the BOE on February 9th, 2016)

The basic objective of Bank of Spain Circular 2/2016, which was published in the BOE on February 9th 2016, is to complete the implementation in Spanish legislation of the provisions of Directive 2013/36/EU (CRD IV) that concern credit institutions and incorporate one of the options that Regulation (EU) no 575/2013 (CRR) confers on competent national authorities. It also implements certain provisions from the transposition of Directive 2011/89/EU on additional supervision of financial institutions that belong to a financial conglomerate.

The **main points** implemented by the Circular are:

I. Scope

The Circular is **applicable** in general to: (a) consolidated groups and subgroups of credit institutions, defined in CRR, whose parent is established in Spain; (b) individual credit institutions constituted in Spain, integrated in a consolidated group or otherwise; and (c) activities

in Spain of credit institutions based in non-EU countries operating through a branch or under the freedom to provide services.

II. Exposures to public sector entities

For the purposes of calculating capital requirements to address credit risk, the Circular defines those agencies that will be given the same weighting as the central government. It also defines the agencies whose exposures will receive the same weighting as exposures to the government body they belong to.

III. Capital buffers

- It establishes the procedures the Bank of Spain will use to set the percentages for the **countercyclical capital buffer** applicable to exposures in Spain, other EU Member States and non-EU countries.
- It also establishes the procedures the Bank of Spain will use to set **systemic risk capital buffer**.
- It determines the **percentage of global systemically important institutions buffer** (G-SII buffer) that will be applied depending on the category they are placed in. Also, it determines the procedure for identifying **other systemically important institutions** and defining their capital buffers.

IV. Internal organisation

- It sets out the conditions under which the appointments and remuneration committees, on the one hand, and the risks and audit committees, on the other, may be **combined**.
- Entities must have a unit or body responsible for the **risk-management function**.
- It establishes the **procedure for assessing the suitability** of the **members of the board of directors, general managers or similar, and other key staff** of credit institutions, financial holding companies and mixed-activity financial holding companies.
- As regards **incompatibilities**, it is provided that if an institution's total **volume of assets at the individual level exceeds 10 billion euros** on the closing date of the two immediately preceding financial years, the members of the board of directors and managing directors and similar officers in the institution and its parent financial holding company or parent mixed financial holding company, may not hold more positions simultaneously than in any of the following combinations: (a) 1 executive position + 2 non-executive positions; or (b) 4 non-executive positions.
- It also stipulates that entities are to prepare an **annual report** on the internal assessment of the **remuneration** policy and identifies the entities to which this requirement is applicable.

V. Internal capital adequacy assessment and treatment of risks

- The Circular specifies the regulations for the **internal capital adequacy assessment** report and how it is to be prepared, along with the **supervisory review and evaluation** process, describing the points this review is to cover.

- It implements various provisions of Royal Decree 84/2015 concerning **risk handling**.

VI. Financial conglomerates

- Groups in which the group's largest financial sector is the banking and investment services sector, and those in which the group's earnings from its insurance sector are 5% or more of its total, or three billion euros, are required to comply with the Bank of Spain's reporting obligations regarding the identification of **financial conglomerates**.
- The coordinator will classify the financial groups in categories and require them to maintain a particular volume of own funds according to their category.
- Groups' obliged entities are to inform the coordinator of the financial conglomerate's supervision each semester of any exposures that, **aggregated to the level of the financial conglomerate, exceed 10% of its own funds, and, in any event, the twenty largest aggregated exposures**.
- Groups' obliged entities are to report each semester to the coordinator for supervision of the financial conglomerate on all intragroup transactions conducted by regulated entities in the banking and investment services sector or regulated entities in the insurance sector, with any other counterparties in other sectors **exceeding 5% of the own funds of the financial conglomerate concerned**. To this end, the Circular sets out the minimum information they are to send for each transaction.

VII. Disclosure requirements to the market and the Bank of Spain

- In the case of **market disclosure requirements**, the Circular defines the information entities' websites are to provide on corporate governance and remunerations, and their configuration.

- Entities must be able to **inform the Bank of Spain** about the composition of the assets, liabilities and equity reflected in their financial statements and, where applicable, other balances used when calculating own funds and their requirements.

VIII. Transitional and repealing provisions

- Transitional arrangements have been established for other systemically important institutions' capital buffers.
- In the case of **securitisations** formalised between July 7th, 2014, and the entry into force of the Circular, originating entities seeking to apply the treatment established in CRR when calculating their capital requirements for these securitisations must provide the Bank of Spain with information on these securitisations using the standard format included in the Circular.
- Credit institutions will have **three months from the entry into force of the Circular to publish information about their corporate governance and remuneration policy on their website**.
- The Circular repeals the existing **Solvency circular** although it leaves some aspects of it in force.
- The Circular came into effect on February 10th.

Bank of Spain Circular amending the Circular on information regarding discount rates and interchange fees charged (Circular 1/2016, published in the BOE on February 6th, 2016)

Circular 1/2016 of January 29th, 2016, which was published in the BOE on February 6th, 2016, amends Circular 1/2015, which established the content of the information on discount rates and interchange fees to be provided to the Bank

of Spain by payment service providers (PSPs) regarding card payment transactions, establishing the data to be published by the Bank of Spain and service providers on their websites, and the first statements to be filed.

The Circular's objective is to amend the interchange and discount statements envisaged in Circular 1/2015, of March 24th, 2015, introducing improvements in the information requested on interchange fees and discount rates charged by entities in order to facilitate their analysis and comparability.

The first statements to be submitted to the Bank of Spain in the new format are those for the **last calendar quarter of 2015**.

As regards the **publication of discount rates and interchange fees**, Circular 1/2015 provided that the Bank of Spain would publish on its website in **aggregate form** all the information received quarterly from institutions, except that on discount rates charged on three-party card payment systems. The new Circular specifies that the Bank of Spain will publish the information received but unpublished prior to the entry into force of the Circular in **individual and aggregate** form in the new statement format.

Draft Bank of Spain Circular on amending Accounting Circular (Circular 4/2004) and Central Credit Register Circular (Circular 1/2013)

On January 22nd, the Bank of Spain published a draft Circular updating Annex IX of the Accounting Circular and introducing changes in the Circular regarding the Bank of Spain's Central Credit Register.

The aim is to adapt the Accounting Circular to the **latest regulatory developments**,¹ while

¹ Commercial Code, Royal Decree 878/2015, FINREP, and accounting guidance of the Basel Committee on Banking Supervision.

ensuring it remains compatible with the IFRS accounting framework.

The **main changes** relate to the following:

- Summarise the changes in the Bank of Spain's organisation chart taking place in 2015.
- In the case of the sale of capital instruments, the change in ownership is now deemed to take place on the settlement date rather than the contract date.
- New accounting criteria for the amortisation of **intangible assets**. In the case of individual and consolidated annual accounts not subject to IFRS, these assets will be considered to have a defined lifetime (ten years if it cannot be estimated reliably).
- Adapt the confidential and public statements to the amendments in the Circular and add new statements.
- Modify the content of the Bank of Spain's **Central Credit Register** collateral data module.

The main features of the **new Annex IX** are:

- **General provisions** for standard exposures will be estimated collectively and **specific provisions** for doubtful risks may be estimated individually or collectively, depending on whether a series of conditions are met. The principles are also established for: (i) **estimates of allowances and provisions** (governance and integration with management, effectiveness and simplicity, documentation and traceability) and (ii) development of own proprietary methodologies for **individual estimation** of specific provisions and internal methodologies for **collective estimation** of specific and general provisions.
- **Classification of operations according to credit risk due to insolvency** into the

following categories: standard, doubtful, and write-off. The **substandard category** has been eliminated and a **new subcategory of exposures subject to special monitoring** has been added within the standard exposures category. It also introduces a carry-over effect whereby transactions involving a party that has accumulated refinancing or restructuring transactions are reclassified in the standard exposures under special monitoring category.

- When calculating **allowances and provisions for credit risk due to insolvency**, estimates must be consistent with the downgrading of the risk category and must take into account the existence of effective guarantees. Moreover, the value of the collateral will be calculated applying a haircut to the collateral appraisal. The Bank of Spain has also included a series of **practical solutions** with which to estimate specific allowances or provisions for doubtful exposures and general allowances and provisions for standard exposures. These solutions will be kept up to date.
- Criteria are included for estimating the **adjusted appraisal value** of real estate assets foreclosed or received in payment of debt, allowing: (i) allowances and provisions on financial assets applied to be released; (ii) reversion of cumulative impairment since the initial recognition of the foreclosed asset under some circumstances.

The Circular **will come into force on June 30th, 2016**, except for certain provisions concerning statements, which will come into effect later. Notwithstanding the above, institutions are to **apply the new accounting criteria retroactively** as a change in accounting criteria and report on their impact on their individual and consolidated annual accounts for 2016. If this is not practical, there will be the option to apply it as a change of estimation prospectively (reporting on this in the notes to the individual and consolidated financial statements for 2016).

Spanish economic forecasts panel: March 2016¹

Funcas Economic Trends and Statistics Department

The forecast for 2016 remains unchanged at 2.7%

The limited information available so far about the first quarter of 2016 generally points towards a slowdown in growth. The consensus forecast for this period estimates a quarter-on-quarter growth rate of 0.6% (Table 2), which is expected to remain stable for the rest of the year. The forecast for the year as a whole is for growth of 2.7%, which is unchanged from the last Panel forecast, and in line with international organisations' projections.

The composition of this growth has been altered slightly. A contribution to domestic demand of 2.8 percentage points is now expected –as against 2.9 pp in the previous Panel– along with a contribution from the external sector of -0.1, one tenth of a percentage point less negative than in the previous consensus forecast. Expected export and import growth have both been reviewed downwards significantly.

The forecast for 2017 is 2.3%

This Panel offers forecasts for 2017 for the first time. GDP growth is expected to be 2.3%, deriving from a contribution of 2.4 pp from domestic demand and -0.1 pp from the external sector. The

quarterly growth rate is expected to remain stable at around 0.6% throughout the period.

Strong growth in the manufacturing industry

January's industrial production index was somewhat weak, prolonging the decelerating trend this indicator has been showing for some months. The growth rate remains high, however. The year-on-year rate for the general index was 3.2%, while the manufacturing index showed much higher growth, at 6%, as the energy subsector has fallen sharply since the middle of last year. Based on social security affiliation numbers, job creation in the sector was also strong in both January and February.

The consensus forecast for IPI growth in 2016 has been revised downwards one tenth of a percentage point to 3%, and IPI growth in 2017 is forecast at 2.7%. Both these figures are well above the average for the pre-crisis growth period.

Falling oil prices mean inflation is lower than expected

February's inflation rate was again lower than expected, at -0.8%, held down by falling prices of

¹ The Spanish Economic Forecasts Panel is a survey run by Funcas which consults the 16 analysis departments listed in Table 1. The survey, which has taken place since 1999, is published bi-monthly in the first half of January, March, May, July, September and November. The responses to the survey are used to produce a "consensus" forecast, which is calculated as the arithmetic mean of the 16 individual contributions. The forecasts of the Spanish Government, the Bank of Spain, and the main international organisations are also included for comparison, but do not form part of the consensus forecast.

energy products and foodstuffs. The consensus forecast for the annual average rate in 2016 has been revised downwards significantly to 0%, seven tenths of a percent lower than in the previous Panel. An annual rate of 1.3% is forecast for 2017. The December 2016 and 2017 year-on-year rates were 0.6% and 1.3%, respectively (Table 3).

Positive trend in employment

According to social security affiliation numbers, employment grew in January at a similar rate to previous months, but slowed in February. Nevertheless, this slowdown was due to the drop in agricultural sector employment caused by the olive harvest ending early and the freeze on public sector recruitment. Excluding the agricultural sector and public-sector employment to obtain a clearer view of the underlying trend in employment, the result is in line with previous months, despite the signs of an economic slowdown that may be observed in other activity and demand indicators.

Employment is expected to grow by 2.4% in 2016—unchanged from the previous Panel—while the forecast for 2017 is 2.1%. Using consensus estimates for GDP, employment and wage growth to deduce the implicit productivity and unit labour cost growth estimates, productivity per worker is expected to grow by 0.3% in 2016 and 0.2% in 2017, while ULCs are expected to change by 0.7% in 2016 and 0.9% next year.

The current account surplus will shrink in 2016

There was a surplus of 1.5% of GDP on the current account of the balance of payments in 2015, compared with 1% the previous year. This improvement is partly the result of a declining energy balance deficit, due to falling oil prices, and also the smaller negative balance on the income and transfers account, owing to smaller interest payments abroad.

The consensus forecast for the current account balance is for a surplus of 1.4% of GDP in 2016, three tenths higher than forecast in the previous Panel, and 1.2% in 2017.

The government deficit will overshoot the target by a few tenths of a percent

In the period to November 2015, the combined deficit of the central government, the social security funds, and the autonomous regions came to 41.8 billion euros, 5.4 billion euros less than in the year-earlier period, a figure equivalent to 3.87% of annual GDP. This result is still under the 4.2% target, but given December's highly negative seasonality, particularly in the case of the social security accounts, the deficit will overshoot the target.

In line with the consensus forecasts for 2016 and 2017, the result will also exceed the targets established for both years (2.8% and 1.4%, respectively). A deficit of 3.5% of GDP is forecast for this year and 2.7% for 2017.

The perception of the global economy remains negative

In recent weeks, there has been an easing of the strains financial markets suffered in January, while expectations of further interest rate rises in the United States have receded, and the European Central Bank has stepped up its QE policy. In any event, the situation in China and other emerging economies continues to cause concern, while job growth in the United States remains strong, despite the signs of weakness in other indicators.

The majority view of the current situation in the EU among panellists is that its impact on the Spanish economy is neutral, as in previous panels, and this is not expected to change in the coming months. As in the previous Panel, the situation outside

the EU is mainly considered unfavourable, and is expected to remain so over the coming months.

Long-term interest rates are too low

Short-term interest rates (three-month EURIBOR) remain in negative territory, and even the one-year rate has dropped below 0%. As in previous Forecast Panels, interest rates are still felt to be too low for the state of the Spanish economy, but they are expected to remain stable over the coming months.

Since the start of the year, the long-term rate (Spanish ten-year bonds) has been in the 1.6% to 1.8% range, with a widening of the spread relative to German bonds. Most panellists continue to think this level is very low, but expect it to remain stable over the coming months.

The euro continues to depreciate

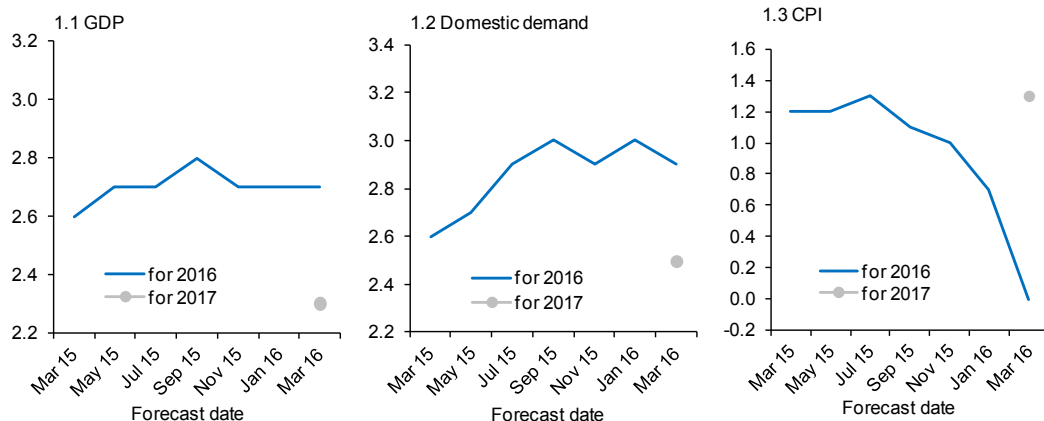
The euro remains over 1.09 dollars, where, for the time being, it seems to have bottomed out. Most panellists consider the level to be appropriate, but expect a downward trend over the next few months.

Fiscal policy is neutral

There has been a shift in the Panel's opinion on the current fiscal policy stance. This was previously considered expansionary, but is now felt to be neutral, which the majority of panellists considers appropriate. As regards monetary policy, there is still unanimity that it is expansionary, and that this is the appropriate stance.

Exhibit 1

Change in forecasts (Consensus values) (Percentage annual change)



Source: Funcas Panel of forecasts.

Table 1

Economic Forecasts for Spain – March 2016

(Average year-on-year change, as a percentage, unless otherwise stated)

	GDP		Household consumption		Public consumption		Gross fixed capital formation		GFCF machinery and capital goods		GFCF Construction		Domestic demand	
	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017
Analistas Financieros Internacionales (AFI)	2.7	2.3	2.9	2.1	1.6	1.3	5.0	4.9	7.0	6.1	4.6	4.9	2.9	2.5
Banco Bilbao Vizcaya Argentaria (BBVA)	2.7	--	2.9	--	0.4	--	5.5	--	6.3	--	5.0	--	2.9	--
Bankia	2.8	2.3	3.0	2.2	2.0	1.3	4.8	4.3	8.2	6.8	3.2	3.0	3.2	2.5
CaixaBank	2.8	2.1	2.9	2.1	0.4	-0.7	4.6	3.7	6.5	3.6	3.7	3.8	2.7	1.9
Cemex	2.8	2.5	3.1	2.6	1.4	2.0	5.1	4.6	6.0	4.8	4.9	5.2	3.1	2.8
Centro de Estudios Económica de Madrid (CEEM-URJC)	2.6	2.4	2.9	2.6	1.5	1.2	4.4	3.7	4.6	4.1	4.8	3.8	2.8	2.5
Centro de Predicción Económica (CEPREDE-UAM)	2.3	2.2	2.5	2.2	1.7	1.2	4.3	4.7	6.3	5.2	3.1	4.8	2.7	2.7
CEOE	2.7	2.5	2.9	2.3	1.2	1.5	5.1	4.1	7.2	5.1	4.3	3.8	2.8	2.4
Funcas	2.7	2.3	3.3	2.6	2.0	1.3	4.3	3.9	6.2	4.8	3.6	3.8	3.2	2.5
Instituto Complutense de Análisis Económico (ICAE-UCM)	2.8	2.4	2.9	2.5	1.0	1.2	4.9	4.0	6.7	5.0	3.0	2.7	3.0	2.5
Instituto de Estudios Económicos (IEE)	2.8	2.4	2.9	2.2	1.8	1.6	4.2	3.0	6.6	3.8	3.1	2.6	2.7	2.3
Instituto Flores de Lemus (IFL-UC3M)	2.8	2.1	3.1	3.1	1.0	-1.0	4.6	4.9	7.4	8.6	3.2	3.1	2.9	2.5
Intermoney	2.6	2.1	2.9	2.1	1.1	1.4	4.3	2.9	5.1	3.9	3.5	2.0	2.8	2.2
Repsol	2.8	2.5	2.9	2.5	1.1	2.4	4.8	4.9	7.1	5.6	3.5	4.6	3.0	2.9
Santander	2.9	2.3	3.0	2.1	1.7	1.2	5.7	4.5	6.2	3.0	5.7	5.7	3.2	2.4
Solchaga Recio & asociados	2.6	2.3	3.0	2.4	0.8	0.5	4.9	4.6	7.6	6.9	3.7	3.7	3.0	2.5
CONSENSUS (AVERAGE)	2.7	2.3	2.9	2.4	1.3	1.1	4.8	4.2	6.6	5.2	3.9	3.8	2.9	2.5
Maximum	2.9	2.5	3.3	3.1	2.0	2.4	5.7	4.9	8.2	8.6	5.7	5.7	3.2	2.9
Minimum	2.3	2.1	2.5	2.1	0.4	-1.0	4.2	2.9	4.6	3.0	3.0	2.0	2.7	1.9
Change on 2 months earlier ¹	0.0	--	-0.1	--	0.3	--	-0.2	--	-0.1	--	-0.8	--	-0.1	--
- Rise ²	4	--	5	--	9	--	3	--	4	--	2	--	4	--
- Drop ²	5	--	8	--	4	--	10	--	10	--	12	--	7	--
Change on 6 months earlier ¹	-0.1	--	0.0	--	0.5	--	-0.6	--	-0.5	--	-1.0	--	-0.1	--
<u>Memorandum items:</u>														
Government (September 2015)	3.0	--	3.0	--	0.3	--	5.4	--	--	--	5.5	--	3.0	--
Bank of Spain (June 2015)	2.7	--	2.3	--	0.1	--	6.1	--	8.9	--	4.5	--	--	--
EC (February 2016)	2.8	2.5	3.4	2.3	0.6	0.6	4.6	4.8	8.0 ⁽³⁾	5.9 ⁽³⁾	--	--	3.1	2.5
IMF (January 2016)	2.7	2.3	--	--	--	--	--	--	--	--	--	--	--	--
OECD (November 2015)	2.7	2.5	3.0	2.4	0.3	1.1	5.1	4.1	--	--	--	--	2.9	2.5

¹ Difference in percentage points between the current month's average and that of two months earlier (or six months earlier).

² Number of panellists revising their forecast upwards (or downwards) since two months earlier.

³ Investment in capital goods.

Table 1 (Continued)

Economic Forecasts for Spain – March 2016

(Average year-on-year change, as a percentage, unless otherwise stated)

	Exports of goods & services		Imports of goods & services		Industrial output		CPI (annual av.)		Labour costs ³		Jobs ⁴		Unempl. (% labour force)		C/A bal. of payments (% of GDP) ⁵		Gen. gov. bal. (% of GDP) ⁷	
	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017
Analistas Financieros Internacionales (AFI)	5.5	4.7	6.8	6.1	--	--	-0.2	1.1	--	--	2.5	2.0	20.1	18.9	--	--	-3.7	-2.7
Banco Bilbao Vizcaya Argentaria (BBVA)	5.2	--	6.0	--	--	--	1.2	--	1.7	--	2.5	--	20.5	--	1.9	--	-3.0	--
Bankia	5.0	4.6	6.4	5.5	2.6	--	-0.1	1.4	0.8	1.1	2.4	2.0	20.0	18.5	--	--	--	--
CaixaBank	5.6	4.9	5.4	4.4	3.9	2.4	0.1	2.2	0.8	1.1	2.5	2.0	19.9	18.5	1.7	1.5	-3.9	-2.1
Cemex	5.4	5.0	6.8	6.4	--	--	-0.2	2.0	--	--	2.7	2.5	20.0	19.0	2.0	1.5	--	--
Centro de Estudios Económica de Madrid (CEEM-URJC)	4.9	5.2	6.0	5.9	--	--	0.1	1.2	--	--	2.1	1.9	20.3	18.7	0.9	0.7	-3.6	-2.7
Centro de Predicción Económica (CEPREDE-UAM)	5.0	4.7	6.4	6.7	2.9	2.5	0.4	1.1	1.2	1.4	1.4	1.2	20.7	19.8	0.4	-0.2	-4.1	-3.4
CEOE	5.3	5.4	5.9	5.6	--	--	-0.4	1.5	1.0	1.0	2.5	2.2	20.0	18.1	2.2	1.8	-3.3	-2.8
Funcas	3.8	4.8	5.7	6.0	2.3	2.4	-0.3	1.5	0.8	1.3	2.4	2.0	19.9	18.2	2.0	1.6	-4.0	-2.9
Instituto Complutense de Análisis Económico (ICAE-UCM)	5.6	5.5	6.0	6.0	2.9	--	0.5	1.3	--	--	2.5	2.1	20.4	19.0	1.7	1.5	-2.7	-1.9
Instituto de Estudios Económicos (IEE)	5.3	5.3	5.4	5.6	2.5	2.1	0.0	1.1	0.6	--	2.1	1.8	20.5	19.5	1.1	--	-3.4	--
Instituto Flores de Lemus (IFL-UC3M)	4.6	3.7	5.2	5.5	3.3	3.8	-0.8	1.1	--	--	2.8	2.9	20.0	18.8	--	--	--	--
Intermoney	4.9	3.7	5.9	4.4	2.8	3.0	-0.4	1.3	--	--	2.3	1.9	20.6	18.9	0.8	--	-3.6	--
Repsol	4.0	5.1	5.2	6.7	3.5	3.1	-0.3	1.2	0.8	1.0	2.8	2.5	20.6	18.5	0.9	1.0	-3.2	-3.0
Santander	4.8	3.9	6.0	4.6	--	--	-0.3	1.1	1.0	1.0	2.5	1.8	19.8	18.0	1.0	0.8	-3.2	-2.0
Solchaga Recio & asociados	4.5	5.0	6.0	5.9	--	--	0.0	1.0	--	--	2.5	2.2	20.1	18.3	1.4	1.4	-3.8	-3.0
CONSENSUS (AVERAGE)	5.0	4.8	5.9	5.7	3.0	2.7	0.0	1.3	1.0	1.1	2.4	2.1	20.2	18.7	1.4	1.2	-3.5	-2.7
Maximum	5.6	5.5	6.8	6.7	3.9	3.8	1.2	2.2	1.7	1.4	2.8	2.9	20.7	19.8	2.2	1.8	-2.7	-1.9
Minimum	3.8	3.7	5.2	4.4	2.3	2.1	-0.8	1.0	0.6	1.0	1.4	1.2	19.8	18.0	0.4	-0.2	-4.1	-3.4
Change on 2 months earlier ¹	-0.5	--	-0.9	--	-0.1	--	-0.7	--	0.0	--	0.0	--	-0.2	--	0.3	--	-0.2	--
- Rise ²	1	--	2	--	3	--	0	--	2	--	2	--	3	--	8	--	1	--
- Drop ²	12	--	13	--	4	--	15	--	2	--	5	--	9	--	1	--	6	--
Change on 6 months earlier ³	-0.3	--	-0.5	--	-0.3	--	-1.1	--	0.0	--	-0.3	--	-0.3	--	0.5	--	-0.3	--
Memorandum items:																		
Government (September 2015)	6.0	--	6.4	--	--	--	--	--	1.4	--	3.0	--	19.7	--	1.2	--	-2.8	-1.4
Bank of Spain (June 2015)	5.7	--	5.9	--	--	--	1.3	--	--	--	2.6	--	--	--	1.1 ⁶	--	--	--
EC (February 2016)	6.1	5.8	7.4	6.2	--	--	0.1	1.5	0.5	1.0	2.6	2.0	20.4	18.9	1.4	1.3	-3.6	-2.6
IMF (January 2016)	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--
OECD (November 2015)	5.1	5.4	5.8	5.8	--	--	0.3	0.9	0.6	1.2	2.7	2.4	19.8	18.2	1.3	1.2	-2.9	-1.8

¹ Difference in percentage points between the current month's average and that of two months earlier (or six months earlier).² Number of panellists revising their forecast upwards (or downwards) since two months earlier.³ Average earnings per full-time equivalent job.⁴ In National Accounts terms: full-time equivalent jobs.⁵ Current account balance, according to Bank of Spain estimates.⁶ Net lending position vis-à-vis rest of world.⁷ Excluding financial entities bail-out expenditures.

Table 2

Quarterly Forecasts - March 2016¹

	Quarter-on-quarter change (percentage)							
	16-1Q	16-2Q	16-3Q	16-4Q	17-1Q	17-2Q	17-3Q	17-4Q
GDP ²	0.6	0.6	0.5	0.6	0.6	0.6	0.6	0.6
Household consumption ²	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6

¹ Average of forecasts by private institutions listed in Table 1.² According to series corrected for seasonality and labour calendar.

Table 3

CPI Forecasts – March 2016¹

Monthly change (%)				Year-on-year change (%)	
Feb-16	Mar-16	Apr-16	May-16	Dec-16	Dec-17
-0.3	0.4	1.1	0.4	0.6	1.3

¹ Average of forecasts by private institutions listed in Table 1.

Table 4

**Opinions – March 2016
(Number of responses)**

	Currently			Trend for next six months		
	Favourable	Neutral	Unfavourable	Improving	Unchanged	Worsening
International context: EU	4	12	0	1	14	1
International context: Non-EU	0	5	11	0	16	0
	Low ¹	Normal ¹	High ¹	Increasing	Stable	Decreasing
Short-term interest rate ²	13	3	0	0	11	5
Long-term interest rate ³	11	5	0	3	10	3
	Overvalued ⁴	Normal ⁴	Undervalued ⁴	Appreciation	Stable	Depreciation
Euro/dollar exchange rate	2	8	6	1	7	8
	Is being			Should be		
	Restrictive	Neutral	Expansionary	Restrictive	Neutral	Expansionary
Fiscal policy assessment ¹	0	10	6	3	7	6
Monetary policy assessment ¹	0	0	16	0	0	16

¹ In relation to the current state of the Spanish economy.³ Yield on Spanish 10-year public debt.² Three-month Euribor.⁴ Relative to theoretical equilibrium rate.

KEY FACTS:

- ❑ **ECONOMIC INDICATORS** *Page 122*
- ❑ **FINANCIAL SYSTEM INDICATORS** *Page 171*

KEY FACTS: ECONOMIC INDICATORS

Table 1

National accounts: GDP and main expenditure components SWDA* (ESA 2010, Base 2010)

Forecasts in blue

		GDP	Private consumption	Public consumption	Gross fixed capital formation					Exports	Imports	Domestic Demand (a)	Net exports (a)
						Construction							
					Total	Total	Housing	Other construction	Equipment & other products				
Chain-linked volumes, annual percentage changes													
2009		-3.6	-3.6	4.1	-16.9	-16.1	-20.3	-11.4	-18.3	-11.0	-18.3	-6.4	2.8
2010		0.0	0.3	1.5	-4.9	-10.1	-11.6	-8.5	5.4	9.4	6.9	-0.5	0.5
2011		-1.0	-2.4	-0.3	-6.9	-11.7	-13.3	-10.2	0.9	7.4	-0.8	-3.1	2.1
2012		-2.6	-3.5	-4.5	-7.1	-8.3	-5.4	-10.7	-5.3	1.1	-6.2	-4.7	2.1
2013		-1.7	-3.1	-2.8	-2.5	-7.1	-7.2	-7.1	3.5	4.3	-0.3	-3.1	1.4
2014		1.4	1.2	0.0	3.5	-0.2	-1.4	0.8	7.7	5.1	6.4	1.6	-0.2
2015		3.2	3.1	2.7	6.4	5.3	2.4	7.5	7.5	5.4	7.5	3.7	-0.5
2016		2.7	3.3	2.0	4.3	3.6	3.6	3.7	5.1	3.8	5.7	3.2	-0.5
2017		2.3	2.6	1.3	3.9	3.8	5.5	2.4	4.0	4.8	6.0	2.6	-0.3
2014	I	0.4	0.3	0.0	1.4	-6.5	-6.9	-6.2	11.5	4.6	6.2	0.7	-0.3
	II	1.2	1.1	0.2	4.3	0.8	-1.5	2.7	8.3	2.8	5.2	1.8	-0.6
	III	1.7	1.4	0.2	3.4	1.3	0.6	1.8	5.7	6.4	7.3	1.8	-0.1
	IV	2.1	1.8	-0.5	4.9	4.1	2.5	5.2	5.7	6.5	6.8	2.0	0.1
2015	I	2.7	2.5	1.5	6.1	6.2	2.9	8.8	6.0	5.8	7.6	3.1	-0.4
	II	3.2	2.9	2.5	6.3	5.2	2.6	7.3	7.5	6.0	7.4	3.4	-0.2
	III	3.4	3.5	3.0	6.7	5.2	2.1	7.6	8.2	4.5	7.2	4.1	-0.7
	IV	3.5	3.5	3.7	6.4	4.6	2.2	6.4	8.4	5.3	7.7	4.1	-0.6
2016	I	3.3	3.5	2.4	5.5	4.2	3.0	5.1	6.9	4.8	6.2	3.6	-0.3
	II	2.8	3.5	2.1	4.2	3.2	3.0	3.3	5.2	3.8	6.2	3.5	-0.7
	III	2.5	3.1	1.9	4.0	3.4	3.8	3.1	4.6	3.1	4.5	2.8	-0.3
	IV	2.2	3.0	1.7	3.8	3.7	4.5	3.1	3.8	3.5	5.8	2.8	-0.6
Chain-linked volumes, quarter-on-quarter percentage changes, at annual rate													
2014	I	1.5	0.0	-0.2	1.5	-3.1	-1.0	-4.8	6.4	6.6	7.3	1.4	0.0
	II	2.0	1.9	-0.8	8.6	11.9	5.7	16.9	5.3	4.8	7.2	2.5	-0.5
	III	2.4	1.9	0.1	3.7	2.8	3.3	2.4	4.7	14.0	13.7	1.9	0.5
	IV	2.7	3.1	-1.0	5.7	5.2	2.3	7.5	6.2	0.8	-0.6	2.3	0.5
2015	I	3.7	3.2	8.0	6.4	5.2	0.5	8.9	7.6	4.1	10.7	5.6	-1.9
	II	3.9	3.2	3.0	9.5	7.7	4.2	10.4	11.4	5.8	6.3	3.9	0.0
	III	3.3	4.6	2.2	5.2	2.9	1.7	3.9	7.6	7.6	13.1	4.7	-1.4
	IV	3.2	3.0	1.7	4.7	2.5	2.4	2.7	6.8	3.8	1.1	2.3	0.9
2016	I	2.6	3.4	2.6	2.7	3.6	3.8	3.5	1.9	2.1	4.8	3.2	-0.5
	II	2.2	3.2	1.8	4.1	3.7	4.3	3.3	4.4	1.7	6.3	3.3	-1.2
	III	1.8	3.0	1.6	4.5	3.7	4.7	3.0	5.2	4.9	5.7	2.8	-1.0
	IV	2.1	2.6	1.0	3.9	3.8	5.2	2.8	3.9	5.2	6.2	2.5	-0.4
	Current prices (EUR billions)	Percentage of GDP at current prices											
2009		1,079.0	56.1	20.5	24.3	16.2	8.1	8.1	8.2	22.7	23.8	101.2	-1.2
2010		1,080.9	57.2	20.5	23.0	14.3	6.9	7.4	8.7	25.5	26.8	101.3	-1.3
2011		1,070.4	57.8	20.5	21.5	12.5	5.7	6.8	9.0	28.9	29.2	100.2	-0.2
2012		1,042.9	58.6	19.7	20.1	11.3	5.2	6.2	8.7	30.6	29.1	98.5	1.5
2013		1,031.3	58.0	19.6	19.2	10.3	4.5	5.7	9.0	32.0	28.7	96.8	2.1
2014		1,041.2	58.3	19.4	19.6	10.1	4.4	5.7	9.5	32.5	30.1	97.5	2.5
2015		1,081.2	57.6	19.3	20.4	10.4	4.5	5.9	10.0	33.1	30.7	97.5	2.5
2016		1,118.0	57.3	19.1	20.9	10.6	4.6	6.0	10.3	33.5	31.1	97.6	2.4
2017		1,155.8	57.7	18.9	21.4	10.9	4.8	6.0	10.5	34.4	32.7	98.4	1.6

*Seasonally and Working Day Adjusted.

(a) Contribution to GDP growth.

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 1.1.- GDP
Percentage change

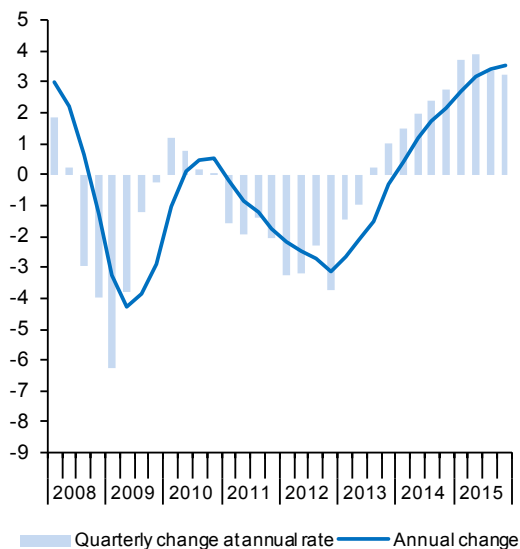


Chart 1.2.- Contribution to GDP annual growth
Per cent points

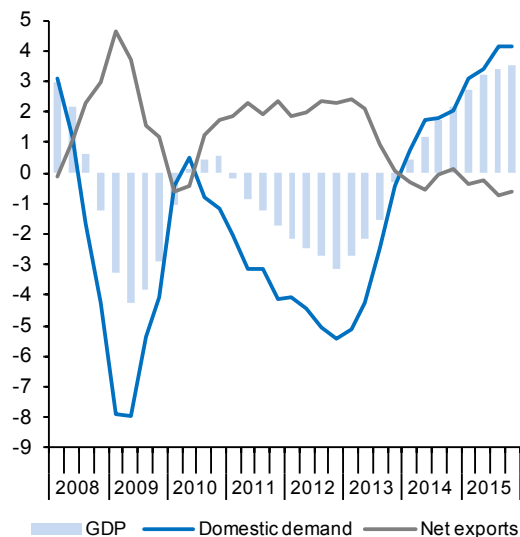


Chart 1.3.- Final consumption
Annual percentage change

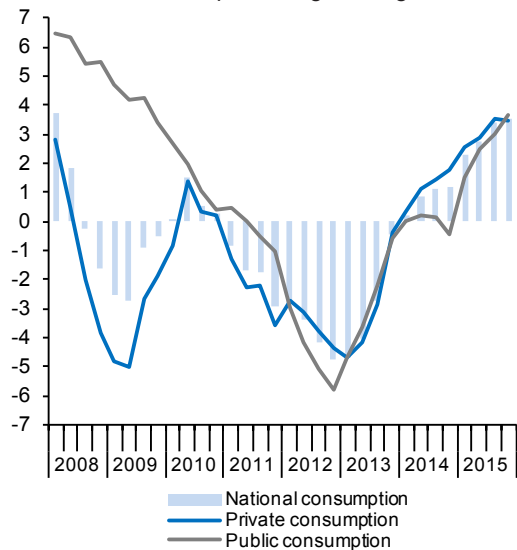


Chart 1.4.- Gross fixed capital formation
Annual percentage change

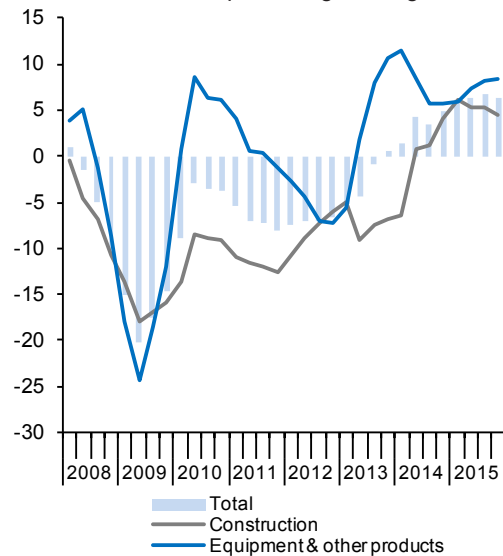


Table 2

National accounts: Gross value added by economic activity SWDA* (ESA 2010, Base 2010)

Forecasts in blue

	Gross value added at basic prices													Taxes less subsidies on products
	Total	Agriculture, forestry and fishing	Manufacturing, energy and utilities	Construction	Total	Trade, transport, accommodation and food services	Information and communication	Finance and insurance	Real estate	Professional, business and support services	Public administration, education, health and social work	Arts, entertainment and other services		
Chain-linked volumes, annual percentage changes														
2009	-3.4	-3.6	-10.0	-7.6	-1.0	-3.7	0.6	-6.1	3.4	-3.7	2.3	0.7	-5.9	
2010	0.0	2.1	3.6	-14.5	1.3	1.5	3.9	-3.3	2.0	-1.4	2.4	1.4	0.1	
2011	-0.6	4.4	-0.2	-12.8	0.7	-0.1	-0.2	-2.4	2.8	2.3	0.9	-0.2	-5.6	
2012	-2.5	-11.0	-4.9	-14.3	-0.4	-0.6	2.2	-3.6	2.0	-1.3	-0.8	-1.4	-4.4	
2013	-1.6	16.5	-5.2	-9.8	-0.6	0.1	0.7	-7.8	1.6	-1.9	-1.1	-0.7	-2.9	
2014	1.4	-3.7	1.2	-2.1	1.9	3.2	4.7	-1.0	1.2	3.4	-0.4	4.4	0.8	
2015	3.3	1.9	3.4	5.2	3.1	4.8	4.7	-0.9	0.8	5.8	1.7	4.2	2.8	
2016	2.7	2.8	2.4	4.4	2.6	3.0	3.3	1.1	1.5	4.5	1.7	3.8	3.0	
2017	2.2	2.0	2.4	4.3	2.1	2.0	2.7	1.4	1.7	4.2	1.3	3.0	2.6	
2014 I	0.5	3.2	-0.8	-7.3	1.3	2.5	4.4	-1.8	1.1	1.1	-0.5	3.4	-0.4	
II	1.2	-6.0	1.5	-3.9	1.8	3.1	4.3	-1.2	1.2	3.1	-0.5	4.4	0.8	
III	1.7	-2.9	1.5	0.2	2.1	3.3	5.0	-0.6	1.3	4.1	-0.5	4.9	1.3	
IV	2.2	-8.7	2.5	3.1	2.5	4.0	5.0	-0.2	1.1	5.3	-0.2	5.0	1.7	
2015 I	2.7	-4.0	3.0	5.9	2.7	4.1	4.4	-2.3	1.0	6.2	0.9	4.5	2.3	
II	3.2	2.0	3.6	5.8	3.0	4.6	5.0	-0.4	0.9	6.5	1.1	3.9	2.6	
III	3.5	3.7	3.8	5.1	3.3	5.1	5.0	-1.1	0.7	5.7	2.2	4.0	2.7	
IV	3.5	6.2	3.4	4.0	3.4	5.3	4.6	0.2	0.8	4.9	2.4	4.5	3.6	
2016 I	3.3	4.9	2.7	3.8	3.3	4.9	4.4	0.7	1.3	4.8	2.0	4.3	3.4	
II	2.8	4.4	2.2	5.0	2.7	3.4	3.5	0.4	1.4	4.0	2.1	4.3	3.4	
III	2.4	2.1	2.3	4.7	2.2	2.0	2.9	1.7	1.5	4.9	1.6	3.5	3.5	
IV	2.2	-0.1	2.6	4.2	2.1	1.9	2.4	1.4	1.8	4.3	1.3	3.1	1.8	
Chain-linked volumes, quarter-on-quarter percentage changes, at annual rate														
2014 I	1.5	-19.4	3.7	-5.6	2.4	5.2	5.3	8.3	-0.9	1.7	-1.0	5.5	1.4	
II	2.1	-18.2	2.7	-0.2	3.0	5.2	3.3	-5.3	2.8	6.7	0.1	5.3	0.3	
III	2.6	4.2	1.0	8.5	2.4	3.7	5.4	-1.0	3.1	3.8	-1.0	6.3	0.5	
IV	2.6	0.9	2.5	10.5	2.1	1.8	5.8	-2.4	-0.7	9.4	1.2	2.8	4.7	
2015 I	3.7	-1.3	5.9	4.9	3.3	5.8	3.0	-0.6	-1.0	5.2	3.3	3.7	3.7	
II	4.1	4.1	4.8	-0.4	4.3	7.2	5.8	2.4	2.3	7.6	1.0	2.7	1.5	
III	3.5	11.4	1.8	5.5	3.5	5.7	5.2	-3.8	2.1	0.7	3.3	6.9	1.0	
IV	2.7	11.3	1.0	6.2	2.6	2.5	4.5	2.8	-0.2	6.3	2.1	4.8	8.3	
2016 I	2.6	-6.0	3.0	4.1	2.7	4.1	2.1	1.4	1.0	4.8	1.5	2.8	2.8	
II	2.2	2.0	2.8	4.2	1.9	1.2	2.4	1.4	2.7	4.4	1.3	2.8	1.7	
III	1.9	2.0	2.3	4.2	1.6	0.2	2.5	1.4	2.5	4.0	1.3	3.6	1.2	
IV	2.2	2.0	2.3	4.3	2.0	2.1	2.6	1.4	1.0	4.0	1.3	3.2	1.5	
Current prices (EUR billions)														
Percentage of value added at basic prices														
2009	1006.1	2.3	16.6	10.6	70.4	22.0	4.4	5.7	8.9	7.3	18.2	4.0	7.2	
2010	989.9	2.6	17.2	8.8	71.4	22.5	4.4	4.4	10.2	7.2	18.7	4.1	9.2	
2011	983.7	2.5	17.4	7.5	72.6	22.9	4.3	4.2	10.9	7.4	18.7	4.2	8.8	
2012	957.1	2.5	17.2	6.3	74.0	23.6	4.4	4.3	11.6	7.4	18.6	4.2	9.0	
2013	941.3	2.8	17.1	5.6	74.5	23.8	4.3	3.8	12.0	7.3	19.0	4.2	9.6	
2014	948.3	2.5	17.0	5.4	75.1	24.1	4.3	4.1	12.0	7.4	18.8	4.3	9.8	
2015	981.8	2.5	17.0	5.5	74.9	24.5	4.2	3.9	11.7	7.6	18.7	4.4	10.1	
2016	1,013.4	2.6	16.9	5.6	74.9	24.5	4.2	3.6	11.5	7.8	18.8	4.4	10.3	
2017	1,045.9	2.7	17.0	5.7	74.6	23.7	4.2	4.0	11.4	8.1	18.9	4.3	10.5	

*Seasonally and Working Day Adjusted.

Sources: INE (Quarterly National Accounts) and FUNCAS (Forecasts).

Chart 2.1.- GVA by sectors
Annual percentage change

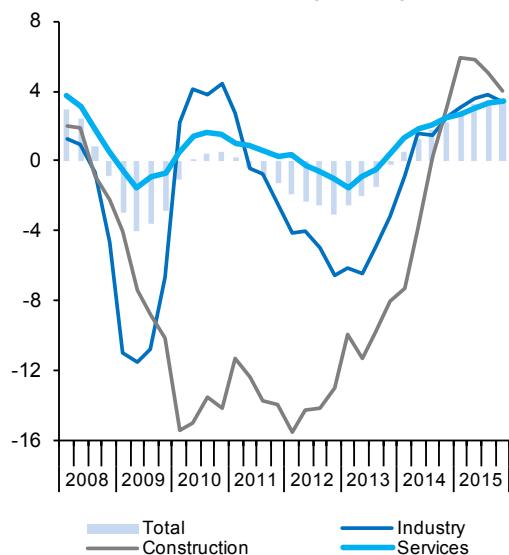


Chart 2.2.- GVA, services (I)
Annual percentage change

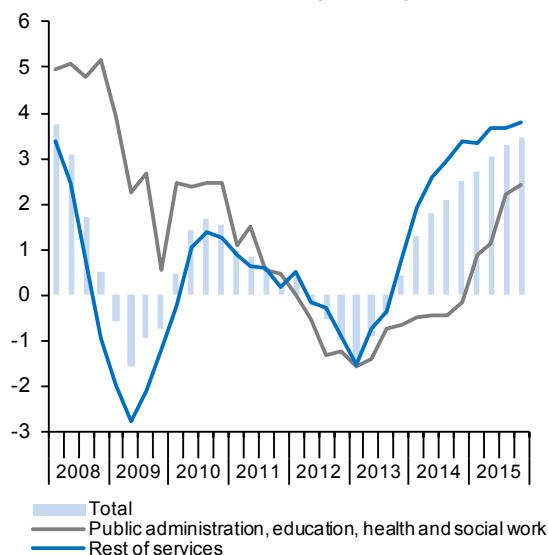


Chart 2.3.- GVA, services (II)
Annual percentage change

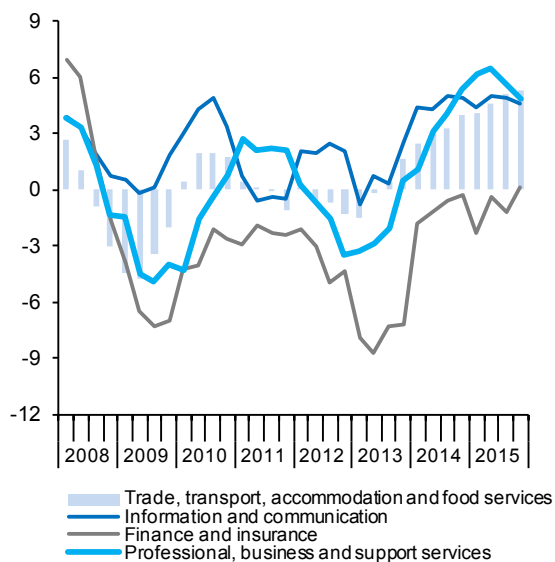


Chart 2.4.- GVA, structure by sectors
Percentage of value added at basic prices

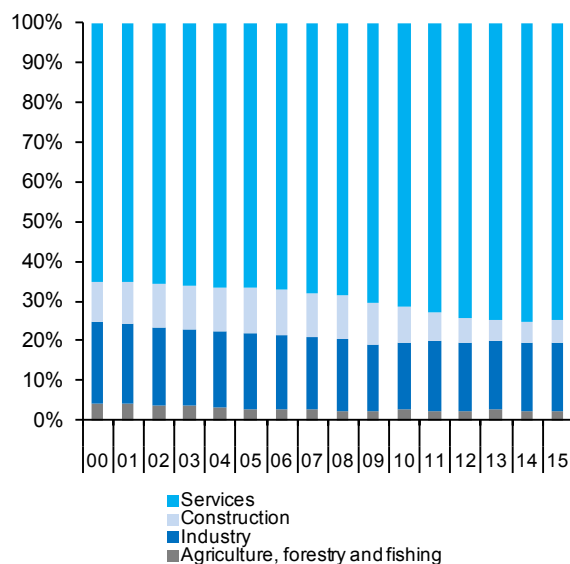


Table 3a

National accounts: Productivity and labour costs (I) (ESA 2010, Base 2010)

Forecasts in blue

	Total economy						Manufacturing industry					
	GDP, constant prices	Employment (jobs, full time equivalent)	Employment productivity	Compensation per job	Nominal unit labour cost	Real unit labour cost (a)	Gross value added, constant prices	Employment (jobs, full time equivalent)	Employment productivity	Compensation per job	Nominal unit labour cost	Real unit labour cost (a)
	1	2	3=1/2	4	5=4/3	6	7	8	9=7/8	10	11=10/9	12
Indexes, 2000 = 100, SWDA												
2009	124.5	117.1	106.4	144.4	135.7	101.2	100.1	82.2	121.8	152.6	125.3	99.0
2010	124.5	114.0	109.3	145.9	133.5	99.4	100.1	78.9	126.9	155.6	122.6	97.7
2011	123.3	110.8	111.3	147.1	132.2	98.4	98.8	75.9	130.1	159.0	122.1	95.3
2012	120.1	105.4	113.9	146.2	128.4	95.5	93.5	70.8	132.1	161.4	122.1	95.6
2013	118.1	101.7	116.1	148.7	128.1	94.8	92.3	67.8	136.2	163.7	120.2	94.2
2014	119.7	102.8	116.4	147.9	127.0	94.3	94.3	67.8	139.1	166.3	119.5	93.9
2015	123.5	105.8	116.7	148.7	127.4	94.0	97.8	69.8	140.2	166.0	118.4	92.7
2016	126.8	108.4	117.0	149.9	128.1	93.9	100.9	--	--	--	--	--
2017	129.7	111.0	116.9	151.8	129.9	94.2	103.4	--	--	--	--	--
2014	I	118.7	101.6	116.8	147.8	126.6	94.1	93.6	67.2	139.3	164.8	93.1
	II	119.3	102.5	116.3	147.9	127.2	94.5	93.9	67.8	138.6	166.3	93.8
	III	120.0	103.1	116.4	148.0	127.2	94.4	94.4	68.0	138.8	166.7	94.6
	IV	120.8	103.8	116.3	147.9	127.1	94.3	95.3	68.3	139.6	167.2	94.2
2015	I	121.9	104.6	116.6	148.8	127.7	94.4	96.2	68.9	139.5	166.2	93.2
	II	123.1	105.5	116.6	148.4	127.3	94.1	97.5	70.0	139.4	166.5	93.1
	III	124.1	106.3	116.7	148.2	127.0	93.6	98.5	70.1	140.4	166.0	92.7
	IV	125.0	106.9	116.9	149.2	127.6	94.0	99.2	70.0	141.7	165.5	91.6
Annual percentage changes												
2009	-3.6	-6.1	2.7	4.4	1.6	1.4	-10.9	-12.4	1.8	2.2	0.5	0.5
2010	0.0	-2.7	2.7	1.1	-1.6	-1.8	0.0	-4.0	4.2	1.9	-2.1	-1.3
2011	-1.0	-2.8	1.8	0.9	-0.9	-1.0	-1.3	-3.8	2.6	2.2	-0.4	-2.4
2012	-2.6	-4.9	2.4	-0.6	-2.9	-3.0	-5.3	-6.8	1.5	1.5	0.0	0.3
2013	-1.7	-3.5	1.9	1.7	-0.2	-0.8	-1.4	-4.3	3.1	1.5	-1.5	-1.4
2014	1.4	1.1	0.3	-0.6	-0.8	-0.4	2.2	0.1	2.1	1.5	-0.6	-0.3
2015	3.2	3.0	0.2	0.5	0.3	-0.3	3.7	2.9	0.8	-0.1	-1.0	-1.3
2016	2.7	2.4	0.3	0.8	0.6	-0.1	3.1	--	--	--	--	--
2017	2.3	2.4	-0.1	1.3	1.4	0.3	2.5	--	--	--	--	--
2014	I	0.4	-0.7	1.2	-0.6	-1.7	-1.2	1.6	-2.8	4.6	1.7	-1.7
	II	1.2	1.0	0.2	-0.5	-0.7	-0.2	2.4	-0.1	2.4	1.5	-0.7
	III	1.7	1.7	0.0	-0.7	-0.7	-0.5	2.2	1.5	0.7	1.3	0.5
	IV	2.1	2.4	-0.3	-0.5	-0.2	0.1	2.6	1.8	0.7	1.7	0.8
2015	I	2.7	2.9	-0.2	0.7	0.9	0.3	2.8	2.6	0.2	0.8	0.1
	II	3.2	2.9	0.3	0.3	0.1	-0.5	3.8	3.2	0.6	0.1	-0.8
	III	3.4	3.1	0.3	0.1	-0.2	-0.8	4.3	3.1	1.1	-0.4	-2.0
	IV	3.5	3.0	0.5	0.9	0.4	-0.3	4.1	2.5	1.5	-1.0	-2.7

(a) Nominal ULC deflated by GDP/GVA deflator.

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 3a.1.- Nominal ULC, total economy
Index, 2000=100

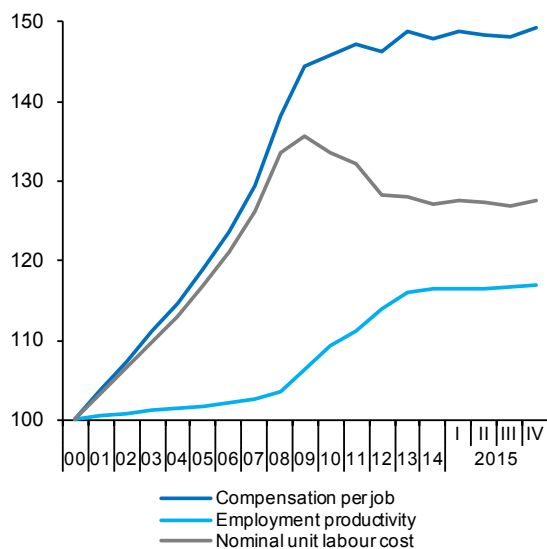
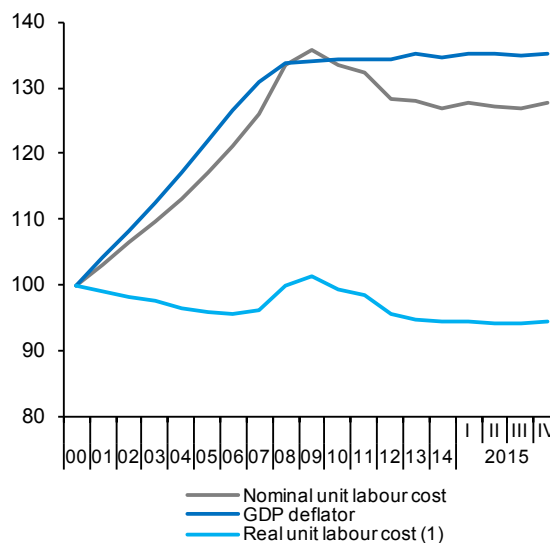


Chart 3a.2.- Real ULC, total economy
Index, 2000=100



(1) Nominal ULC deflated by GDP deflator.

Chart 3a.3.- Nominal ULC, manufacturing industry
Index, 2000=100

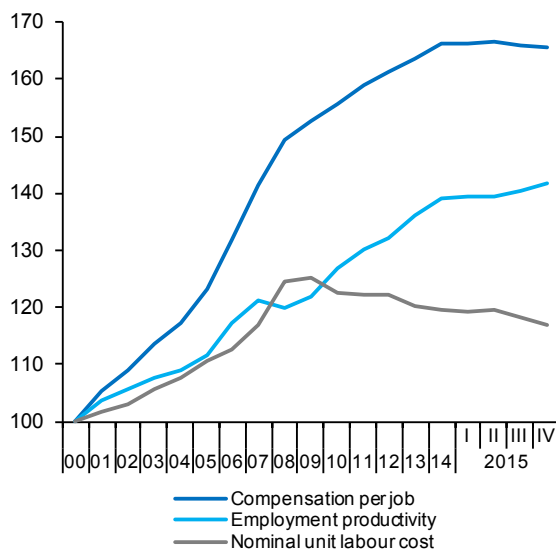
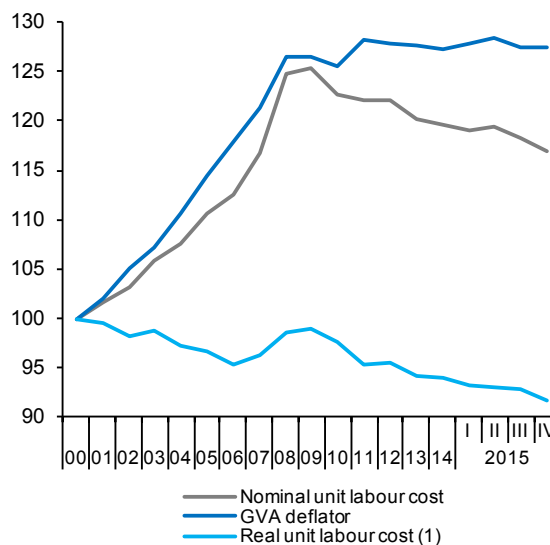


Chart 3a.4.- Real ULC, manufacturing industry
Index, 2000=100



(1) Nominal ULC deflated by GVA deflator.

Table 3b

National accounts: Productivity and labour costs (II) (ESA 2010, Base 2010)

Forecasts in blue

	Construction						Services					
	Gross value added, constant prices	Employment (jobs, full time equivalent)	Employment productivity	Compensation per job	Nominal unit labour cost	Real unit labour cost (a)	Gross value added, constant prices	Employment (jobs, full time equivalent)	Employment productivity	Compensation per job	Nominal unit labour cost	Real unit labour cost (a)
	1	2	3=1/2	4	5=4/3	6	7	8	9=7/8	10	11=10/9	12
Indexes, 2000 = 100, SWDA												
2009	109.4	99.1	110.4	170.0	154.0	93.6	135.8	133.6	101.6	137.7	135.5	96.9
2010	93.5	85.2	109.7	172.1	156.9	99.2	137.5	132.0	104.2	139.1	133.4	96.7
2011	81.5	72.2	112.8	169.6	150.3	98.0	138.5	130.5	106.1	140.2	132.2	97.2
2012	69.9	58.7	119.1	170.6	143.2	97.9	138.0	126.1	109.4	138.6	126.7	95.6
2013	63.0	50.4	124.9	172.1	137.8	97.9	137.1	122.8	111.7	141.1	126.4	93.9
2014	61.7	48.9	126.3	172.5	136.6	97.1	139.7	124.8	112.0	139.9	124.9	92.7
2015	64.9	51.8	125.3	171.6	137.0	96.8	144.1	128.4	112.2	140.9	125.6	91.8
2016	67.8	53.6	126.5	--	--	--	147.8	131.6	112.3	--	--	--
2017	70.7	55.5	127.3	--	--	--	150.8	134.2	112.4	--	--	--
2014 I	60.7	47.5	127.8	172.6	135.1	94.8	138.4	123.2	112.3	140.2	124.9	92.8
II	60.7	48.1	126.1	172.3	136.7	97.1	139.4	124.6	111.9	139.9	125.0	92.9
III	61.9	49.3	125.7	172.4	137.2	98.3	140.2	125.2	112.0	139.9	125.0	92.3
IV	63.5	50.6	125.6	172.6	137.4	98.3	141.0	126.2	111.7	139.6	124.9	92.8
2015 I	64.3	51.4	125.1	171.4	137.0	95.6	142.1	126.9	112.0	141.1	126.0	91.8
II	64.2	52.0	123.6	171.3	138.6	97.7	143.6	127.9	112.3	140.6	125.2	92.3
III	65.1	51.8	125.7	173.2	137.8	97.9	144.9	129.0	112.3	140.4	124.9	91.8
IV	66.1	52.2	126.7	170.4	134.5	96.0	145.8	129.9	112.2	141.8	126.3	91.5
Annual percentage changes												
2009	-7.6	-21.7	18.0	9.8	-6.9	-8.6	-1.0	-2.4	1.5	4.0	2.5	0.7
2010	-14.5	-14.0	-0.6	1.3	1.9	6.0	1.3	-1.2	2.5	1.0	-1.5	-0.2
2011	-12.8	-15.3	2.9	-1.4	-4.2	-1.2	0.7	-1.1	1.8	0.8	-0.9	0.5
2012	-14.3	-18.8	5.5	0.6	-4.7	-0.1	-0.4	-3.4	3.1	-1.2	-4.2	-1.6
2013	-9.8	-14.0	4.9	0.9	-3.8	0.0	-0.6	-2.7	2.1	1.9	-0.2	-1.7
2014	-2.1	-3.1	1.1	0.2	-0.8	-0.8	1.9	1.7	0.2	-0.9	-1.1	-1.3
2015	5.2	6.0	-0.8	-0.5	0.3	-0.3	3.1	2.9	0.2	0.8	0.5	-0.9
2016	4.4	3.4	1.0	--	--	--	2.6	2.5	0.1	--	--	--
2017	4.3	3.6	0.6	--	--	--	2.1	2.0	0.1	--	--	--
2014 I	-7.3	-10.5	3.6	0.4	-3.1	-2.3	1.3	0.0	1.3	-0.6	-2.0	-1.6
II	-3.9	-4.7	0.9	0.0	-0.9	-1.2	1.8	1.8	0.0	-0.8	-0.9	-1.3
III	0.2	-0.2	0.4	0.7	0.3	0.1	2.1	2.1	0.0	-1.1	-1.0	-1.2
IV	3.1	3.7	-0.5	-0.1	0.4	0.1	2.5	2.8	-0.3	-1.0	-0.7	-1.2
2015 I	5.9	8.1	-2.1	-0.7	1.4	0.8	2.7	3.0	-0.3	0.6	0.9	-1.1
II	5.8	7.9	-2.0	-0.6	1.4	0.6	3.0	2.6	0.4	0.5	0.1	-0.6
III	5.1	5.1	0.0	0.4	0.4	-0.3	3.3	3.0	0.3	0.3	0.0	-0.5
IV	4.0	3.1	0.8	-1.2	-2.1	-2.3	3.4	3.0	0.4	1.6	1.1	-1.5

(a) Nominal ULC deflated by GVA deflator.

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 3b.1.- Nominal ULC, construction
Index, 2000=100

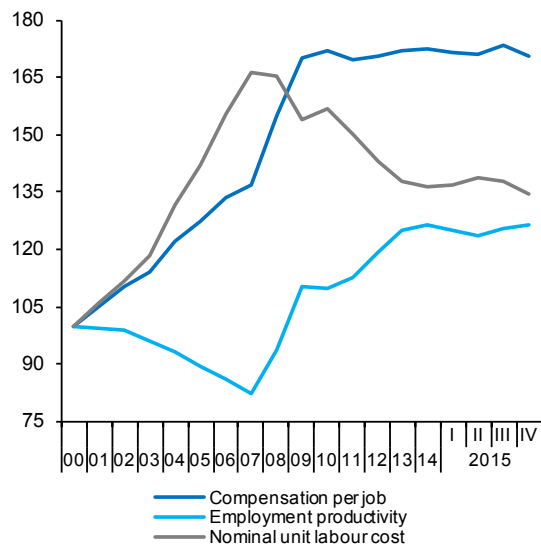
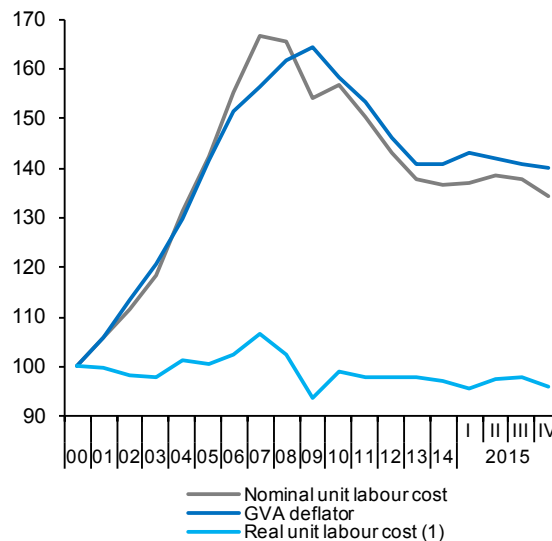


Chart 3b.2.- Real ULC, construction
Index, 2000=100



(1) Nominal ULC deflated by GVA deflator.

Chart 3b.3.- Nominal ULC, services
Index, 2000=100

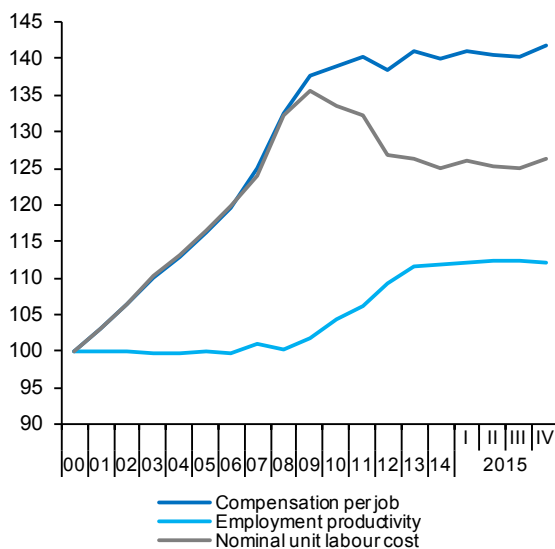
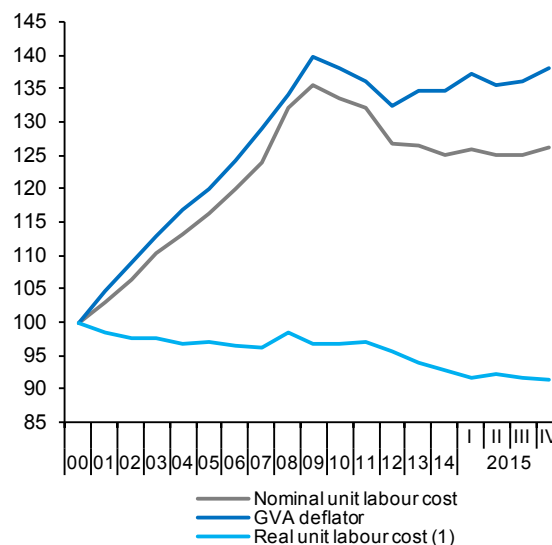


Chart 3b.4.- Real ULC, services
Index, 2000=100



(1) Nominal ULC deflated by GVA deflator.

Table 4

National accounts: National income, distribution and disposition (ESA 2010, Base 2010)

Forecasts in blue

	Gross domestic product	Compensation of employees	Gross operating surplus	Taxes on production and imports less subsidies	Income payments to the rest of the world, net	Gross national product	Current transfers to the rest of the world, net	Gross national income	Final national consumption	Gross national saving (a)	Compensation of employees	Gross operating surplus	Taxes on production and imports less subsidies
	1=2+3+4	2	3	4	5	6=1+5	7	8=6+7	9	10=8-9	11	12	13
	EUR Billions, 4-quarter cumulated transactions										Percentage of GDP		
2009	1,079.0	549.2	455.2	74.7	-19.8	1,059.2	-14.3	1,045.0	826.4	218.6	50.9	42.2	6.9
2010	1,080.9	541.5	445.9	93.6	-15.2	1,065.8	-12.7	1,053.0	840.5	212.6	50.1	41.3	8.7
2011	1,070.4	531.0	449.4	90.0	-18.6	1,051.9	-14.1	1,037.7	838.5	199.2	49.6	42.0	8.4
2012	1,042.9	498.6	450.0	94.2	-7.3	1,035.5	-12.6	1,023.0	816.6	206.3	47.8	43.2	9.0
2013	1,031.3	486.6	444.7	99.9	-4.8	1,026.5	-13.1	1,013.4	800.8	212.6	47.2	43.1	9.7
2014	1,041.2	490.8	446.4	103.9	-4.2	1,036.9	-11.5	1,025.5	809.3	216.2	47.1	42.9	10.0
2015	1,081.2	509.9	460.2	111.1	1.2	1,082.3	-11.5	1,070.9	830.9	240.0	47.2	42.6	10.3
2016	1,118.0	527.7	473.1	117.3	7.0	1,125.0	-11.6	1,113.4	854.6	258.8	47.2	42.3	10.5
2017	1,155.8	545.6	486.3	124.0	10.9	1,166.8	-11.8	1,155.0	886.3	268.7	47.2	42.1	10.7
2014	I 1,031.0	484.9	445.0	101.1	-3.4	1,027.6	-13.5	1,014.1	801.4	212.7	47.0	43.2	9.8
	II 1,033.1	486.2	445.6	101.3	-5.9	1,027.2	-13.0	1,014.2	804.8	209.3	47.1	43.1	9.8
	III 1,036.6	488.1	446.0	102.5	-6.3	1,030.2	-11.7	1,018.5	808.2	210.4	47.1	43.0	9.9
	IV 1,041.2	490.8	446.4	103.9	-4.2	1,036.9	-11.5	1,025.5	809.3	216.2	47.1	42.9	10.0
2015	I 1,049.2	495.1	450.1	104.0	-3.5	1,045.7	-11.5	1,034.2	813.0	221.2	47.2	42.9	9.9
	II 1,059.7	499.5	452.9	107.2	-1.3	1,058.4	-11.3	1,047.1	818.9	228.2	47.1	42.7	10.1
	III 1,070.5	504.3	457.6	108.6	-0.8	1,069.7	-10.9	1,058.8	824.9	233.9	47.1	42.7	10.1
	IV 1,081.2	509.9	460.2	111.1	1.2	1,082.3	-11.5	1,070.9	830.9	240.0	47.2	42.6	10.3
	Annual percentage changes										Difference from one year ago		
2009	-3.3	-1.9	-2.2	-18.1	-33.9	-2.5	-9.1	-2.4	-2.0	-3.9	0.7	0.5	-1.3
2010	0.2	-1.4	-2.0	25.3	-23.4	0.6	-10.9	0.8	1.7	-2.8	-0.8	-0.9	1.7
2011	-1.0	-1.9	0.8	-3.8	22.5	-1.3	11.2	-1.5	-0.2	-6.3	-0.5	0.7	-0.2
2012	-2.6	-6.1	0.1	4.7	-60.5	-1.6	-11.0	-1.4	-2.6	3.6	-1.8	1.2	0.6
2013	-1.1	-2.4	-1.2	6.0	-34.7	-0.9	4.3	-0.9	-1.9	3.0	-0.6	0.0	0.7
2014	1.0	0.9	0.4	4.0	-11.7	1.0	-12.7	1.2	1.1	1.7	0.0	-0.2	0.3
2015	3.8	3.9	3.1	6.9	-127.4	4.4	0.0	4.4	2.7	11.0	0.0	-0.3	0.3
2016	3.4	3.5	2.8	5.5	505.4	3.9	1.5	4.0	2.9	7.8	0.0	-0.2	0.2
2017	3.4	3.4	2.8	5.7	55.8	3.7	1.5	3.7	3.7	3.8	0.0	-0.2	0.2
2014	I -0.6	-1.6	-0.9	6.4	-43.4	-0.3	14.6	-0.5	-0.9	1.1	-0.5	-0.1	0.6
	II -0.1	-0.3	-0.6	3.5	46.9	-0.2	3.9	-0.3	0.2	-2.2	-0.1	-0.2	0.3
	III 0.6	0.6	-0.3	3.9	51.7	0.3	-11.1	0.5	1.1	-1.9	0.0	-0.4	0.3
	IV 1.0	0.9	0.4	4.0	-11.7	1.0	-12.7	1.2	1.1	1.7	0.0	-0.2	0.3
2015	I 1.8	2.1	1.2	2.9	4.1	1.8	-14.9	2.0	1.4	4.0	0.2	-0.3	0.1
	II 2.6	2.8	1.6	5.8	-77.7	3.0	-13.7	3.2	1.7	9.0	0.1	-0.4	0.3
	III 3.3	3.3	2.6	6.0	-87.2	3.8	-6.8	4.0	2.1	11.2	0.0	-0.3	0.3
	IV 3.8	3.9	3.1	6.9	-127.4	4.4	0.0	4.4	2.7	11.0	0.0	-0.3	0.3

(a) Including change in net equity in pension funds reserves.

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 4.1.- National income, consumption and saving

EUR Billions, 4-quarter cumulated

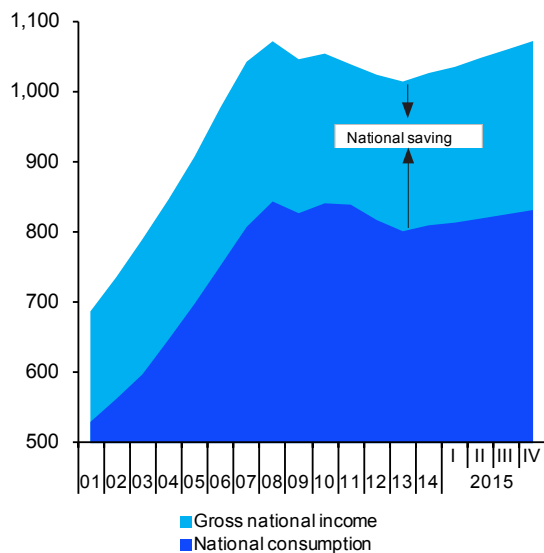


Chart 4.2.- National income, consumption and saving rate

Annual percentage change and percentage of GDP, 4-quarter moving averages

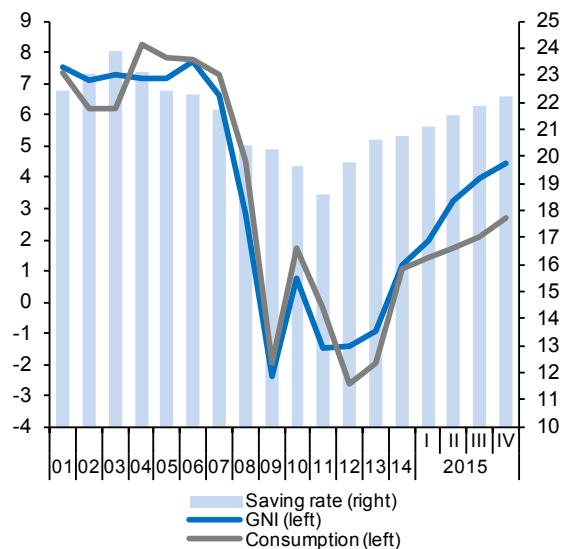


Chart 4.3.- Components of National income

Annual percentage change

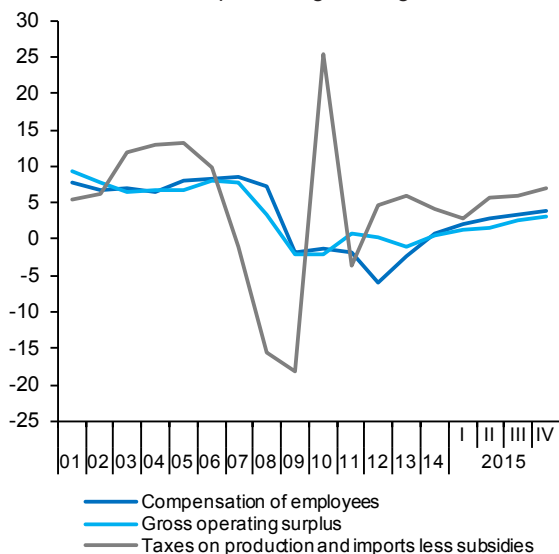


Chart 4.4.- Functional distribution of income

Percentage of GDP, 4-quarter moving averages

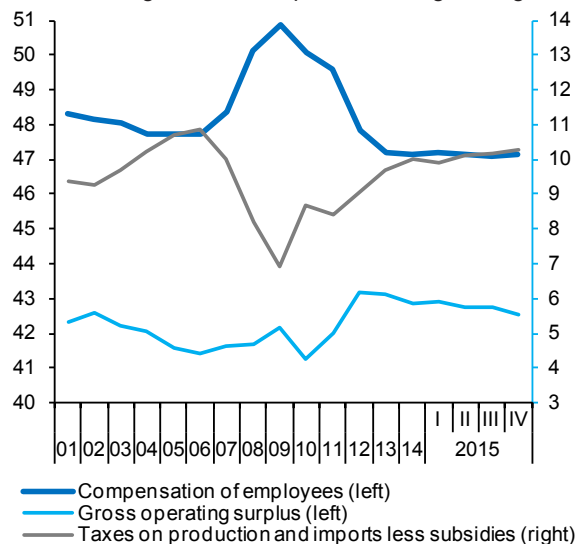


Table 5

National accounts: Net transactions with the rest of the world (ESA 2010, Base 2010)

Forecasts in blue

	Goods and services				Income	Current transfers	Current account	Capital transfers	Net lending/ borrowing with rest of the world	Saving-Investment-Deficit		
	Total	Goods	Tourist services	Non-tourist services						Gross national saving	Gross capital formation	Current account deficit
	1=2+3+4	2	3	4	5	6	7=1+5+6	8	9=7+8	10	11	12=7-10-11
EUR Billions, 4-quarter cumulated transactions												
2009	-12.4	-41.5	22.4	6.6	-19.8	-14.3	-46.5	4.5	-42.0	218.6	265.1	-46.5
2010	-14.1	-47.8	23.0	10.7	-15.2	-12.7	-42.0	5.9	-36.1	212.6	254.5	-42.0
2011	-2.6	-44.5	26.2	15.6	-18.6	-14.1	-35.3	4.4	-30.9	199.2	234.5	-35.3
2012	15.3	-29.3	27.1	17.5	-7.3	-12.6	-4.6	5.4	0.8	206.3	211.0	-4.6
2013	33.1	-14.2	28.3	18.9	-4.8	-13.1	15.2	7.8	22.9	212.6	197.4	15.2
2014	26.0	-22.5	28.8	19.7	-4.2	-11.5	10.3	6.1	16.4	216.2	205.9	10.3
2015	26.9	-21.6	28.6	20.0	1.2	-11.5	16.6	7.3	23.9	240.0	223.4	16.6
2016	26.8	-22.8	28.9	20.7	7.0	-11.6	22.2	7.5	29.6	258.8	236.6	22.2
2017	18.8	-32.6	29.8	21.6	10.9	-11.8	18.0	7.6	25.6	268.7	250.7	18.0
2014 I	30.6	-17.2	28.5	19.3	-3.4	-13.5	13.7	8.2	21.8	212.7	199.0	13.7
II	26.7	-20.7	28.7	18.8	-5.9	-13.0	7.8	7.5	15.3	209.3	201.5	7.8
III	25.5	-22.2	28.7	19.0	-6.3	-11.7	7.5	7.1	14.5	210.4	202.9	7.5
IV	26.0	-22.5	28.8	19.7	-4.2	-11.5	10.3	6.1	16.4	216.2	205.9	10.3
2015 I	27.4	-21.1	28.7	19.8	-3.5	-11.5	12.4	5.2	17.5	221.2	208.8	12.4
II	27.5	-21.2	28.6	20.2	-1.3	-11.3	15.0	5.7	20.7	228.2	213.2	15.0
III	27.2	-21.7	28.4	20.5	-0.8	-10.9	15.5	7.2	22.6	233.9	218.4	15.5
IV	26.9	-21.6	28.6	20.0	1.2	-11.5	16.6	7.3	23.9	240.0	223.4	16.6
Percentage of GDP, 4-quarter cumulated transactions												
2009	-1.2	-3.8	2.1	0.6	-1.8	-1.3	-4.3	0.4	-3.9	20.3	24.6	-4.3
2010	-1.3	-4.4	2.1	1.0	-1.4	-1.2	-3.9	0.5	-3.3	19.7	23.5	-3.9
2011	-0.2	-4.2	2.4	1.5	-1.7	-1.3	-3.3	0.4	-2.9	18.6	21.9	-3.3
2012	1.5	-2.8	2.6	1.7	-0.7	-1.2	-0.4	0.5	0.1	19.8	20.2	-0.4
2013	3.2	-1.4	2.7	1.8	-0.5	-1.3	1.5	0.8	2.2	20.6	19.1	1.5
2014	2.5	-2.2	2.8	1.9	-0.4	-1.1	1.0	0.6	1.6	20.8	19.8	1.0
2015	2.5	-2.0	2.6	1.8	0.1	-1.1	1.5	0.7	2.2	22.2	20.7	1.5
2016	2.4	-2.0	2.6	1.8	0.6	-1.0	2.0	0.7	2.7	23.1	21.2	2.0
2017	1.6	-2.8	2.6	1.9	0.9	-1.0	1.6	0.7	2.2	23.2	21.7	1.6
2014 I	3.0	-1.7	2.8	1.9	-0.3	-1.3	1.3	0.8	2.1	20.6	19.3	1.3
II	2.6	-2.0	2.8	1.8	-0.6	-1.3	0.8	0.7	1.5	20.3	19.5	0.8
III	2.5	-2.1	2.8	1.8	-0.6	-1.1	0.7	0.7	1.4	20.3	19.6	0.7
IV	2.5	-2.2	2.8	1.9	-0.4	-1.1	1.0	0.6	1.6	20.8	19.8	1.0
2015 I	2.6	-2.0	2.7	1.9	-0.3	-1.1	1.2	0.5	1.7	21.1	19.9	1.2
II	2.6	-2.0	2.7	1.9	-0.1	-1.1	1.4	0.5	2.0	21.5	20.1	1.4
III	2.5	-2.0	2.7	1.9	-0.1	-1.0	1.4	0.7	2.1	21.8	20.4	1.4
IV	2.5	-2.0	2.6	1.8	0.1	-1.1	1.5	0.7	2.2	22.2	20.7	1.5

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 5.1.- Balance of goods and services
Percentage of GDP, 4-quarter moving averages

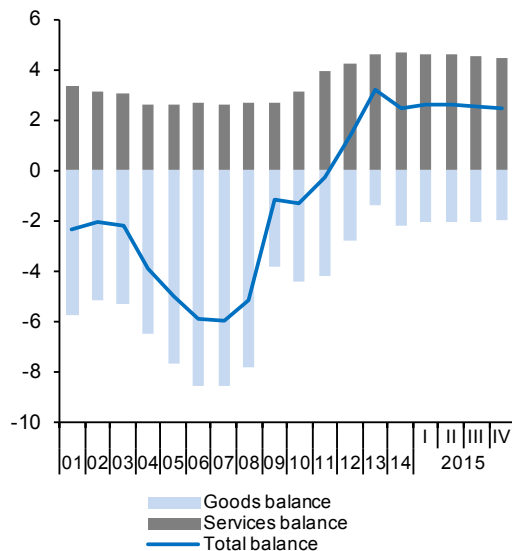


Chart 5.2.- Services balance
Percentage of GDP, 4-quarter moving averages

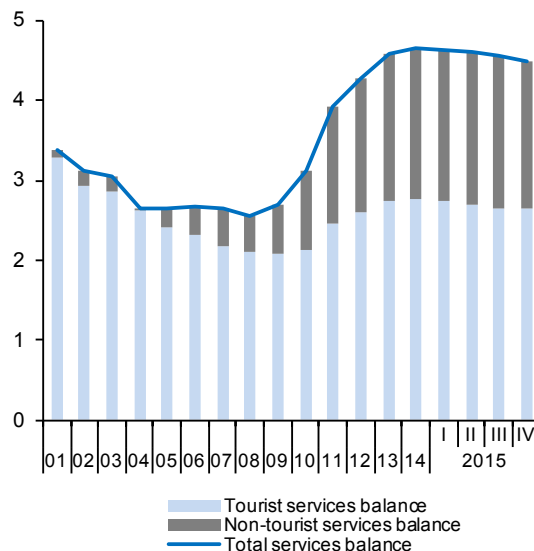


Chart 5.3.- Net lending or borrowing
Percentage of GDP, 4-quarter moving averages

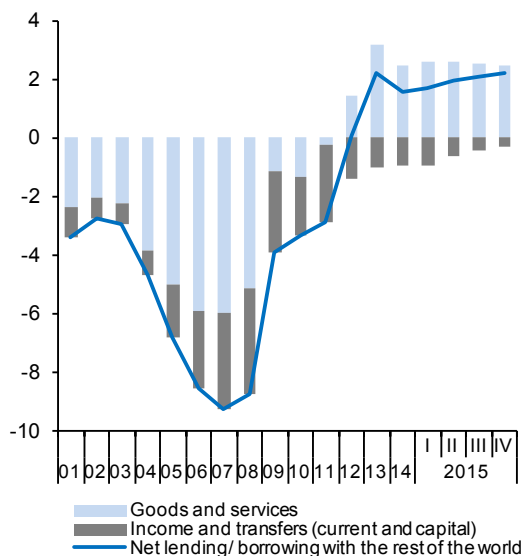


Chart 5.4.- Saving, investment and current account balance
Percentage of GDP, 4-quarter moving averages

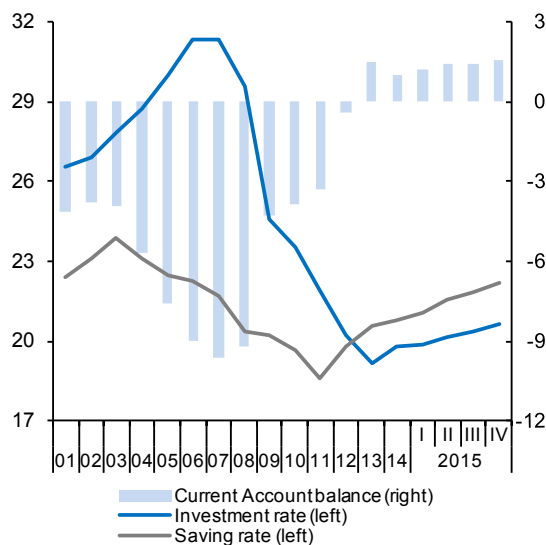


Table 6

National accounts: Household income and its disposition (ESA 2010, Base 2010)

Forecasts in blue

	Gross disposable income (GDI)						Final consumption expenditure	Gross saving (a)	Saving rate (gross saving as a percentage of GDI)	Net capital transfers	Gross capital formation	Net lending (+) or borrowing (-)	Net lending or borrowing as a percentage of GDP
	Total	Compensation of employees (received)	Mixed income and net property income	Social benefits and other current transfers (received)	Social contributions and other current transfers (paid)	Personal income taxes							
	1=2+3+4-5-6	2	3	4	5	6	7	8=1-7	9=8/1	10	11	12=8+10-11	13
EUR Billions, 4-quarter cumulated operations													
2009	698.9	549.9	199.1	235.9	209.8	76.2	605.3	93.6	13.4	6.7	69.0	31.3	2.9
2010	688.4	542.3	196.3	239.3	209.7	79.9	618.8	69.5	10.1	7.6	63.0	14.2	1.3
2011	694.2	531.9	212.1	242.9	210.3	82.4	618.9	74.7	10.8	5.2	53.8	26.1	2.4
2012	672.1	499.9	210.9	247.3	202.4	83.6	611.4	58.8	8.7	5.0	38.4	25.4	2.4
2013	666.6	488.7	211.0	249.5	199.2	83.4	598.4	66.2	9.9	3.7	26.9	43.0	4.2
2014	672.5	492.9	218.5	240.4	195.3	83.9	606.8	64.6	9.6	4.5	29.3	39.9	3.8
2015	685.3	512.1	215.9	240.1	198.7	84.1	622.2	61.9	9.0	3.9	29.9	35.9	3.3
2016	708.0	529.9	225.8	242.3	203.4	86.6	640.9	66.0	9.3	3.4	30.9	38.6	3.4
2017	733.5	547.9	238.7	246.1	209.6	89.7	667.3	65.1	8.9	3.2	32.8	35.5	3.1
2014 I	664.2	487.1	212.4	246.5	198.3	83.6	598.9	63.8	9.6	3.3	27.3	39.7	3.9
II	665.1	488.3	212.3	244.6	196.8	83.3	602.4	61.4	9.2	3.4	27.6	37.1	3.6
III	667.8	490.2	216.0	240.8	195.3	83.9	605.2	61.3	9.2	3.3	27.9	36.7	3.5
IV	672.5	492.9	218.5	240.4	195.3	83.9	606.8	64.6	9.6	4.5	29.3	39.9	3.8
2015 I	675.5	497.4	216.4	240.8	195.4	83.7	609.0	64.9	9.6	4.1	28.6	40.4	3.8
II	679.9	501.8	218.2	240.7	196.8	84.0	612.9	65.6	9.7	3.1	28.4	40.3	3.8
III	681.7	506.6	216.0	241.0	197.4	84.4	617.5	62.7	9.2	3.1	28.8	37.0	3.5
IV	685.3	512.1	215.9	240.1	198.7	84.1	622.2	61.9	9.0	3.9	29.9	35.9	3.3
Annual percentage changes, 4-quarter cumulated operations								Difference from one year ago	Annual percentage changes, 4-quarter cumulated operations		Difference from one year ago		
2009	1.9	-1.9	-6.6	8.7	-4.6	-10.1	-4.5	64.4	5.1	8.3	-23.5	--	5.3
2010	-1.5	-1.4	-1.4	1.4	-0.1	4.8	2.2	-25.8	-3.3	13.8	-8.7	--	-1.6
2011	0.8	-1.9	8.0	1.5	0.3	3.2	0.0	7.5	0.7	-32.3	-14.6	--	1.1
2012	-3.2	-6.0	-0.5	1.8	-3.7	1.5	-1.2	-21.3	-2.0	-3.1	-28.6	--	0.0
2013	-0.8	-2.3	0.0	0.9	-1.6	-0.3	-2.1	12.7	1.2	-26.5	-29.9	--	1.7
2014	0.9	0.9	3.6	-3.7	-1.9	0.7	1.4	-2.4	-0.3	23.2	8.6	--	-0.3
2015	1.9	3.9	-1.2	-0.1	1.7	0.3	2.5	-4.2	-0.6	-15.0	2.1	--	-0.5
2016	3.3	3.5	4.6	0.9	2.3	2.9	3.0	6.6	0.3	-11.0	3.6	--	0.1
2017	3.6	3.4	5.7	1.6	3.0	3.6	4.1	-1.4	-0.5	-8.0	6.0	--	-0.4
2014 I	-0.8	-1.5	0.5	-0.9	-1.7	0.5	-1.2	3.0	0.4	-28.7	-23.8	--	0.9
II	-0.6	-0.2	0.1	-2.2	-1.6	1.4	0.0	-5.4	-0.5	-17.5	-16.9	--	0.1
III	0.4	0.7	2.4	-3.6	-1.9	1.0	0.9	-4.1	-0.4	-10.8	-9.3	--	0.0
IV	0.9	0.9	3.6	-3.7	-1.9	0.7	1.4	-2.4	-0.3	23.2	8.6	--	-0.3
2015 I	1.7	2.1	1.9	-2.3	-1.4	0.1	1.7	1.8	0.0	25.0	4.8	--	0.0
II	2.2	2.8	2.8	-1.6	0.0	0.9	1.7	6.9	0.4	-9.3	2.8	--	0.2
III	2.1	3.3	0.0	0.1	1.1	0.6	2.0	2.2	0.0	-4.5	3.2	--	-0.1
IV	1.9	3.9	-1.2	-0.1	1.7	0.3	2.5	-4.2	-0.6	-15.0	2.1	--	-0.5

(a) Including change in net equity of households in pension funds reserves.

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 6.1.- Households: Gross disposable income
EUR Billions, 4-quarter cumulated

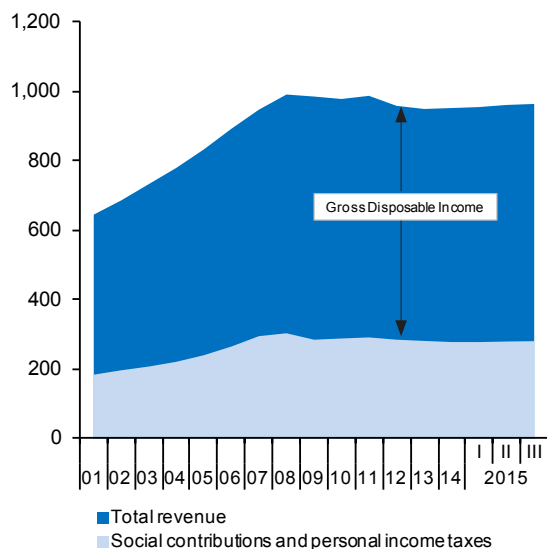
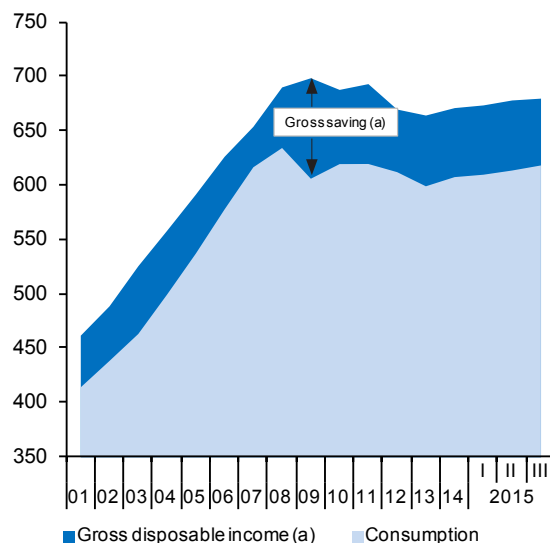


Chart 6.2.- Households: Gross saving
EUR Billions, 4-quarter cumulated



(a) Including change in net equity of households in pension funds reserves.

Chart 6.3.- Households: Income, consumption and saving

Annual percentage change and percentage of GDI, 4-quarter moving averages

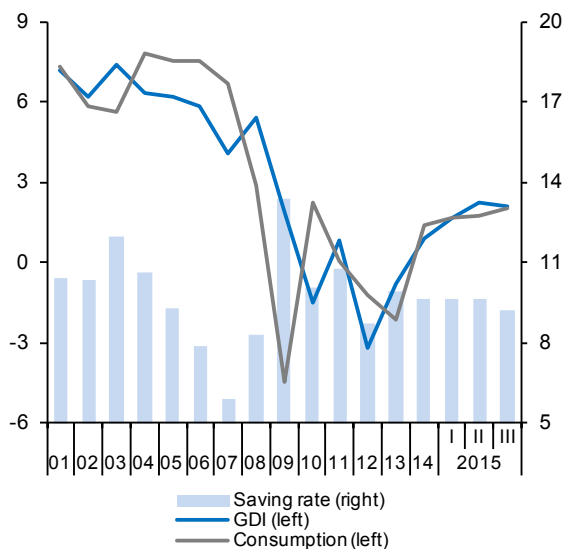
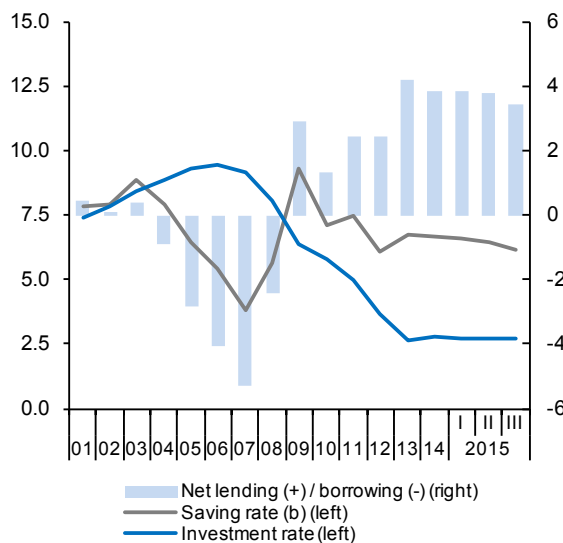


Chart 6.4.- Households: Saving, investment and deficit

Percentage of GDP, 4-quarter moving averages



(b) Including net capital transfers.

Table 7

National accounts: Non-financial corporations income and its disposition (ESA 2010, Base 2010)

Forecasts in blue

	Gross value added	Compensation of employees and net taxes on production (paid)	Gross operating surplus	Net property income	Net current transfers	Income taxes	Gross saving	Net capital transfers	Gross capital formation	Net lending (+) or borrowing (-)	Net lending or borrowing as a percentage of GDP	Profit share (percentage)	Investment rate (percentage)
	1	2	3=1-2	4	5	6	7=3+4+5-6	8	9	10=7+8-9	11	12=3/1	13=9/1
EUR Billions, 4-quarter cumulated operations													
2009	590.7	354.4	236.3	-59.9	-13.3	19.0	144.2	11.4	130.1	25.4	2.4	40.0	22.0
2010	581.8	346.0	235.8	-49.2	-8.6	16.2	161.8	10.2	132.0	40.0	3.7	40.5	22.7
2011	573.0	340.2	232.8	-63.4	-8.8	15.8	144.9	8.9	131.8	22.0	2.1	40.6	23.0
2012	557.4	320.9	236.5	-60.7	-9.7	19.8	146.4	6.4	139.9	12.9	1.2	42.4	25.1
2013	546.0	309.3	236.7	-43.6	-9.0	18.0	166.2	5.1	140.7	30.6	3.0	43.4	25.8
2014	550.9	314.4	236.6	-49.5	-6.6	18.6	161.9	4.6	150.9	15.6	1.5	42.9	27.4
2015	574.7	327.4	247.3	-37.4	-5.8	21.1	183.1	5.2	166.0	22.2	2.1	43.0	28.9
2016	591.5	340.3	251.1	-31.8	-6.0	20.8	192.5	5.2	177.5	20.2	1.8	42.5	30.0
2017	609.4	353.8	255.6	-28.5	-6.2	21.3	199.6	5.2	189.0	15.8	1.4	42.0	31.0
2014 I	545.4	308.4	237.0	-43.8	-8.3	18.1	166.8	5.5	143.6	28.6	2.8	43.5	26.3
II	547.4	310.0	237.4	-47.9	-7.7	19.4	162.3	4.9	143.4	23.9	2.3	43.4	26.2
III	548.6	311.6	236.9	-49.8	-7.2	19.2	160.8	4.8	145.3	20.2	2.0	43.2	26.5
IV	550.9	314.4	236.6	-49.5	-6.6	18.6	161.9	4.6	150.9	15.6	1.5	42.9	27.4
2015 I	555.8	317.5	238.3	-44.9	-6.6	18.0	168.7	3.9	154.2	18.5	1.8	42.9	27.7
II	561.8	320.7	241.2	-43.3	-6.5	19.1	172.3	4.6	160.0	16.9	1.6	42.9	28.5
III	568.8	324.5	244.3	-40.2	-6.3	19.9	177.9	5.7	160.4	23.1	2.2	42.9	28.2
IV	574.7	327.4	247.3	-37.4	-5.8	21.1	183.1	5.2	166.0	22.2	2.1	43.0	28.9
Annual percentage changes, 4-quarter cumulated operations											Difference from one year ago		
2009	-2.4	-4.1	0.4	-23.9	50.6	-25.4	17.8	-5.3	-27.2	--	6.3	1.1	-7.5
2010	-1.5	-2.4	-0.2	-17.9	-34.9	-15.0	12.2	-9.8	1.5	--	1.3	0.5	0.7
2011	-1.5	-1.7	-1.2	29.0	1.4	-2.4	-10.5	-13.0	-0.2	--	-1.6	0.1	0.3
2012	-2.7	-5.7	1.6	-4.3	10.4	25.3	1.0	-27.7	6.2	--	-0.8	1.8	2.1
2013	-2.0	-3.6	0.1	-28.2	-6.8	-9.2	13.6	-20.5	0.5	--	1.7	0.9	0.7
2014	0.9	1.6	-0.1	13.6	-27.0	3.5	-2.6	-10.9	7.2	--	-1.5	-0.4	1.6
2015	4.3	4.1	4.6	-24.5	-12.1	13.7	13.1	14.0	10.1	--	0.6	0.1	1.5
2016	2.9	4.0	1.5	-14.8	3.5	-1.5	5.2	0.0	6.9	--	-0.2	-0.6	1.1
2017	3.0	3.9	1.8	-10.6	4.0	2.5	3.7	0.0	6.5	--	-0.4	-0.5	1.0
2014 I	-1.5	-2.5	0.0	-24.0	-10.8	-6.4	10.6	-19.8	3.1	--	1.0	0.6	1.2
II	-0.6	-1.0	-0.2	-7.7	-16.2	-1.2	3.3	-26.1	1.8	--	0.1	0.2	0.6
III	-0.1	0.2	-0.4	8.5	-19.4	4.4	-2.5	-22.2	1.8	--	-0.8	-0.2	0.5
IV	0.9	1.6	-0.1	13.6	-27.0	3.5	-2.6	-10.9	7.2	--	-1.5	-0.4	1.6
2015 I	1.9	3.0	0.5	2.6	-20.4	-0.9	1.2	-28.1	7.4	--	-1.0	-0.6	1.4
II	2.6	3.4	1.6	-9.5	-15.6	-1.9	6.1	-6.0	11.5	--	-0.7	-0.4	2.3
III	3.7	4.1	3.1	-19.3	-11.9	3.6	10.6	18.7	10.4	--	0.2	-0.2	1.7
IV	4.3	4.1	4.6	-24.5	-12.1	13.7	13.1	14.0	10.1	--	0.6	0.1	1.5

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 7.1.- Non-financial corporations: Gross operating surplus

EUR Billions, 4-quarter cumulated

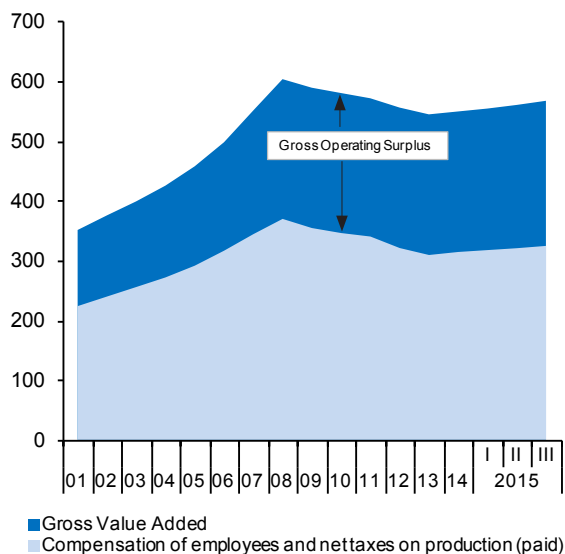


Chart 7.2.- Non-financial corporations: GVA, GOS and saving

Annual percentage change, 4-quarter moving averages

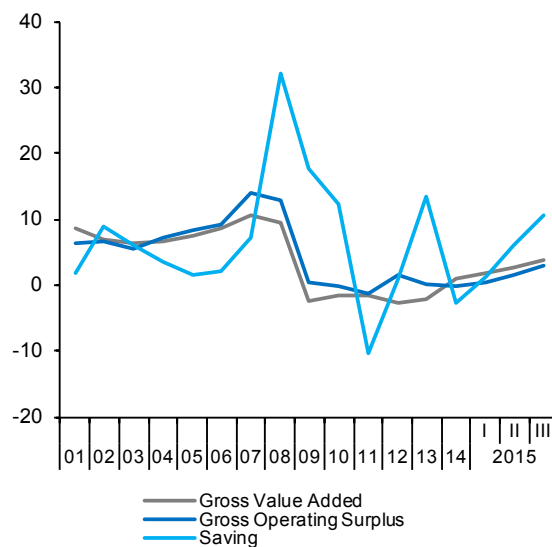


Chart 7.3.- Non-financial corporations: Saving, investment and deficit

Percentage of GDP, 4-quarter moving averages

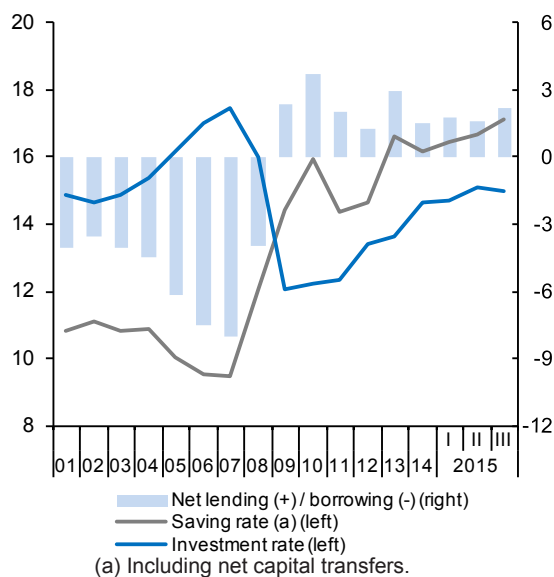


Chart 7.4.- Non-financial corporations: Profit share and investment rate

Percentage of non-financial corporations GVA, 4-quarter moving averages

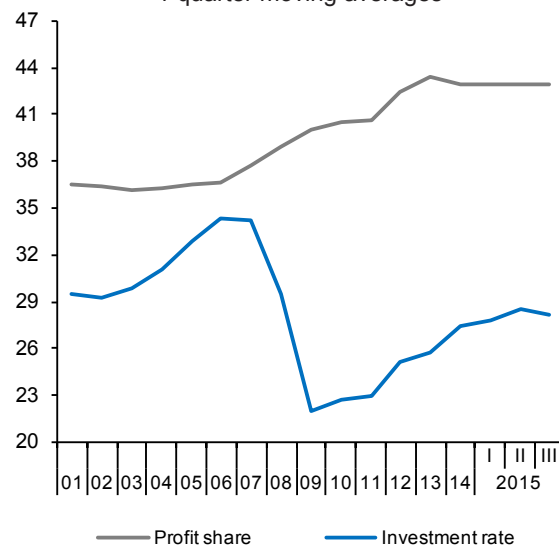


Table 8

National accounts: Public revenue, expenditure and deficit (ESA 2010, Base 2010)

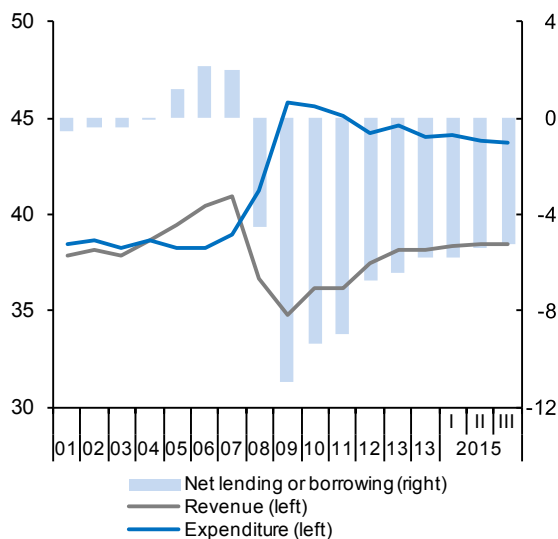
Forecasts in blue

	Gross value added	Taxes on production and imports receivable	Taxes on income and wealth receivable	Social contributions receivable	Compensation of employees	Interests and other capital incomes payable (net)	Social benefits payable	Subsidies and net current transfers payable	Gross disposable income	Final consumption expenditure	Gross saving	Net capital expenditure	Net lending(+)/net borrowing(-)	Net lending(+)/net borrowing(-) excluding financial entities bail-out
	1	2	3	4	5	6	7	8	9=1+2+3+4-5-6-7-8	10	11=9-10	12	13=11-12	14
EUR Billions, 4-quarter cumulated operations														
2009	151.0	91.9	101.6	139.7	125.6	8.0	155.1	23.9	171.7	221.0	-49.3	68.9	-118.2	-118.2
2010	152.0	110.1	100.6	138.6	124.9	10.8	162.7	21.4	181.5	221.7	-40.2	61.3	-101.4	-101.1
2011	150.3	106.2	102.0	137.8	122.6	16.2	164.2	22.6	170.7	219.7	-49.0	52.3	-101.3	-96.1
2012	142.2	108.2	106.3	131.9	113.9	20.3	168.5	18.7	167.1	205.2	-38.1	70.8	-108.9	-69.8
2013	142.9	114.6	105.0	128.2	114.7	24.1	170.6	20.5	160.8	202.4	-41.5	29.7	-71.2	-66.3
2014	143.1	118.9	105.4	130.1	114.9	25.7	170.7	20.5	165.6	202.4	-36.8	24.5	-61.3	-60.1
2015	147.9	125.9	108.7	132.1	119.2	24.9	170.4	21.3	178.8	208.7	-29.9	24.4	-54.3	-54.2
2016	152.1	132.2	110.9	135.5	122.8	21.1	171.4	21.4	193.9	213.7	-19.8	24.6	-44.4	-44.4
2017	155.7	139.3	114.6	139.7	125.8	18.6	173.4	21.7	209.9	219.0	-9.1	24.8	-33.9	-33.9
2014 I	142.8	115.9	105.6	128.6	114.6	24.7	170.2	20.8	162.6	202.6	-40.0	29.1	-69.1	-64.2
II	142.7	117.0	105.9	128.6	114.5	24.9	169.8	22.5	162.5	202.5	-40.0	25.9	-65.9	-63.7
III	143.0	118.0	106.2	129.2	114.8	24.9	169.1	21.3	166.3	203.0	-36.6	23.7	-60.3	-59.5
IV	143.1	118.9	105.4	130.1	114.9	25.7	170.7	20.5	165.6	202.4	-36.8	24.5	-61.3	-60.1
2015 I	144.2	120.4	106.1	130.2	115.9	26.1	170.6	21.6	166.8	203.9	-37.1	25.0	-62.1	-60.9
II	145.2	123.1	107.6	131.1	116.8	25.8	170.6	20.7	173.1	205.9	-32.9	25.2	-58.0	-56.8
III	145.7	125.3	109.0	131.5	117.3	25.4	170.8	21.0	177.2	207.3	-30.1	26.9	-57.0	-56.3
IV	147.9	125.9	108.7	132.1	119.2	24.9	170.4	21.3	178.8	208.7	-29.9	24.4	-54.3	-54.2
Percentage of GDP, 4-quarter cumulated operations														
2009	14.0	8.5	9.4	12.9	11.6	0.7	14.4	2.2	15.9	20.5	-4.6	6.4	-11.0	-11.0
2010	14.1	10.2	9.3	12.8	11.6	1.0	15.1	2.0	16.8	20.5	-3.7	5.7	-9.4	-9.3
2011	14.0	9.9	9.5	12.9	11.5	1.5	15.3	2.1	15.9	20.5	-4.6	4.9	-9.5	-9.0
2012	13.6	10.4	10.2	12.6	10.9	1.9	16.2	1.8	16.0	19.7	-3.7	6.8	-10.4	-6.7
2013	13.9	11.1	10.2	12.4	11.1	2.3	16.5	2.0	15.6	19.6	-4.0	2.9	-6.9	-6.4
2014	13.7	11.4	10.1	12.5	11.0	2.5	16.4	2.0	15.9	19.4	-3.5	2.4	-5.9	-5.8
2015	13.7	11.6	10.1	12.2	11.0	2.3	15.8	2.0	16.5	19.3	-2.8	2.3	-5.0	-5.0
2016	13.6	11.8	9.9	12.1	11.0	1.9	15.3	1.9	17.3	19.1	-1.8	2.2	-4.0	-4.0
2017	13.5	12.0	9.9	12.1	10.9	1.6	15.0	1.9	18.2	18.9	-0.8	2.1	-2.9	-2.9
2014 I	13.9	11.2	10.2	12.5	11.1	2.4	16.5	2.0	15.8	19.6	-3.9	2.8	-6.7	-6.2
II	13.8	11.3	10.3	12.4	11.1	2.4	16.4	2.2	15.7	19.6	-3.9	2.5	-6.4	-6.2
III	13.8	11.4	10.2	12.5	11.1	2.4	16.3	2.1	16.0	19.6	-3.5	2.3	-5.8	-5.7
IV	13.7	11.4	10.1	12.5	11.0	2.5	16.4	2.0	15.9	19.4	-3.5	2.4	-5.9	-5.8
2015 I	13.7	11.5	10.1	12.4	11.1	2.5	16.3	2.1	15.9	19.4	-3.5	2.4	-5.9	-5.8
II	13.7	11.6	10.2	12.4	11.0	2.4	16.1	1.9	16.3	19.4	-3.1	2.4	-5.5	-5.4
III	13.6	11.7	10.2	12.3	11.0	2.4	16.0	2.0	16.6	19.4	-2.8	2.5	-5.3	-5.3
IV	13.7	11.6	10.1	12.2	11.0	2.3	15.8	2.0	16.5	19.3	-2.8	2.3	-5.0	-5.0

Sources: INE (Quarterly National Accounts) and Funcas (Forecasts).

Chart 8.1.- Public sector: Revenue, expenditure and deficit (a)

Percentage of GDP, 4-quarter moving averages



(a) Excluding financial entities bail-out expenditures.

Chart 8.2.- Public sector: Main revenues
Percentage of GDP, 4-quarter moving averages

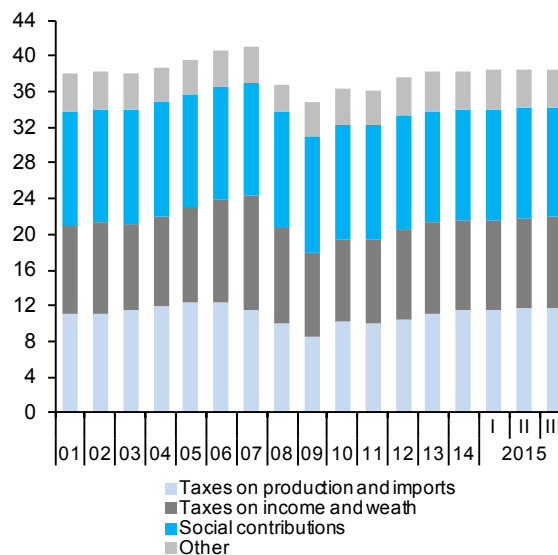


Chart 8.3.- Public sector: Main expenditures
Percentage of GDP, 4-quarter moving averages

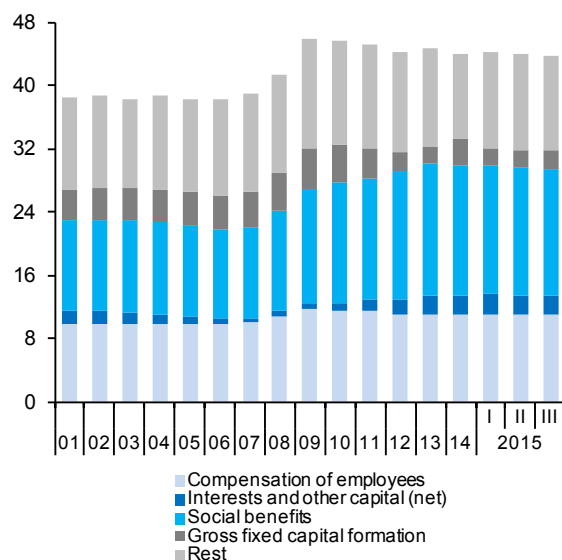
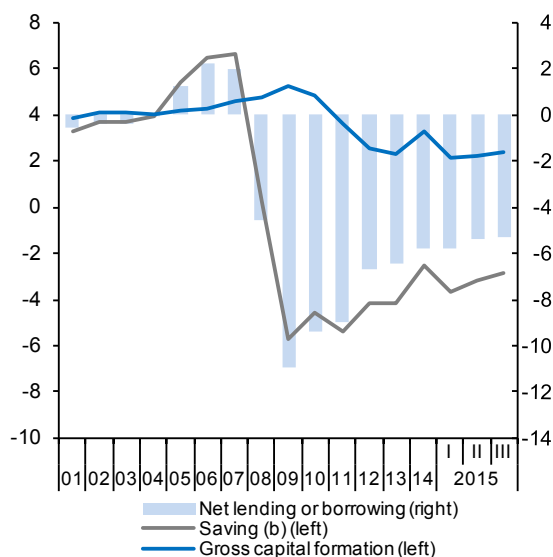


Chart 8.4.- Public sector: Saving, investment and deficit (a)
Percentage of GDP, 4-quarter moving averages



(a) Excluding financial entities bail-out expenditures.

(b) Including net capital transfers.

Table 9

Public sector balances, by level of Government

Forecasts in blue

	Deficit					Debt				
	Central Government (a)	Regional Governments	Local Governments	Social Security	TOTAL Government (a)	Central Government	Regional Governments	Local Governments	Social Security	TOTAL Government (consolidated)
EUR Billions, 4-quarter cumulated operations						EUR Billions, end of period				
2009	-98.4	-21.7	-5.9	7.8	-118.2	487.7	92.4	34.7	17.2	568.7
2010	-51.4	-40.2	-7.1	-2.4	-101.1	551.6	123.4	35.5	17.2	649.3
2011	-31.7	-54.8	-8.5	-1.1	-96.1	624.2	145.1	36.8	17.2	743.5
2012	-43.5	-19.4	3.3	-10.2	-69.8	761.9	188.4	44.0	17.2	890.7
2013	-44.3	-16.2	5.7	-11.5	-66.3	837.9	209.8	42.1	17.2	966.0
2014	-37.0	-18.2	5.9	-10.9	-60.1	895.7	236.8	38.3	17.2	1,033.7
2015	-29.4	-17.3	5.4	-13.0	-54.2	938.8	261.3	35.1	17.2	1,070.3
2016	-19.8	-11.2	3.4	-16.8	-44.4	--	--	--	--	1,109.3
2017	-12.5	-6.9	2.9	-17.3	-33.9	--	--	--	--	1,143.3
2014 I	-42.1	-16.9	5.3	-10.6	-64.2	866.0	225.0	41.9	17.2	995.7
II	-37.1	-18.3	5.4	-13.8	-63.7	885.1	228.2	42.0	17.2	1,012.5
III	-39.0	-18.2	6.0	-8.3	-59.5	891.8	232.1	40.8	17.2	1,020.1
IV	-37.0	-18.2	5.9	-10.9	-60.1	895.7	236.8	38.3	17.2	1,033.7
2015 I	-38.5	-17.2	6.3	-11.5	-60.9	907.1	240.4	38.3	17.2	1,046.0
II	-33.3	-16.7	7.0	-13.8	-56.8	918.0	249.9	37.7	17.2	1,052.5
III	-30.4	-17.6	5.4	-13.7	-56.3	934.3	253.2	36.9	17.2	1,062.7
IV	-29.4	-17.3	5.4	-13.0	-54.2	938.8	261.3	35.1	17.2	1,070.3
Percentage of GDP, 4-quarter cumulated operations						Percentage of GDP				
2009	-9.1	-2.0	-0.5	0.7	-11.0	45.2	8.6	3.2	1.6	52.7
2010	-4.8	-3.7	-0.7	-0.2	-9.3	51.0	11.4	3.3	1.6	60.1
2011	-3.0	-5.1	-0.8	-0.1	-9.0	58.3	13.6	3.4	1.6	69.5
2012	-4.2	-1.9	0.3	-1.0	-6.7	73.1	18.1	4.2	1.6	85.4
2013	-4.3	-1.6	0.6	-1.1	-6.4	81.3	20.3	4.1	1.7	93.7
2014	-3.6	-1.7	0.6	-1.0	-5.8	86.0	22.7	3.7	1.7	99.3
2015	-2.7	-1.6	0.5	-1.2	-5.0	86.8	24.2	3.3	1.6	99.0
2016	-1.8	-1.0	0.3	-1.5	-4.0	--	--	--	--	99.2
2017	-1.1	-0.6	0.3	-1.5	-2.9	--	--	--	--	98.9
2014 I	-4.1	-1.6	0.5	-1.0	-6.2	84.0	21.8	4.1	1.7	96.6
II	-3.6	-1.8	0.5	-1.3	-6.2	85.7	22.1	4.1	1.7	98.0
III	-3.8	-1.8	0.6	-0.8	-5.7	86.0	22.4	3.9	1.7	98.4
IV	-3.6	-1.7	0.6	-1.0	-5.8	86.0	22.7	3.7	1.7	99.3
2015 I	-3.7	-1.6	0.6	-1.1	-5.8	86.5	22.9	3.6	1.6	99.7
II	-3.1	-1.6	0.7	-1.3	-5.4	86.6	23.6	3.6	1.6	99.3
III	-2.8	-1.6	0.5	-1.3	-5.3	87.3	23.6	3.4	1.6	99.3
IV	-2.7	-1.6	0.5	-1.2	-5.0	86.8	24.2	3.3	1.6	99.0

(a) Excluding financial entities bail-out expenditures.

Sources: National Statistics Institute, Bank of Spain (Financial Accounts of the Spanish Economy) and Funcas (Forecasts).

Chart 9.1.- Government deficit
Percent of GDP, 4-quarter cumulated operations

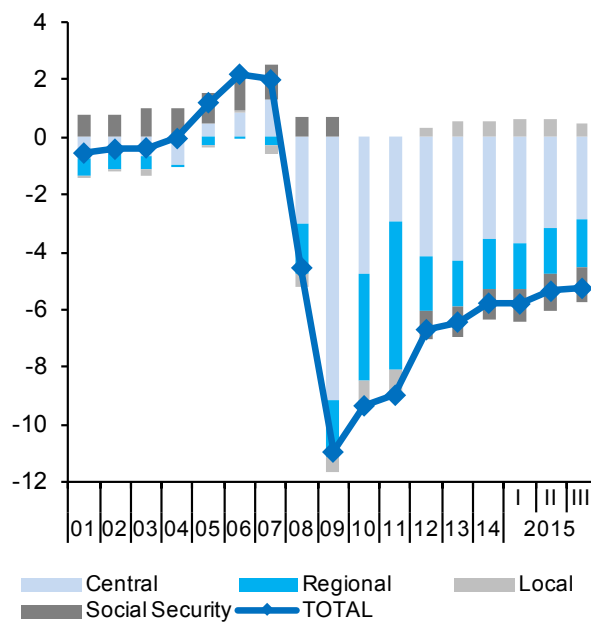


Chart 9.2.- Government debt
Percent of GDP

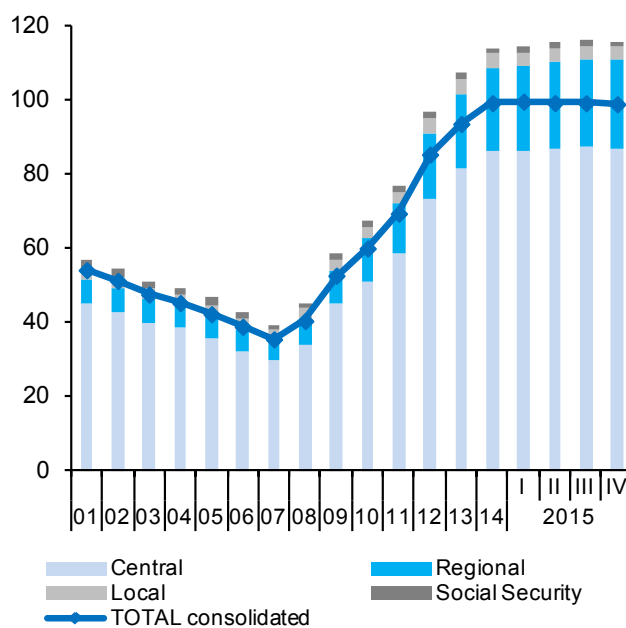


Table 10

General activity and industrial sector indicators (a)

	General activity indicators				Industrial sector indicators					
	Economic Senti- ment Index	Composite PMI index	Social Security affiliates (f)	Electricity consumption (temperature adjusted)	Industrial pro- duction index	Social Secu- rity affiliates in industry	Manufacturing PMI index	Industrial confidence index	Turnover index deflated	Industrial orders
	Index	Index	Thousands	1000 GWH (smoothed)	2010=100	Thou- sands	Index	Balance of responses	2010=100 (smoothed)	Balance of responses
2009	82.6	40.9	17,657	256.9	99.2	2,411	40.9	-30.8	96.5	-54.5
2010	93.1	50.0	17,244	263.8	100.0	2,295	50.6	-13.8	100.0	-36.9
2011	93.1	46.6	16,970	261.3	98.4	2,232	47.3	-12.5	101.1	-30.7
2012	88.4	43.1	16,335	255.7	91.9	2,114	43.8	-17.5	97.0	-36.9
2013	92.5	48.3	15,855	250.2	90.5	2,022	48.5	-13.9	93.8	-30.6
2014	102.4	55.1	16,111	249.8	91.6	2,023	53.2	-7.1	95.1	-16.5
2015	108.8	56.7	16,642	253.6	94.7	2,067	53.6	-0.3	96.5	-5.9
2016 (b)	107.6	54.9	16,697	24.1	91.6	2,083	54.7	-2.0	--	-5.9
2014	II	101.9	55.7	16,045	62.6	2,019	53.0	-8.2	95.4	-18.4
	III	103.2	56.0	16,163	62.5	2,026	53.5	-5.7	95.4	-13.9
	IV	103.9	54.6	16,288	62.6	2,033	53.9	-5.3	95.3	-13.1
2015	I	107.3	56.6	16,430	63.0	2,045	54.2	-3.2	95.7	-11.2
	II	109.3	57.7	16,600	63.3	2,061	54.0	0.9	96.3	-2.6
	III	109.1	57.2	16,708	63.4	2,074	53.4	0.7	96.9	-5.2
	IV	109.6	55.4	16,827	63.3	2,089	53.3	0.3	97.5	-4.6
2016	I(b)	107.6	54.9	16,920	21.0	2,102	53.7	-2.0	--	-5.9
2015	Dec	111.9	55.2	16,868	21.0	2,094	53.4	3.0	97.8	-2.6
2016	Jan	107.8	55.3	16,906	21.0	2,100	53.6	-1.3	--	-5.9
	Feb	107.3	54.5	16,935	--	2,104	53.8	-2.7	--	-6.0
Percentage changes (c)										
2009	--	--	-6.2	-4.7	-15.8	-10.6	--	--	-19.6	--
2010	--	--	-2.3	2.7	0.8	-4.8	--	--	3.6	--
2011	--	--	-1.6	-0.9	-1.6	-2.7	--	--	1.1	--
2012	--	--	-3.7	-2.2	-6.7	-5.3	--	--	-4.1	--
2013	--	--	-2.9	-2.2	-1.5	-4.4	--	--	-3.3	--
2014	--	--	1.6	-0.2	1.3	0.1	--	--	1.4	--
2015	--	--	3.3	1.5	3.4	2.2	--	--	1.4	--
2016	(d)	--	3.2	-3.2	3.2	2.9	--	--	--	--
2014	II	--	2.3	-0.2	0.9	0.8	--	--	1.5	--
	III	--	3.0	-0.6	-0.9	1.4	--	--	-0.1	--
	IV	--	3.1	0.7	1.0	1.4	--	--	-0.5	--
2015	I	--	3.5	2.0	6.0	2.4	--	--	1.6	--
	II	--	4.2	2.0	6.5	3.2	--	--	2.8	--
	III	--	2.6	1.0	2.2	2.6	--	--	2.2	--
	IV	--	2.9	-1.1	2.2	2.8	--	--	2.8	--
2016	I(e)	--	2.2	-1.5	-0.4	2.6	--	--	--	--
2015	Dec	--	0.2	-0.2	0.0	0.2	--	--	0.3	--
2016	Jan	--	0.2	-0.2	-0.1	0.3	--	--	--	--
	Feb	--	0.2	--	--	0.2	--	--	--	--

(a) Seasonally adjusted, except for annual data. (b) Period with available data. (c) Annualized percent change from the previous quarter for quarterly data, non-annualized percent change from the previous month for monthly data, unless otherwise indicated. (d) Growth of available period over the same period of the previous year. (e) Annualized growth of the average of available months over the monthly average of the previous quarter. (f) Excluding domestic service workers and non-professional caregivers.

Sources: European Commission, Markit Economics Ltd., M. of Labour, M. of Industry, National Statistics Institute, REE and Funcas.

Chart 10.1.- General activity indicators (I)
Annualized percent change from previous period

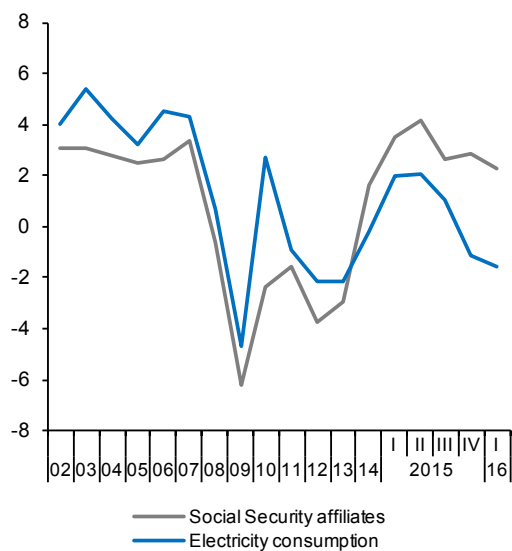


Chart 10.2.- General activity indicators (II)
Index

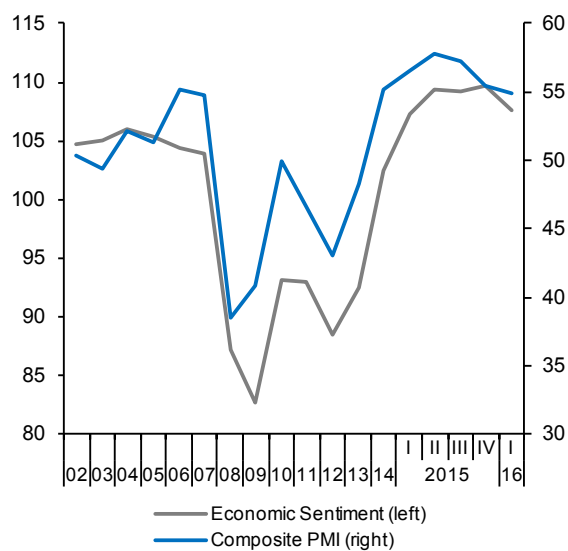


Chart 10.3.- Industrial sector indicators (I)
Annualized percent change from previous period

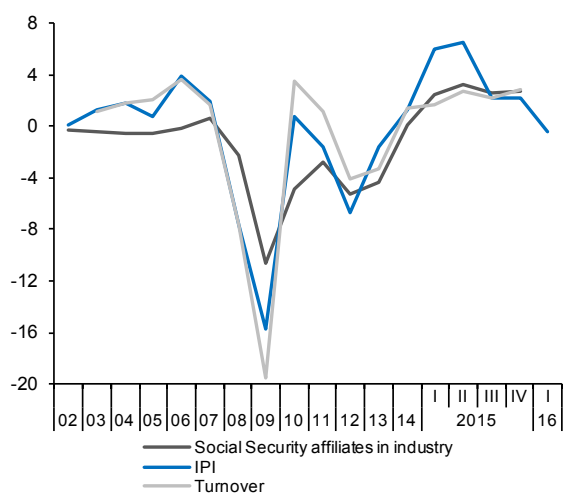


Chart 10.4.- Industrial sector indicators (II)
Index

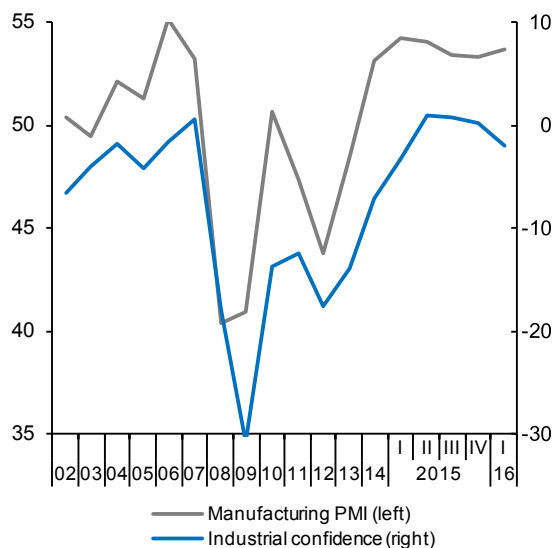


Table 11

Construction and services sector indicators (a)

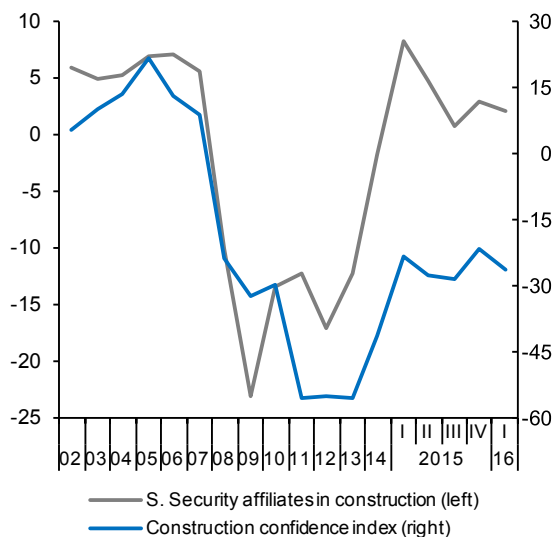
	Construction indicators						Service sector indicators					
	Social Security affiliates in construction	Consumption of cement	Industrial production index construction materials	Construction confidence index	Official tenders (f)	Housing permits (f)	Social Security affiliates in services (g)	Turnover index (nominal)	Services PMI index	Hotel overnight stays	Passenger air transport	Services confidence index
	Thousands	Million Tons	2010=100 (smoothed)	Balance of responses	EUR Billions	Million m²	Thousands	2010=100 (smoothed)	Index	Million (smoothed)	Million (smoothed)	Balance of responses
2009	1,800	28.9	115.9	-32.3	39.6	19.4	12,247	99.2	41.0	251.0	186.3	-29.7
2010	1,559	24.5	100.0	-29.7	26.2	16.3	12,186	100.0	49.3	267.2	191.7	-22.4
2011	1,369	20.4	91.6	-55.4	13.7	14.1	12,176	98.9	46.5	286.8	203.3	-20.8
2012	1,136	13.6	66.8	-54.9	7.4	8.5	11,907	92.8	43.1	280.7	193.2	-21.5
2013	997	10.7	63.1	-55.6	9.2	6.8	11,728	91.0	48.3	286.0	186.5	-15.3
2014	980	10.8	62.1	-41.4	13.1	6.9	11,995	93.3	55.2	295.3	194.9	9.9
2015	1,027	11.4	66.9	-25.3	10.1	9.9	12,432	97.8	57.3	308.2	206.6	19.4
2016 (b)	1,017	1.6	60.6	-26.3	0.5	--	12,466	--	54.3	14.4	26.1	18.6
2014 II	974	2.7	62.5	-55.8	3.1	1.8	11,945	92.8	55.7	73.4	48.2	9.1
III	983	2.8	61.2	-35.0	3.4	1.8	12,044	93.7	56.7	73.9	48.8	8.8
IV	995	2.8	61.8	-22.6	2.9	1.8	12,147	94.7	54.3	74.5	49.3	14.0
2015 I	1,015	2.8	63.8	-23.3	2.7	2.0	12,277	95.9	56.7	75.2	49.9	17.5
II	1,027	2.9	66.0	-27.7	2.9	2.3	12,391	97.2	58.3	76.2	50.8	20.1
III	1,029	2.8	68.0	-28.5	1.8	2.5	12,482	98.3	58.1	77.5	52.0	19.7
IV	1,036	2.9	69.5	-21.7	2.7	2.7	12,578	99.2	55.9	79.2	53.7	20.2
2016 I (b)	1,042	1.9	70.4	-26.3	0.5	--	12,657	--	54.3	26.8	36.8	18.6
2015 Dec	1,039	1.0	70.0	-18.9	1.2	1.3	12,610	99.5	55.1	26.6	18.1	21.3
2016 Jan	1,040	0.9	70.4	-29.9	0.5	--	12,643	--	54.6	26.8	18.3	18.7
Feb	1,043	1.0	--	-22.7	--	--	12,671	--	54.1	--	18.5	18.5
Percentage changes (c)												
2009	-23.1	-32.3	-25.1	--	-0.4	-56.8	-3.1	-13.4	--	-6.5	-7.9	--
2010	-13.4	-15.4	-13.7	--	-33.9	-16.1	-0.5	0.8	--	6.4	2.9	--
2011	-12.2	-16.4	-8.4	--	-47.9	-13.2	-0.1	-1.1	--	7.3	6.0	--
2012	-17.0	-33.6	-27.0	--	-45.5	-39.9	-2.2	-6.2	--	-2.1	-5.0	--
2013	-12.2	-20.9	-5.7	--	23.2	-20.3	-1.5	-2.0	--	1.9	-3.5	--
2014	-1.7	0.8	-1.4	--	42.6	2.2	2.3	2.6	--	3.2	4.6	--
2015	4.7	5.4	7.7	--	-22.7	42.6	3.6	4.8	--	4.4	6.0	--
2016 (d)	3.0	3.9	12.6	--	-27.8	--	3.3	--	--	8.2	14.3	--
2014 II	1.3	17.3	-7.4	--	46.4	0.3	3.2	3.1	--	1.9	5.6	--
III	3.7	18.7	-8.0	--	32.8	7.0	3.4	3.8	--	2.5	5.3	--
IV	5.0	-0.1	3.9	--	1.2	12.2	3.5	4.3	--	3.4	4.2	--
2015 I	8.3	3.3	13.5	--	-26.3	23.4	4.3	5.2	--	3.9	5.0	--
II	4.8	9.4	14.6	--	-6.6	32.4	3.7	5.5	--	5.2	7.3	--
III	0.8	-11.5	12.3	--	-46.8	34.1	3.0	4.7	--	7.0	10.1	--
IV	2.9	25.9	9.5	--	-7.5	29.9	3.1	3.8	--	9.2	13.1	--
2016 I (e)	2.2	-10.2	5.5	--	-27.8	--	2.6	--	--	6.5	12.2	--
2015 Dec	0.2	-2.3	0.7	--	26.3	99.9	0.3	0.3	--	0.8	1.1	--
2016 Jan	0.1	-3.6	0.7	--	-27.8	--	0.3	--	--	0.8	1.2	--
Feb	0.3	2.2	--	--	--	--	0.2	--	--	--	1.2	--

(a) Seasonally adjusted, except for annual data and (f). (b) Period with available data. (c) Annualized percent change from the previous quarter for quarterly data, non-annualized percent change from the previous month for monthly data, unless otherwise indicated. (d) Growth of available period over the same period of the previous year. (e) Annualized growth of the average of available months over the monthly average of the previous quarter. (f) Percent changes are over the same period of the previous year. (g) Excluding domestic service workers and non-professional caregivers.

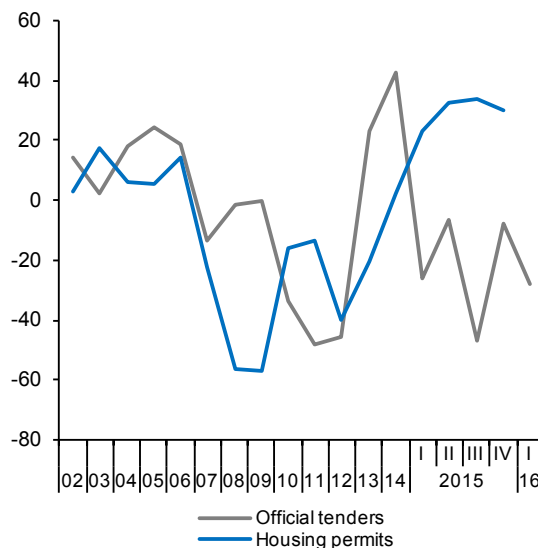
Sources: European Commission, Markit Economics Ltd., M. of Labour, M. of Public Works, National Statistics Institute, AENA, OFICEMEN, SEOPAN and Funcas.

Chart 11.1.- Construction indicators (I)

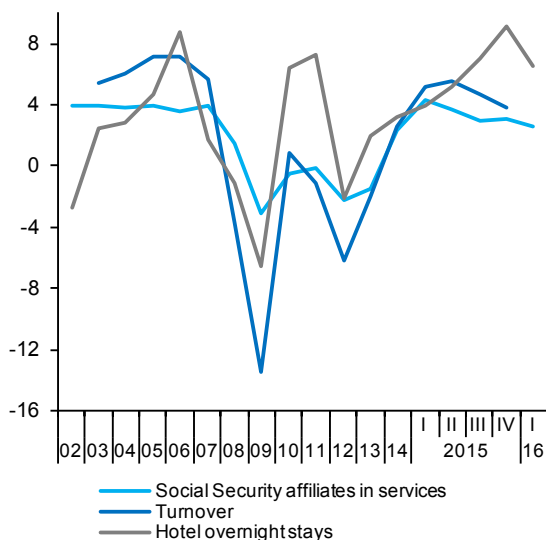
Annualized percentage changes from previous period and index

**Chart 11.2.- Construction indicators (II)**

Annualized percentage changes from previous period

**Chart 11.3.- Services indicators (I)**

Percentage changes from previous period

**Chart 11.4.- Services indicators (II)**

Index

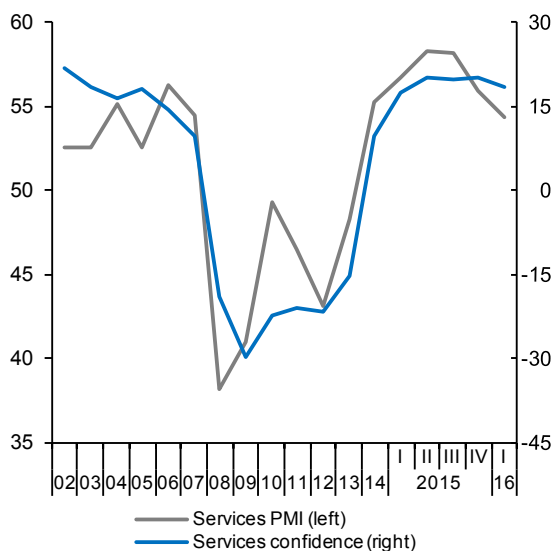


Table 12

Consumption and investment indicators (a)

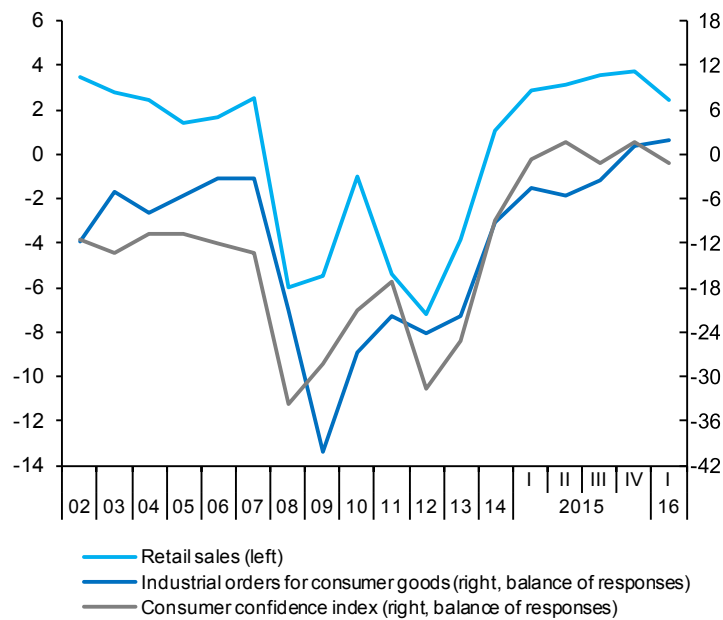
	Consumption indicators					Investment in equipment indicators		
	Retail sales deflated	Car registrations	Consumer confidence index	Hotel overnight stays by residents in Spain	Industrial orders for consumer goods	Cargo vehicles registrations	Industrial orders for investment goods	Import of capital goods (volume)
	2010=100 (smoothed)	Thousands (smoothed)	Balance of responses	Million (smoothed)	Balance of responses	Thousands (smoothed)	Balance of responses	2005=100 (smoothed)
2009	101.0	971.2	-28.3	109.8	-40.2	142.1	-50.8	66.6
2010	100.0	1,000.1	-20.9	113.2	-26.7	152.1	-31.1	70.9
2011	94.6	808.3	-17.1	111.5	-21.7	142.0	-23.0	68.7
2012	87.8	710.6	-31.7	102.1	-24.2	107.7	-38.6	61.3
2013	84.4	742.3	-25.3	100.6	-21.8	107.6	-33.5	70.0
2014	85.3	890.1	-8.9	104.7	-9.2	137.5	-16.1	83.1
2015	87.9	1,094.0	0.3	110.3	-3.1	180.3	0.2	95.3
2016 (b)	93.5	81.7	-1.2	5.4	1.8	12.7	0.1	--
2014	II	84.8	217.0	-6.1	25.8	-7.8	-16.9	83.0
	III	85.3	228.0	-7.9	26.2	-7.3	-15.8	84.5
	IV	85.9	241.4	-9.6	26.7	-10.0	-11.3	87.3
2015	I	86.5	254.8	-0.6	27.0	-4.5	-9.1	92.4
	II	87.2	265.7	1.6	27.3	-5.6	5.7	96.1
	III	88.0	276.8	-1.3	27.6	-3.4	-0.7	96.3
	IV	88.8	289.6	1.6	27.8	1.2	4.9	92.7
2016 I (b)	89.3	99.5	-1.2	9.4	1.8	16.0	0.1	--
2015 Dec	89.0	98.0	5.4	9.3	3.7	15.9	-3.2	--
2016 Jan	89.3	99.5	-0.9	9.4	2.7	16.0	-7.8	--
Feb	--	--	-1.4	--	0.9	--	-9.5	--
Percentage changes (c)								
2009	-5.5	-18.1	--	-3.0	--	-40.0	--	-26.3
2010	-1.0	3.0	--	3.2	--	7.0	--	6.5
2011	-5.4	-19.2	--	-1.5	--	-6.6	--	-3.1
2012	-7.2	-12.1	--	-8.4	--	-24.2	--	-10.7
2013	-3.8	4.5	--	-1.4	--	-0.1	--	14.1
2014	1.0	19.9	--	4.1	--	27.8	--	18.7
2015	3.0	22.9	--	5.3	--	31.1	--	14.8
2016 (d)	3.7	14.7	--	8.9	--	12.7	--	--
2014	II	2.1	24.8	--	5.2	--	--	16.3
	III	2.6	21.8	--	6.5	--	--	7.5
	IV	2.8	25.6	--	6.3	--	--	14.2
2015	I	2.8	24.1	--	5.5	--	--	25.3
	II	3.1	18.3	--	4.8	--	--	17.1
	III	3.5	17.7	--	3.3	--	--	0.6
	IV	3.7	19.8	--	4.0	--	--	-14.1
2016 I (e)	2.5	13.0	--	4.3	--	5.2	--	--
2015 Dec	0.3	1.5	--	0.5	--	0.6	--	-1.6
2016 Jan	0.3	1.6	--	0.6	--	0.6	--	-1.8
Feb	--	--	--	--	--	--	--	--

(a) Seasonally adjusted, except for annual data. (b) Period with available data. (c) Annualized percent change from the previous quarter for quarterly data, non-annualized percent change from the previous month for monthly data, unless otherwise indicated. (d) Growth of available period over the same period of the previous year. (e) Annualized growth of the average of available months over the monthly average of the previous quarter.

Sources: European Commission, M. of Economy, M. of Industry, National Statistics Institute, DGT, ANFAC and Funcas.

Chart 12.1.- Consumption indicators

Percent change from previous period and balance of responses

**Chart 12.2.- Investment indicators**

Percent change from previous period and balance of responses

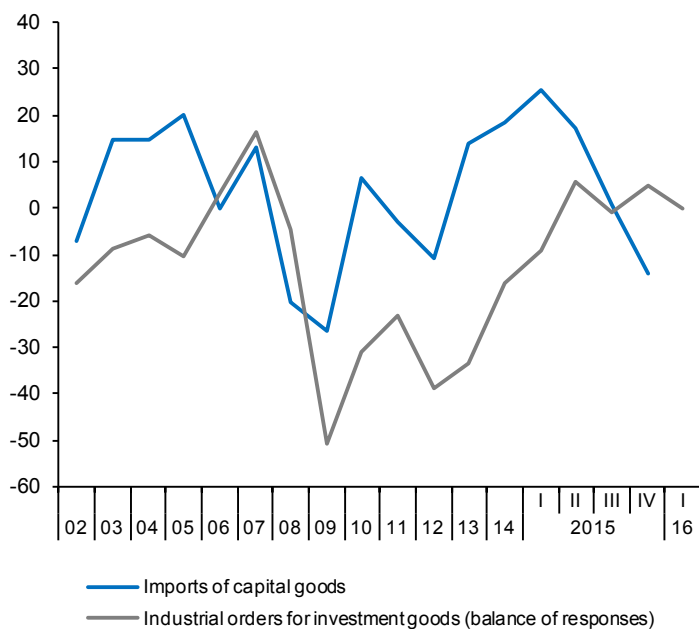


Table 13a

Labour market (I)

Forecasts in blue

		Population aged 16-64	Labour force		Employment		Unemployment		Participation rate 16-64 (a)	Employment rate 16-64 (b)	Unemployment rate (c)			
			Original	Seasonally adjusted	Original	Seasonally adjusted	Original	Seasonally adjusted			Total	Aged 16-24	Spanish	Foreign
		1	2=4+6	3=5+7	4	5	6	7	Seasonally adjusted					
Million								Percentage						
2009		31.2	23.3	--	19.1	--	4.2	--	74.1	60.8	17.9	37.7	16.0	28.2
2010		31.1	23.4	--	18.7	--	4.6	--	74.6	59.7	19.9	41.5	18.1	29.9
2011		31.1	23.4	--	18.4	--	5.0	--	74.9	58.8	21.4	46.2	19.5	32.6
2012		30.9	23.4	--	17.6	--	5.8	--	75.3	56.5	24.8	52.9	23.0	35.9
2013		30.6	23.2	--	17.1	--	6.1	--	75.3	55.6	26.1	55.5	24.4	37.0
2014		30.3	23.0	--	17.3	--	5.6	--	75.3	56.8	24.4	53.2	23.0	34.5
2015		30.2	22.9	--	17.9	--	5.1	--	75.5	58.7	22.1	48.3	20.9	30.5
2016		30.1	22.8	--	18.3	--	4.6	--	75.4	60.3	19.9	--	--	--
2017		30.0	22.8	--	18.7	--	4.1	--	75.5	61.7	18.2	--	--	--
2014	I	30.3	22.9	22.9	17.0	17.1	5.9	5.8	75.1	55.4	25.3	54.4	23.7	36.2
	II	30.3	23.0	22.9	17.4	17.3	5.6	5.6	75.2	56.8	24.5	52.7	23.1	34.4
	III	30.3	22.9	22.9	17.5	17.4	5.4	5.5	75.2	57.3	24.1	53.5	22.8	33.7
	IV	30.3	23.0	23.0	17.6	17.5	5.5	5.4	75.5	57.6	23.7	51.7	22.4	33.2
2015	I	30.2	22.9	23.0	17.5	17.7	5.4	5.3	75.4	57.3	23.1	50.2	21.8	32.1
	II	30.2	23.0	23.0	17.9	17.8	5.1	5.1	75.6	58.7	22.4	48.9	20.9	33.0
	III	30.2	22.9	22.9	18.0	17.9	4.9	4.9	75.4	59.4	21.6	47.7	20.0	33.2
	IV	30.1	22.9	22.8	18.1	18.1	4.8	4.8	75.3	59.5	20.9	46.2	19.1	32.8
Percentage changes (d)								Difference from one year ago						
2009		0.4	0.8	--	-6.7	--	60.0	--	0.3	-4.6	6.6	13.3	5.8	10.8
2010		-0.1	0.4	--	-2.0	--	11.7	--	0.4	-1.2	2.0	3.8	2.1	1.7
2011		-0.2	0.3	--	-1.6	--	8.0	--	0.4	-0.9	1.5	4.7	1.4	2.7
2012		-0.5	0.0	--	-4.3	--	15.9	--	0.4	-2.3	3.4	6.7	3.5	3.3
2013		-1.1	-1.1	--	-2.8	--	4.1	--	0.0	-0.9	1.3	2.6	1.5	1.1
2014		-0.9	-1.0	--	1.2	--	-7.3	--	0.0	1.2	-1.7	-2.3	-1.4	-2.5
2015		-0.5	-0.1	--	3.0	--	-9.9	--	0.2	1.9	-2.4	-4.9	-2.1	-4.0
2016		-0.4	-0.3	--	2.4	--	-10.0	--	0.0	1.6	-2.1	--	--	--
2017		-0.3	-0.2	--	2.0	--	-8.8	--	0.1	1.4	-1.7	--	--	--
2014	I	-1.3	-1.8	-2.0	-0.5	0.4	-5.5	-8.9	-0.3	0.5	-1.0	-1.6	-0.8	-1.5
	II	-1.0	-1.0	0.3	1.1	4.4	-7.0	-11.1	0.1	1.3	-1.5	-2.7	-1.4	-1.6
	III	-0.8	-1.0	-0.5	1.6	1.7	-8.7	-7.1	-0.2	1.3	-1.9	-1.7	-1.6	-3.8
	IV	-0.6	-0.2	1.3	2.5	3.5	-8.1	-5.5	0.2	1.7	-2.0	-3.2	-1.8	-3.2
2015	I	-0.4	0.1	-0.7	3.0	2.4	-8.2	-10.2	0.3	1.8	-2.2	-4.1	-1.9	-4.1
	II	-0.5	0.2	0.4	3.0	4.0	-8.4	-10.9	0.4	1.9	-2.1	-3.8	-2.2	-1.4
	III	-0.5	-0.1	-1.4	3.1	2.6	-10.6	-14.5	0.2	2.1	-2.5	-5.8	-2.8	-0.5
	IV	-0.5	-0.7	-0.9	3.0	2.9	-12.4	-13.9	-0.2	1.9	-2.8	-5.5	-3.2	-0.4

(a) Labour force aged 16-64 over population aged 16-64. (b) Employed aged 16-64 over population aged 16-64. (c) Unemployed in each group over labour force in that group. (d) Annual percentage changes for original data; annualized quarterly percentage changes for S.A. data.

Sources: INE (Labour Force Survey) and Funcas.

Chart 13a.1.- Labour force, Employment and Unemployment, SA
Annual / annualized quarterly growth rates and percentage of active population

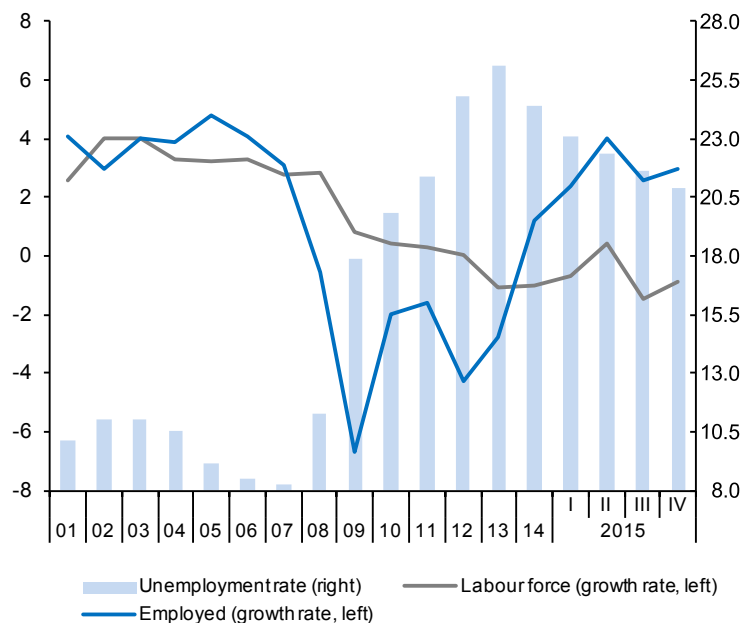


Chart 13a.2.- Unemployment rates, SA
Percentage

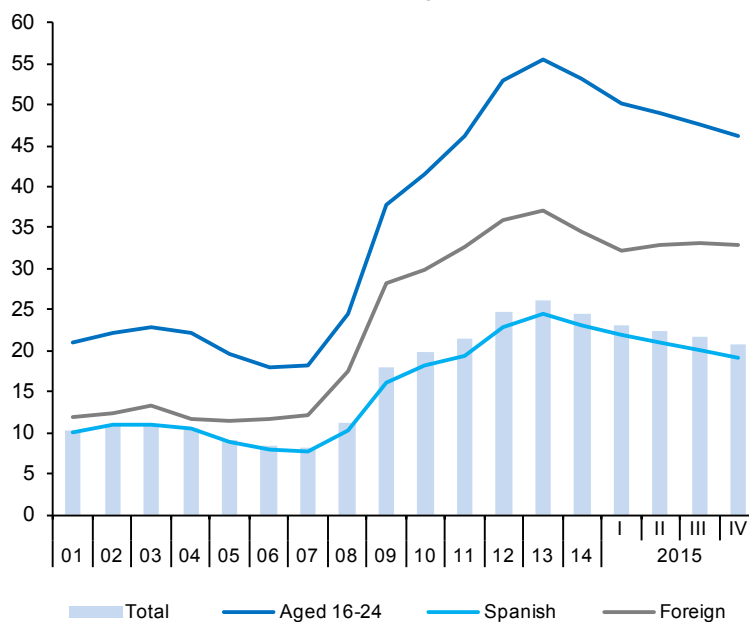


Table 13b

Labour market (II)

	Employed by sector				Employed by professional situation					Employed by duration of the working-day			
	Agriculture	Industry	Construc- tion	Services	Employees				Self-emplo- yed	Full-time	Part-time	Part-time employ- ment rate (b)	
					Total	By type of contract							
						Temporary	Indefinite	Temporary employment rate (a)					
	1	2	3	4	5=6+7	6	7	8=6/5	9	10	11	12	
Million (original data)													
2009	0.79	2.81	1.89	13.62	15.88	4.00	11.88	25.2	3.23	16.71	2.40	12.5	
2010	0.79	2.65	1.65	13.64	15.59	3.86	11.73	24.7	3.13	16.29	2.44	13.0	
2011	0.76	2.60	1.40	13.66	15.39	3.87	11.52	25.1	3.03	15.92	2.50	13.6	
2012	0.74	2.48	1.16	13.24	14.57	3.41	11.16	23.4	3.06	15.08	2.55	14.5	
2013	0.74	2.36	1.03	13.02	14.07	3.26	10.81	23.1	3.07	14.43	2.71	15.8	
2014	0.74	2.38	0.99	13.23	14.29	3.43	10.86	24.0	3.06	14.59	2.76	15.9	
2015	0.74	2.48	1.07	13.57	14.77	3.71	11.06	25.1	3.09	15.05	2.81	15.7	
2014	I	0.81	2.30	0.94	12.90	13.93	3.22	10.71	23.1	3.02	14.20	2.75	16.2
	II	0.74	2.36	0.98	13.28	14.32	3.43	10.89	24.0	3.04	14.51	2.84	16.4
	III	0.67	2.43	1.02	13.39	14.41	3.55	10.86	24.6	3.09	14.88	2.62	15.0
	IV	0.73	2.44	1.03	13.37	14.48	3.51	10.97	24.2	3.09	14.75	2.82	16.1
2015	I	0.72	2.44	1.06	13.24	14.39	3.40	11.00	23.6	3.06	14.62	2.84	16.3
	II	0.74	2.51	1.09	13.53	14.76	3.70	11.06	25.1	3.10	15.05	2.82	15.8
	III	0.71	2.52	1.08	13.74	14.95	3.91	11.04	26.2	3.10	15.30	2.75	15.2
	IV	0.78	2.46	1.06	13.79	14.99	3.85	11.14	25.7	3.11	15.25	2.84	15.7
Annual percentage changes								Difference from one year ago	Annual percentage changes		Difference from one year ago		
2009	-4.8	-13.3	-23.2	-2.3	-5.8	-18.4	-0.6	-3.9	-10.6	-7.5	-0.4	0.8	
2010	-0.3	-5.6	-12.6	0.1	-1.8	-3.6	-1.2	-0.5	-2.9	-2.5	1.7	0.5	
2011	-3.9	-1.7	-15.0	0.2	-1.3	0.3	-1.8	0.4	-3.3	-2.2	2.5	0.5	
2012	-1.6	-4.6	-17.3	-3.0	-5.3	-11.8	-3.1	-1.7	1.1	-5.3	2.3	0.9	
2013	-0.9	-5.2	-11.4	-1.7	-3.5	-4.6	-3.1	-0.3	0.4	-4.3	6.0	1.3	
2014	-0.1	1.0	-3.5	1.7	1.5	5.3	0.4	0.9	-0.4	1.1	1.9	0.1	
2015	0.1	4.3	8.1	2.6	3.4	8.3	1.9	1.1	1.1	3.2	1.9	-0.2	
2014	I	12.9	-3.4	-11.6	0.2	-0.4	5.0	-1.9	1.2	-0.7	-0.9	2.1	0.4
	II	-1.8	-0.1	-5.3	2.0	1.7	6.5	0.3	1.1	-1.7	0.8	2.6	0.2
	III	-4.8	3.5	-0.5	1.8	2.0	4.6	1.3	0.6	-0.5	1.8	0.4	-0.2
	IV	-6.2	4.2	4.0	2.6	2.8	5.3	2.0	0.6	1.4	2.6	2.4	0.0
2015	I	-11.3	6.2	12.6	2.6	3.3	5.4	2.7	0.5	1.3	2.9	3.3	0.1
	II	0.1	6.4	11.6	1.9	3.1	8.0	1.6	1.1	2.3	3.7	-0.9	-0.6
	III	6.5	3.8	5.9	2.6	3.7	10.1	1.6	1.5	0.3	2.8	4.8	0.2
	IV	7.0	1.0	2.7	3.2	3.5	9.5	1.6	1.4	0.6	3.4	0.8	-0.3

(a) Percentage of employees with temporary contract over total employees. (b) Percentage of part-time employed over total employed.

Source: INE (Labour Force Survey).

Chart 13b.1.- Employment by sector
Annual percentage changes

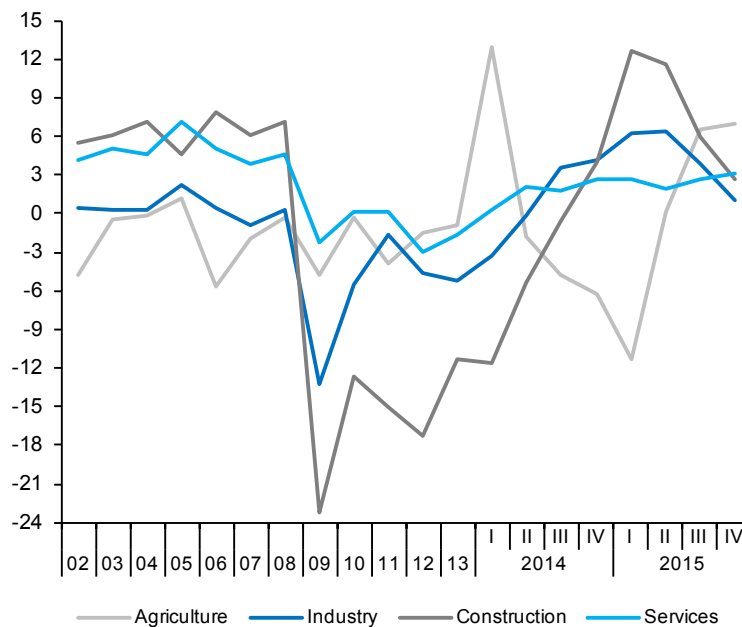


Chart 13b.2.- Employment by type of contract

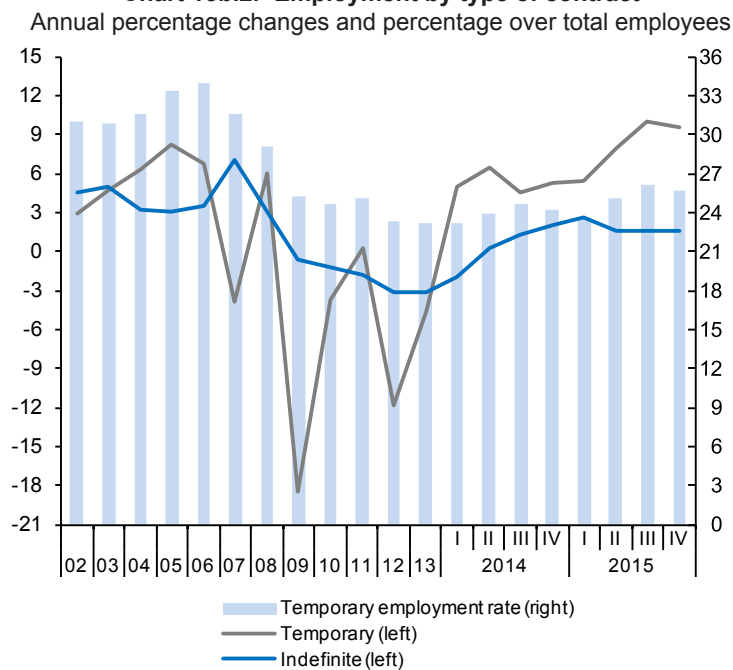


Table 14

Index of Consumer Prices

Forecasts in blue

	Total	Total excluding food and energy	Excluding unprocessed food and energy				Unprocessed food	Energy	Food
			Total	Non-energy industrial goods	Services	Processed food			
% of total in 2016	100.0	67.06	82.12	26.94	40.13	15.06	6.45	11.42	21.50
Indexes, 2011 = 100									
2010	96.9	98.7	98.3	99.4	98.3	96.4	98.2	86.4	96.9
2011	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
2012	102.4	101.3	101.6	100.8	101.5	103.1	102.3	108.9	102.8
2013	103.9	102.4	103.0	101.4	102.9	106.2	105.9	108.9	106.1
2014	103.7	102.3	103.1	101.0	103.1	106.6	104.6	108.0	106.0
2015	103.2	102.9	103.7	101.3	103.8	107.6	106.4	98.3	107.3
2016	103.0	103.8	104.7	101.7	105.1	108.9	108.4	89.3	108.8
Annual percentage changes									
2010	1.8	0.6	0.6	-0.5	1.3	1.0	0.0	12.5	0.7
2011	3.2	1.3	1.7	0.6	1.8	3.8	1.8	15.7	3.2
2012	2.4	1.3	1.6	0.8	1.5	3.1	2.3	8.9	2.8
2013	1.4	1.1	1.4	0.6	1.4	3.1	3.6	0.0	3.2
2014	-0.2	0.0	0.0	-0.4	0.1	0.4	-1.2	-0.8	-0.1
2015	-0.5	0.5	0.6	0.3	0.7	0.9	1.8	-9.0	1.2
2016	-0.2	0.9	1.0	0.4	1.2	1.2	1.8	-9.1	1.4
2015	Jan	-1.3	0.2	0.2	-0.1	0.5	-0.1	-0.7	-0.3
	Feb	-1.1	0.2	0.2	-0.1	0.3	0.1	0.9	-10.2
	Mar	-0.7	0.2	0.2	-0.2	0.4	0.3	0.9	-7.4
	Apr	-0.6	0.2	0.3	0.0	0.3	0.7	0.2	-7.2
	May	-0.2	0.4	0.5	0.1	0.6	0.9	2.3	-6.4
	Jun	0.1	0.5	0.6	0.3	0.7	1.2	3.2	-5.7
	Jul	0.1	0.7	0.8	0.4	0.9	1.2	1.7	-5.8
	Aug	-0.4	0.6	0.7	0.3	0.8	1.4	2.7	-9.8
	Sep	-0.9	0.7	0.8	0.4	0.9	1.4	2.6	-13.6
	Oct	-0.7	0.8	0.9	0.6	1.0	1.4	2.7	-13.1
	Nov	-0.3	0.9	1.0	0.7	1.0	1.4	2.4	-9.9
	Dec	0.0	0.8	0.9	0.6	0.9	1.4	2.5	-7.5
2016	Jan	-0.3	0.8	0.9	0.5	1.0	1.4	3.3	-10.3
	Feb	-0.8	1.0	1.0	0.5	1.3	1.3	0.8	-14.1
	Mar	-0.9	1.1	1.1	0.5	1.5	1.3	2.1	-16.2
	Apr	-0.9	0.8	0.8	0.4	1.0	1.2	2.8	-14.2
	May	-0.8	0.9	0.9	0.4	1.2	1.2	1.7	-13.8
	Jun	-0.8	0.9	0.9	0.4	1.2	1.2	1.1	-13.2
	Jul	-0.5	0.9	0.9	0.5	1.2	1.1	2.6	-11.8
	Aug	0.1	1.0	1.0	0.6	1.3	1.1	1.7	-7.0
	Sep	0.5	1.0	1.0	0.5	1.3	1.1	1.9	-3.8
	Oct	0.5	0.9	0.9	0.4	1.3	1.0	0.5	-2.3
	Nov	0.5	0.9	0.9	0.3	1.2	1.0	1.3	-2.6
	Dec	0.9	0.9	0.9	0.3	1.3	1.1	2.1	0.0

Sources: INE and Funcas (Forecasts).

Chart 14.1.- Inflation rate (I)
Annual percentage changes

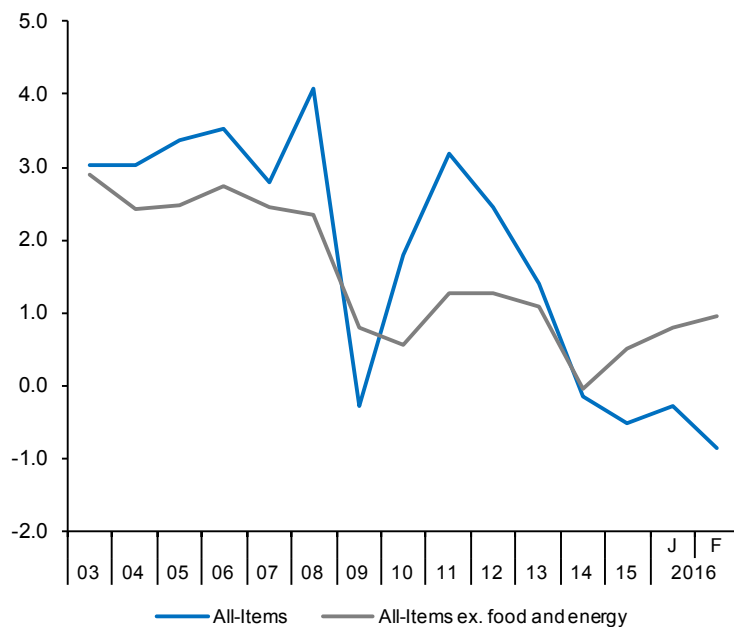


Chart 14.2.- Inflation rate (II)
Annual percentage changes

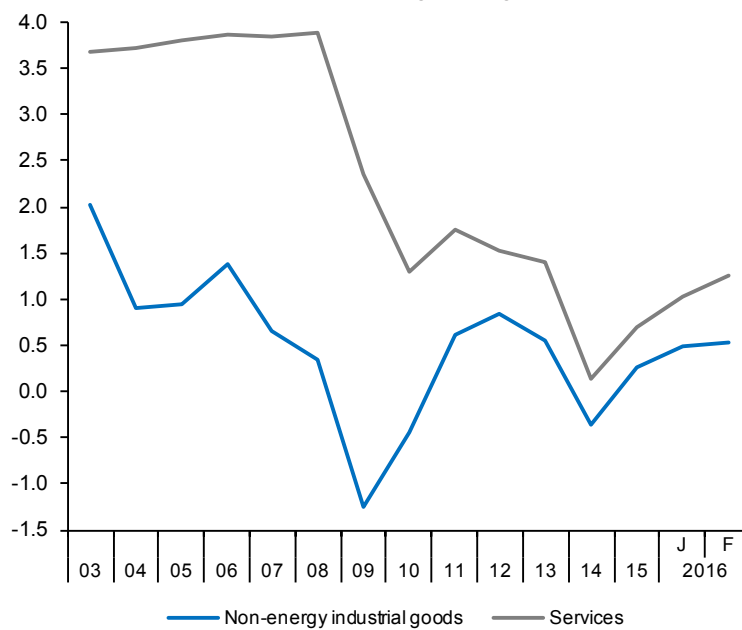


Table 15

Other prices and costs indicators

		GDP deflator (a)	Industrial producer prices		Housing prices		Urban land prices (M. Public Works)	Labour Costs Survey				Wage increases agreed in collective bargaining
			Total	Excluding energy	Housing Price Index (INE)	M² average price (M. Public Works)		Total labour costs per worker	Wage costs per worker	Other cost per worker	Total labour costs per hour worked	
		2010=100	2010=100		2007=100			2000=100				
2008		99.6	99.8	100.5	98.5	100.7	91.1	137.4	134.8	145.6	142.8	--
2009		99.8	96.4	98.2	91.9	93.2	85.8	142.3	139.2	151.8	150.0	--
2010		100.0	100.0	100.0	90.1	89.6	74.8	142.8	140.4	150.2	151.5	--
2011		100.0	106.9	104.2	83.4	84.6	69.8	144.5	141.9	152.5	154.8	--
2012		100.1	111.0	105.9	72.0	77.2	65.4	143.6	141.1	151.3	154.7	--
2013		100.6	111.7	106.7	64.3	72.7	55.1	143.8	141.1	152.2	155.2	--
2014		100.2	110.2	105.9	64.5	71.0	52.6	143.3	140.9	150.7	155.5	--
2015		100.9	107.9	106.2	66.8	71.7	54.9	144.2	142.5	149.6	156.5	--
2016	(b)	--	102.8	105.4	--	--	--	--	--	--	--	--
2014	I	100.1	109.8	105.7	63.6	71.0	50.8	139.8	135.2	154.0	145.6	--
	II	100.2	110.6	105.8	64.7	71.0	52.5	145.9	144.5	150.2	153.9	--
	III	100.3	111.2	106.0	64.8	70.8	51.2	138.5	134.8	149.7	160.3	--
	IV	100.4	109.1	105.8	65.0	71.2	55.9	149.1	149.2	148.9	162.2	--
2015	I	100.7	107.7	105.9	64.6	70.9	53.8	140.6	137.2	151.1	147.0	--
	II	100.7	109.2	106.5	67.3	71.8	55.0	146.5	145.4	149.8	154.6	--
	III	101.0	108.5	106.6	67.8	71.8	56.1	138.8	135.6	148.9	160.0	--
	IV	101.1	106.1	105.7	67.7	72.5	54.5	151.0	151.8	148.6	164.5	--
2015	Dec	--	105.5	105.5	--	--	--	--	--	--	--	--
2016	Jan	--	102.8	105.4	--	--	--	--	--	--	--	--
	Feb	--	--	--	--	--	--	--	--	--	--	--
Annual percent changes												
2008		2.1	6.5	4.5	-1.5	0.7	-8.9	4.8	5.1	4.0	5.2	3.6
2009		0.3	-3.4	-2.3	-6.7	-7.4	-5.8	3.5	3.2	4.3	5.1	2.3
2010		0.2	3.7	1.8	-2.0	-3.9	-12.8	0.4	0.9	-1.1	1.0	1.5
2011		0.0	6.9	4.2	-7.4	-5.6	-6.7	1.2	1.0	1.6	2.2	2.0
2012		0.0	3.8	1.7	-13.7	-8.7	-6.4	-0.6	-0.6	-0.8	-0.1	1.0
2013		0.6	0.6	0.7	-10.6	-5.8	-15.7	0.2	0.0	0.6	0.3	0.5
2014		-0.4	-1.3	-0.8	0.3	-2.4	-4.6	-0.3	-0.1	-1.0	0.2	0.5
2015		0.6	-2.1	0.3	3.6	1.1	4.3	0.6	1.1	-0.7	0.6	0.8
2016	(c)	--	-4.2	-0.4	--	--	--	--	--	--	--	1.1
2014	I	-0.5	-2.2	-1.5	-1.6	-3.8	-10.0	-0.3	-0.2	-0.6	0.3	0.6
	II	-0.5	-0.1	-1.0	0.8	-2.9	-9.3	0.0	0.0	-0.3	0.8	0.5
	III	-0.2	-0.9	-0.4	0.3	-2.6	-3.3	-0.4	-0.1	-1.4	-0.1	0.6
	IV	-0.3	-2.1	-0.1	1.8	-0.3	5.2	-0.5	-0.2	-1.6	-0.2	0.5
2015	I	0.5	-1.9	0.2	1.5	-0.1	5.9	0.5	1.4	-1.9	0.9	0.7
	II	0.5	-1.2	0.7	4.0	1.2	4.7	0.4	0.6	-0.2	0.5	0.7
	III	0.7	-2.4	0.5	4.5	1.4	9.7	0.3	0.5	-0.5	-0.1	0.8
	IV	0.7	-2.8	-0.1	4.2	1.8	-2.4	1.2	1.7	-0.2	1.4	0.8
2015	Dec	--	-2.2	-0.2	--	--	--	--	--	--	--	0.8
2016	Jan	--	-4.2	-0.4	--	--	--	--	--	--	--	1.1
	Feb	--	--	--	--	--	--	--	--	--	--	1.1

(a) Seasonally adjusted. (b) Period with available data. (c) Growth of available period over the same period of the previous year.

Sources: M. of Public Works, M. of Labour and INE (National Statistics Institute).

Chart 15.1.- Housing and Urban land prices
Index (2007=100)

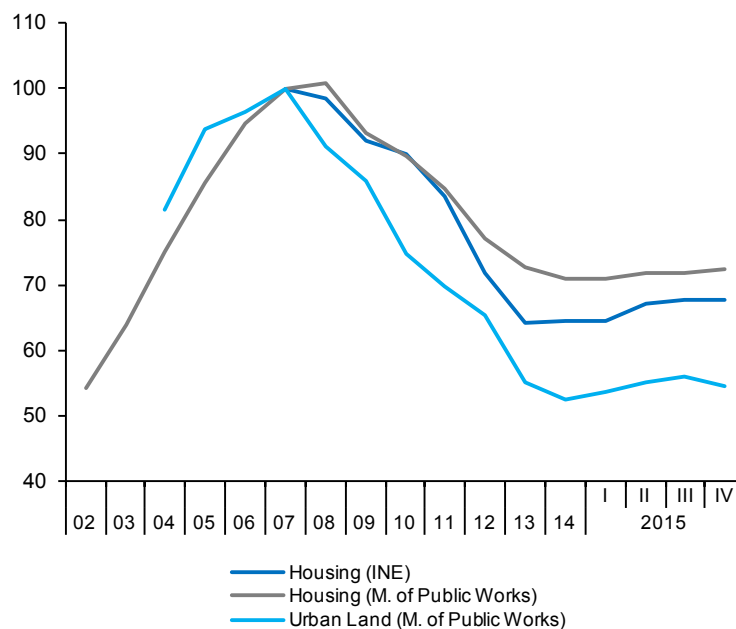


Chart 15.2.- Wage costs
Annual percent change

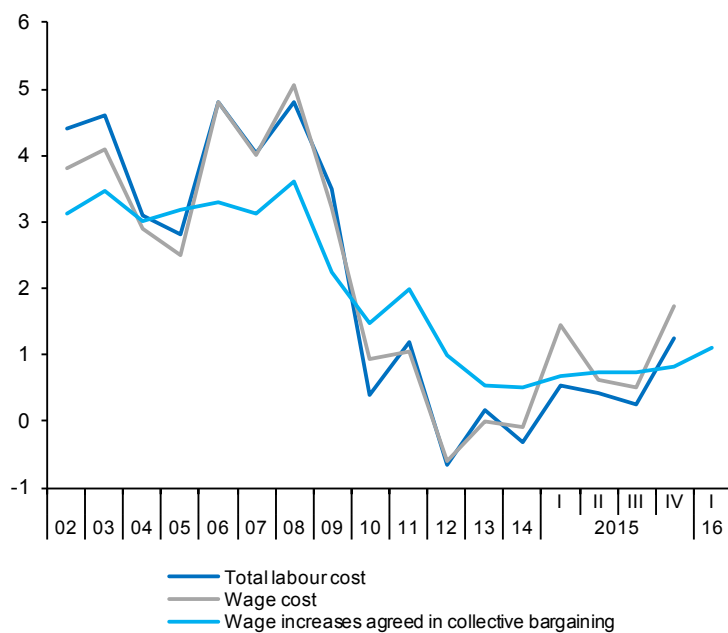


Table 16

External trade (a)

	Exports of goods			Imports of goods			Exports to EU countries	Exports to non-EU countries	Total Balance of goods	Balance of goods excluding energy	Balance of goods with EU countries	
	Nominal	Prices	Real	Nominal	Prices	Real						
	EUR Billions	2005=100		EUR Billions	2005=100		EUR Billions					
2008	189.2	109.0	112.0	283.4	109.1	111.5	131.0	58.2	-94.2	-50.7	-26.0	
2009	159.9	101.6	101.5	206.1	96.2	92.0	110.7	49.2	-46.2	-18.8	-8.9	
2010	186.8	103.2	116.7	240.1	100.6	102.4	126.5	60.3	-53.3	-17.9	-4.8	
2011	215.2	108.2	128.4	263.1	109.1	103.5	142.6	72.6	-47.9	-4.0	3.6	
2012	226.1	110.4	132.2	257.9	114.2	97.0	143.2	82.9	-31.8	14.3	12.2	
2013	235.8	110.2	138.1	252.3	109.3	99.1	147.7	88.1	-16.5	25.4	17.1	
2014	240.0	109.1	142.3	264.5	106.7	106.8	152.3	87.7	-24.5	15.4	11.2	
2015	250.2	109.7	148.9	274.4	104.1	113.9	162.1	88.2	-24.2	3.2	8.5	
2014	I	58.7	109.0	139.5	65.5	105.5	107.1	37.5	21.2	-6.8	4.6	3.1
	II	60.2	108.7	143.2	65.8	106.6	106.6	37.7	22.5	-5.7	4.2	2.5
	III	62.0	109.1	147.1	67.4	107.6	108.1	38.9	23.1	-5.4	4.4	3.5
	IV	61.6	109.5	145.7	65.9	107.3	106.0	38.2	23.5	-4.2	4.6	2.2
2015	I	61.0	109.7	143.8	67.2	104.1	111.5	39.6	21.3	-6.2	1.0	2.3
	II	63.4	110.2	148.8	69.6	104.9	114.6	40.5	22.8	-6.3	1.2	2.0
	III	64.0	109.1	151.8	69.7	103.9	115.8	40.6	23.4	-5.7	1.2	2.1
	IV	64.0	109.6	151.1	68.0	103.4	113.7	41.0	23.0	-4.1	1.7	1.9
2015	Oct	20.7	110.6	145.5	22.4	103.7	112.1	13.5	7.3	-1.7	0.4	0.8
	Nov	21.5	109.7	152.6	22.9	103.6	114.5	13.7	7.8	-1.4	0.5	0.6
	Dec	21.7	108.5	155.3	22.7	102.8	114.4	13.8	7.9	-1.0	0.8	0.5
Percentage changes (b)									Percentage of GDP			
2008	2.3	1.6	0.7	-0.6	4.1	-4.5	-0.1	8.0	-8.4	-4.5	-2.3	
2009	-15.5	-6.8	-9.4	-27.3	-11.8	-17.5	-15.5	-15.4	-4.3	-1.7	-0.8	
2010	16.8	1.6	15.0	16.5	4.6	11.3	14.3	22.5	-4.9	-1.7	-0.4	
2011	15.2	4.8	10.0	9.6	8.4	1.1	12.7	20.5	-4.5	-0.4	0.3	
2012	5.1	2.0	3.0	-2.0	4.7	-6.3	0.5	14.1	-3.1	1.4	1.2	
2013	4.3	-0.2	4.5	-2.2	-4.3	2.2	3.1	6.3	-1.6	2.5	1.7	
2014	1.8	-1.0	3.0	4.8	-2.4	7.8	3.1	-0.4	-2.4	1.5	1.1	
2015	4.3	0.5	4.6	3.7	-2.4	6.6	6.4	0.5	-2.2	0.3	0.8	
2014	I	-2.3	-8.3	6.5	18.7	-14.0	37.7	5.0	-13.9	-2.6	1.8	1.2
	II	10.1	-1.1	11.1	2.3	4.2	-1.9	1.4	27.1	-2.2	1.6	1.0
	III	12.9	1.5	11.4	9.6	3.8	5.6	14.0	11.0	-2.1	1.7	1.4
	IV	-2.4	1.5	-3.7	-8.6	-1.1	-7.5	-7.5	6.7	-1.6	1.8	0.9
2015	I	-4.2	0.7	-5.1	8.1	-11.4	22.3	16.2	-31.5	-2.3	0.4	0.9
	II	16.7	1.8	14.6	15.5	3.1	11.7	9.5	30.9	-2.3	0.4	0.8
	III	3.9	-3.9	8.3	0.3	-3.8	4.3	0.5	10.0	-2.1	0.5	0.8
	IV	-0.1	1.8	-1.8	-9.0	-1.9	-7.1	4.1	-7.0	-1.5	0.6	0.7
2015	Oct	-3.3	2.3	-5.5	-2.2	0.2	-2.4	-4.0	-2.0	--	--	--
	Nov	4.0	-0.8	4.9	2.1	-0.1	2.1	1.8	8.0	--	--	--
	Dec	0.7	-1.1	1.8	-0.9	-0.8	-0.1	0.9	0.3	--	--	--

(a) Seasonally adjusted, except for annual data. (b) Annualized percent change from the previous quarter for quarterly data, non-annualized percent change from the previous month for monthly data.

Source: Ministry of Economy.

Chart 16.1.- External trade (real)
Percent change from previous period

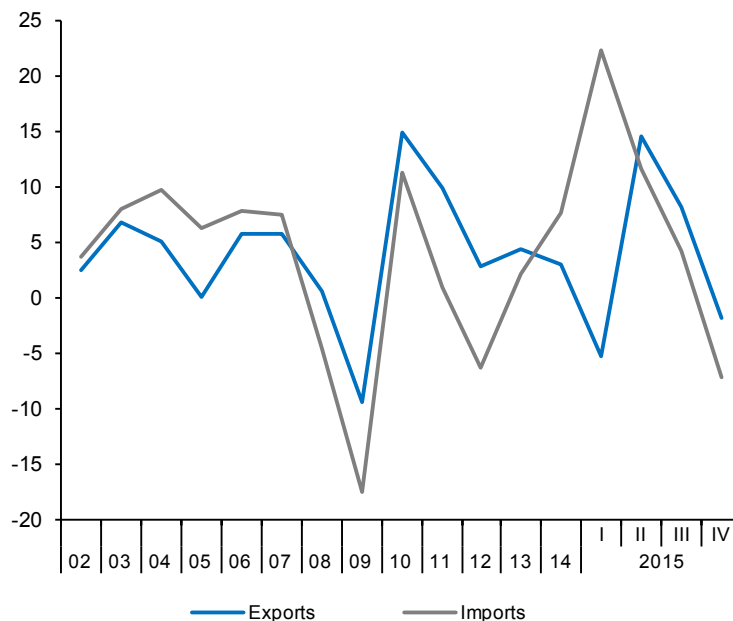


Chart 16.2.- Trade balance
EUR Billions, moving sum of 12 months

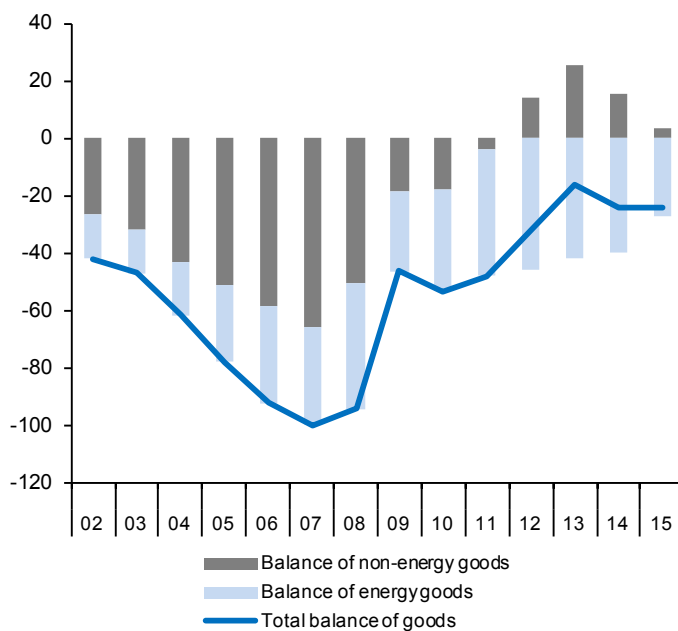


Table 17

Balance of Payments (according to IMF manual)

(Net transactions)

		Current account					Capital account	Current and capital accounts	Financial account						Errors and omissions
		Total	Goods	Services	Income	Transfers			Financial account, excluding Bank of Spain					Bank of Spain	
									Total	Direct investment	Portfolio investment	Other investment	Financial derivatives		
1 = 2 + 3 + 4 + 5		2	3	4	5	6	7=1+6	8 = 9 + 10 + 11 + 12	9	10	11	12	13	14	
EUR billions															
2008		-103.25	-87.04	29.82	-30.49	-15.55	4.67	-98.58	69.23	1.53	-0.96	75.72	-7.07	-30.22	-0.86
2009		-46.19	-41.47	29.54	-19.62	-14.64	3.33	-42.86	40.70	-1.94	44.04	4.66	-6.05	-10.46	-8.31
2010		-42.39	-47.80	33.93	-15.13	-13.38	4.89	-37.49	27.24	1.46	28.40	-11.23	8.61	-15.70	-5.44
2011		-34.04	-44.48	42.59	-18.36	-13.79	4.06	-29.98	-79.51	-9.23	-26.25	-41.96	-2.07	-109.23	0.26
2012		-2.40	-29.25	45.25	-7.01	-11.39	5.18	2.77	-170.51	21.12	-55.40	-144.57	8.35	-168.76	-1.02
2013		15.57	-14.20	47.65	-4.75	-13.14	6.78	22.35	81.94	14.40	34.53	34.05	-1.04	117.08	12.79
2014		10.24	-22.51	48.47	-4.16	-11.56	4.45	14.69	5.56	-9.36	6.10	9.93	-1.11	26.66	6.42
2013	IV	5.40	-4.78	10.15	2.73	-2.70	2.21	7.61	36.95	4.51	35.39	-1.62	-1.33	53.67	9.12
2014	I	-3.26	-5.68	8.47	-1.68	-4.37	1.62	-1.64	-18.80	-5.18	-18.13	5.33	-0.82	-12.49	7.95
	II	0.18	-5.14	12.08	-4.06	-2.70	1.68	1.86	6.79	-0.69	28.64	-22.32	1.16	16.04	7.38
	III	5.22	-6.61	17.11	-3.29	-1.99	0.35	5.57	-4.63	7.62	-33.44	21.41	-0.22	-2.76	-3.70
	IV	8.09	-5.09	10.81	4.87	-2.50	0.81	8.90	22.20	-11.10	29.03	5.51	-1.23	25.87	-5.23
2015	I	-1.41	-4.28	8.51	-1.05	-4.58	0.69	-0.72	-6.37	-0.59	3.36	-9.92	0.77	-14.85	-7.76
	II	3.02	-5.26	12.35	-1.84	-2.22	2.25	5.27	-20.45	-15.10	-4.76	-1.17	0.57	-8.93	6.26
	III	6.10	-7.03	17.20	-2.78	-1.29	1.99	8.10	-9.95	-4.11	-3.22	-2.70	0.08	0.12	1.98
			Goods and Services		Income and Transfers										
2015	Oct	2.39	3.32		-0.93		0.04	2.42	-4.63	1.52	2.59	-8.61	-0.13	5.72	7.93
	Nov	2.11	2.04		0.07		0.11	2.22	-9.80	0.00	-7.41	-2.12	-0.28	-11.66	-4.08
	Dec	4.49	0.53		3.96		0.92	5.41	-19.01	-3.06	8.72	-24.31	-0.36	-10.97	2.63
Percentage of GDP															
2008		-9.5	-8.0	2.7	-2.8	-1.4	0.4	-9.1	6.4	0.1	-0.1	7.0	-0.7	-2.8	-0.1
2009		-4.3	-3.8	2.7	-1.8	-1.4	0.3	-4.0	3.8	-0.2	4.1	0.4	-0.6	-1.0	-0.8
2010		-3.9	-4.4	3.1	-1.4	-1.2	0.5	-3.5	2.5	0.1	2.6	-1.0	0.8	-1.5	-0.5
2011		-3.2	-4.2	4.0	-1.7	-1.3	0.4	-2.8	-7.4	-0.9	-2.5	-3.9	-0.2	-10.2	0.0
2012		-0.2	-2.8	4.3	-0.7	-1.1	0.5	0.3	-16.3	2.0	-5.3	-13.9	0.8	-16.2	-0.1
2013		1.5	-1.4	4.6	-0.5	-1.3	0.7	2.2	7.9	1.4	3.3	3.3	-0.1	11.4	1.2
2014		1.0	-2.2	4.7	-0.4	-1.1	0.4	1.4	0.5	-0.9	0.6	1.0	-0.1	2.6	0.6
2013	IV	2.0	-1.8	3.8	1.0	-1.0	0.8	2.9	13.9	1.7	13.3	-0.6	-0.5	20.2	3.4
2014	I	-1.3	-2.3	3.4	-0.7	-1.7	0.6	-0.7	-7.5	-2.1	-7.3	2.1	-0.3	-5.0	3.2
	II	0.1	-1.9	4.6	-1.5	-1.0	0.6	0.7	2.6	-0.3	10.8	-8.4	0.4	6.1	2.8
	III	2.0	-2.6	6.7	-1.3	-0.8	0.1	2.2	-1.8	3.0	-13.0	8.4	-0.1	-1.1	-1.4
	IV	3.0	-1.9	4.0	1.8	-0.9	0.3	3.3	8.2	-4.1	10.7	2.0	-0.5	9.6	-1.9
2015	I	-0.5	-1.7	3.3	-0.4	-1.8	0.3	-0.3	-2.5	-0.2	1.3	-3.8	0.3	-5.8	-3.0
	II	1.1	-1.9	4.5	-0.7	-0.8	0.8	1.9	-7.4	-5.5	-1.7	-0.4	0.2	-3.2	2.3
	III	2.3	-2.6	6.4	-1.0	-0.5	0.7	3.0	-3.7	-1.5	-1.2	-1.0	0.0	0.0	0.7

Source: Bank of Spain.

Chart 17.1.- Balance of payments: Current and capital accounts
EUR Billions, 12-month cumulated

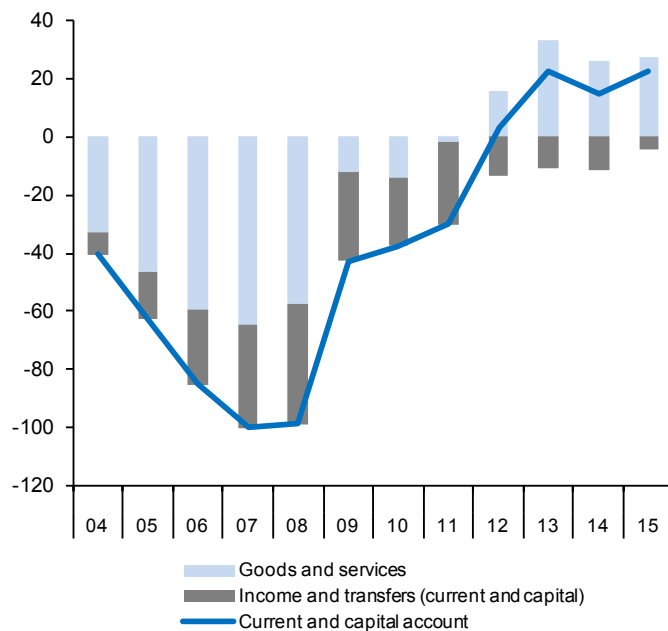


Chart 17.2.- Balance of payments: Financial account
EUR Billions, 12-month cumulated

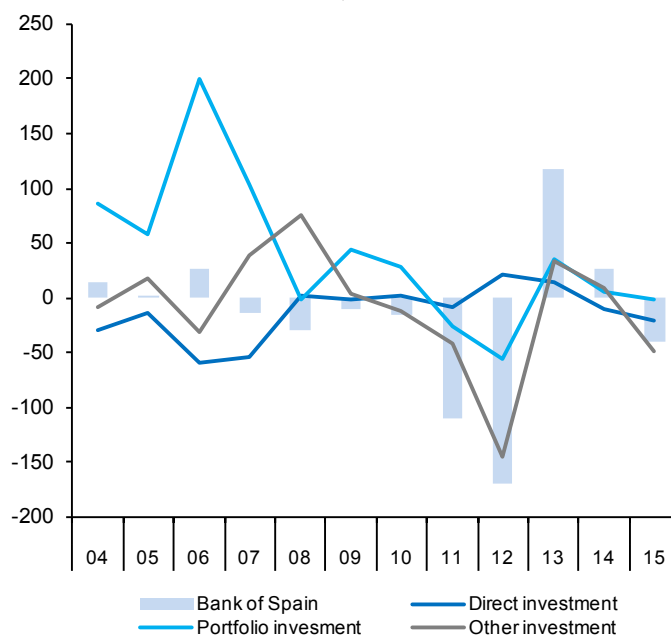


Table 18

State and Social Security System budget

	State							Social Security System (b)					
	National accounts basis			Revenue, cash basis (a)				Surplus or deficit	Accrued income		Expenditure		
	Surplus or deficit	Revenue	Expenditure	Total	Direct taxes	Indirect taxes	Others		Total	of which, social contributions	Total	of which, pensions	
	1=2-3	2	3	4=5+6+7	5	6	7		8=9-11	9	10	11	12
EUR billions, 12-month cumulated													
2009	-99.7	134.0	233.6	162.5	87.5	55.7	19.3	8.8	123.7	107.3	114.9	92.0	
2010	-50.6	161.2	211.8	175.0	86.9	71.9	16.3	2.4	122.5	105.5	120.1	97.7	
2011	-32.0	168.1	200.1	177.0	89.6	71.2	16.1	-0.5	121.7	105.4	122.1	101.5	
2012	-44.1	173.0	217.1	215.4	96.2	71.6	47.7	-5.8	118.6	101.1	124.4	105.5	
2013	-45.4	169.7	215.1	191.1	94.0	73.7	23.3	-8.9	121.3	98.1	130.2	111.1	
2014	-40.2	174.3	214.5	205.9	95.6	78.2	32.1	-14.0	119.3	99.2	133.3	114.4	
2015 (c)	-27.5	163.0	190.5	198.8	89.1	77.9	31.7	-5.8	114.8	92.1	120.6	101.2	
2015	Sep	-33.2	179.7	213.0	218.7	97.9	81.3	39.5	-16.4	122.7	100.0	139.1	116.8
	Oct	-34.0	179.9	213.8	219.9	98.4	81.9	39.6	-16.5	123.0	100.1	139.5	117.1
	Nov	-32.3	181.6	214.0	221.5	98.6	81.8	41.1	-16.3	123.6	100.4	139.9	117.3
Annual percentage changes													
2009	--	-19.3	17.8	-13.9	-14.2	-21.2	20.4	--	-0.5	-1.3	4.7	5.9	
2010	--	20.3	-9.3	7.7	-0.7	29.1	-15.7	--	-1.0	-1.7	4.5	6.2	
2011	--	4.2	-5.6	1.1	3.1	-0.9	-0.8	--	-0.7	-0.1	1.7	3.9	
2012	--	3.0	8.5	21.7	7.3	0.5	195.9	--	-2.5	-4.0	1.9	3.9	
2013	--	-1.9	-0.9	-11.3	-2.2	3.0	-51.1	--	2.3	-3.0	4.6	5.3	
2014	--	2.7	-0.3	7.7	1.6	6.1	37.6	--	-1.6	1.1	2.4	3.0	
2015 (d)	--	4.7	-0.3	8.5	3.6	4.7	39.8	--	3.8	1.3	5.8	3.0	
2015	Sep	--	3.2	-1.5	8.9	2.3	4.8	43.2	--	4.0	1.3	5.3	3.0
	Oct	--	2.9	-0.3	9.4	3.3	4.9	43.2	--	3.2	1.4	5.4	3.0
	Nov	--	4.0	-1.1	9.4	2.8	4.3	46.2	--	3.5	1.5	5.4	3.0
Percentage of GDP, 12-month cumulated													
2009	-9.2	12.4	21.7	15.1	8.1	5.2	1.8	0.8	11.5	9.9	10.6	8.5	
2010	-4.7	14.9	19.6	16.2	8.0	6.7	1.5	0.2	11.3	9.8	11.1	9.0	
2011	-3.0	15.7	18.7	16.5	8.4	6.7	1.5	0.0	11.4	9.8	11.4	9.5	
2012	-4.2	16.6	20.8	20.7	9.2	6.9	4.6	-0.6	11.4	9.7	11.9	10.1	
2013	-4.4	16.5	20.9	18.5	9.1	7.1	2.3	-0.9	11.8	9.5	12.6	10.8	
2014	-3.9	16.7	20.6	19.8	9.2	7.5	3.1	-1.3	11.5	9.5	12.8	11.0	
2015	Sep	-3.1	16.6	19.7	20.2	9.1	7.5	3.7	-1.5	11.3	9.2	12.9	10.8
	Oct	-3.1	16.6	19.8	20.3	9.1	7.6	3.7	-1.5	11.4	9.3	12.9	10.8
	Nov	-3.0	16.8	19.8	20.5	9.1	7.6	3.8	-1.5	11.4	9.3	12.9	10.9

(a) Including the regional and local administrations share in direct and indirect taxes. (b) Not included unemployment benefits and wage guarantee fund. (c) Cumulated since January. (d) Percent change over the same period of the previous year.

Sources: M. of Economy and M. of Labour.

Chart 18.1.- State: Revenue, expenditure and deficit (cash basis)
EUR Billions, 12-month cumulated

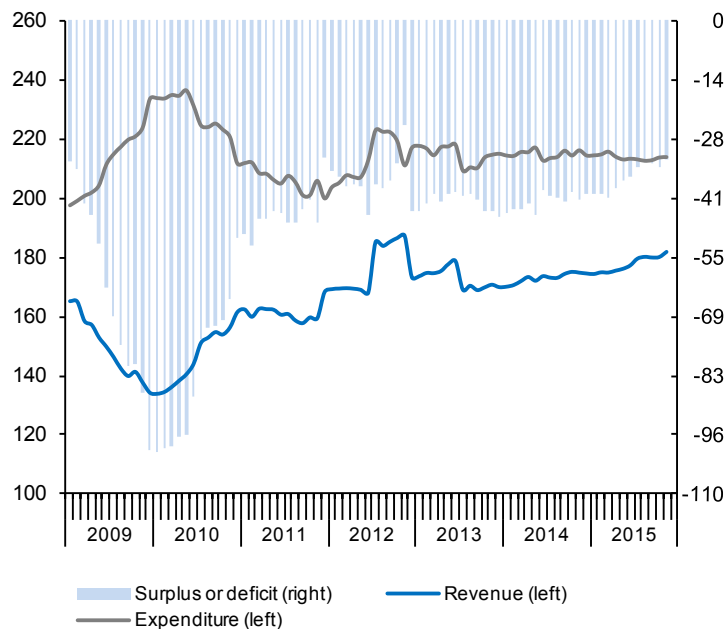


Chart 18.2.- Social Security System: Revenue, expenditure and deficit
EUR Billions, 12-month cumulated

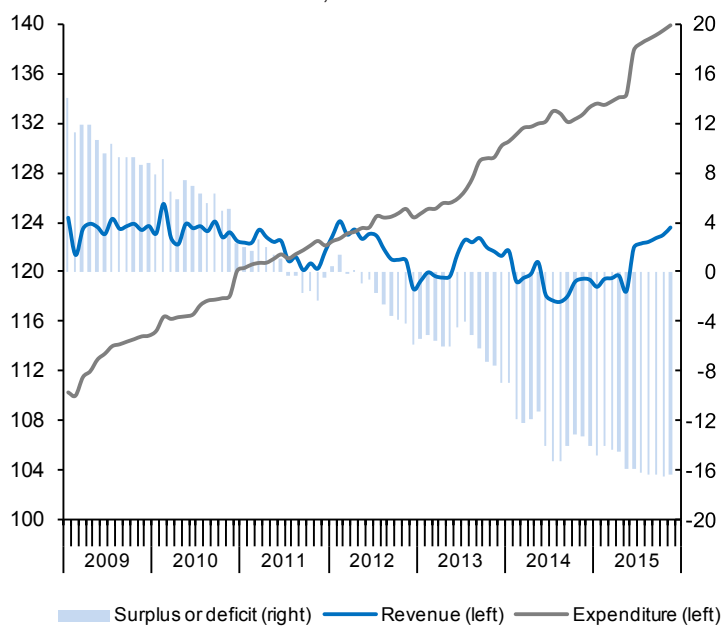


Table 19

Monetary and financial indicators

	Interest rates (percentage rates)					Credit stock (EUR billion)				Contribution of Spanish MFI to Eurozone M3	Stock market (IBEX-35)	
	10 year Bonds	Spread with German Bund (basis points)	Housing credit to households	Consumer credit to households	Credit to non-financial corporations (less than 1 million)	TOTAL	Government	Non-financial corporations	Households			
	Average of period data					End of period data						
2007		4.3	7.3	5.3	9.8	5.8	2,432.2	383.8	1,175.8	872.6	--	15,182.3
2008		4.4	38.3	5.8	10.9	6.4	2,609.0	439.8	1,261.1	908.2	--	9,195.8
2009		4.0	75.7	3.4	10.5	4.7	2,715.6	568.7	1,246.5	900.4	--	11,940.0
2010		4.3	150.8	2.6	8.6	4.3	2,788.5	649.3	1,244.0	895.2	--	9,859.1
2011		5.4	283.3	3.5	8.6	5.1	2,805.5	743.5	1,194.0	867.9	--	8,563.3
2012		5.8	435.1	3.4	9.1	5.6	2,821.3	890.7	1,099.7	830.9	--	8,167.5
2013		4.6	299.2	3.2	9.7	5.5	2,760.0	966.0	1,011.0	783.0	--	9,916.7
2014		2.7	156.0	3.1	9.6	4.9	2,725.1	1,033.7	942.5	748.5	--	10,279.5
2015		1.7	124.0	2.5	9.0	3.8	2,713.5	1,069.9	916.0	724.1	--	9,544.2
2016	(a)	1.7	142.6	2.4	9.0	3.7	2,703.2	1,069.7	911.9	721.6	--	8,461.4
2014	II	2.9	157.0	3.2	9.6	5.1	2,761.2	1,012.5	977.9	770.5	--	10,923.5
	III	2.4	143.7	3.1	9.7	4.8	2,747.6	1,020.1	970.7	756.4	--	10,825.5
	IV	2.0	129.0	2.8	9.5	4.3	2,725.1	1,033.7	942.5	748.5	--	10,279.5
2015	I	1.4	112.3	2.6	9.3	4.2	2,731.6	1,046.1	944.8	740.4	--	11,521.1
	II	1.8	126.0	2.5	8.9	3.7	2,725.5	1,052.5	930.9	741.8	--	10,769.5
	III	2.0	132.5	2.5	9.2	3.7	2,714.8	1,062.3	923.4	728.8	--	9,559.9
	IV	1.7	118.4	2.4	8.7	3.5	2,713.5	1,069.9	916.0	724.1	--	9,544.2
2016	I (a)	1.7	142.6	2.4	9.0	3.7	2,703.2	1,069.7	911.9	721.6	--	8,461.4
2015	Dec	1.7	113.6	2.3	8.4	3.3	2,710.1	1,070.3	916.0	724.1	--	9,544.2
2016	Jan	1.7	129.8	2.4	9.0	3.7	2,703.2	1,069.7	911.9	721.6	--	8,815.8
	Feb	1.7	155.4	--	--	--	--	--	--	--	--	8,461.4
							Percentage change from same period previous year				(b)	
2007		--	--	--	--	--	12.5	-2.1	18.4	12.5	15.1	7.3
2008		--	--	--	--	--	8.0	14.6	8.5	4.3	7.7	-39.4
2009		--	--	--	--	--	4.1	29.3	-1.4	-0.3	-0.8	29.8
2010		--	--	--	--	--	3.4	14.2	0.7	0.2	-2.2	-17.4
2011		--	--	--	--	--	1.7	14.5	-2.0	-2.4	-1.6	-13.1
2012		--	--	--	--	--	1.3	19.8	-6.4	-3.8	0.1	-4.6
2013		--	--	--	--	--	-1.1	8.5	-5.9	-5.1	-4.4	21.4
2014		--	--	--	--	--	-0.2	7.0	-4.4	-3.6	3.4	3.7
2015		--	--	--	--	--	0.4	3.5	-1.0	-2.3	5.3	-7.2
2016	(a)	--	--	--	--	--	0.2	3.3	-1.2	-2.2	7.5	-11.3
2014	II	--	--	--	--	--	-1.0	6.6	-5.3	-4.4	-1.5	5.6
	III	--	--	--	--	--	-0.8	6.2	-4.7	-4.1	0.5	-0.9
	IV	--	--	--	--	--	-0.2	7.0	-4.4	-3.6	3.4	-5.0
2015	I	--	--	--	--	--	0.0	5.1	-2.5	-3.2	4.5	12.1
	II	--	--	--	--	--	-0.2	4.0	-2.6	-2.7	3.6	-6.5
	III	--	--	--	--	--	-0.1	4.2	-2.7	-2.6	4.6	-11.2
	IV	--	--	--	--	--	0.4	3.5	-1.0	-2.3	5.3	-0.2
2016	I (a)	--	--	--	--	--	0.2	3.3	-1.2	-2.2	7.5	-11.3
2015	Dec	--	--	--	--	--	0.4	3.5	-1.0	-2.3	5.3	-8.1
2016	Jan	--	--	--	--	--	0.2	3.3	-1.2	-2.2	7.5	-7.6
	Feb	--	--	--	--	--	--	--	--	--	--	-4.0

(a) Period with available data. (b) Percent change from preceeding period.

Source: Bank of Spain.

Chart 19.1.- 10 year bond yield
Percentage rates and basis points

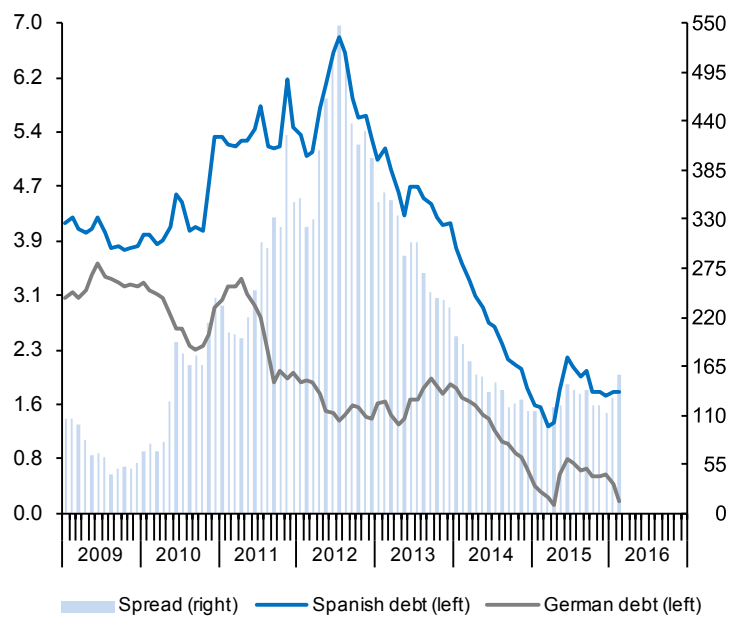


Chart 19.2.- Credit stock growth
Annual percentage change

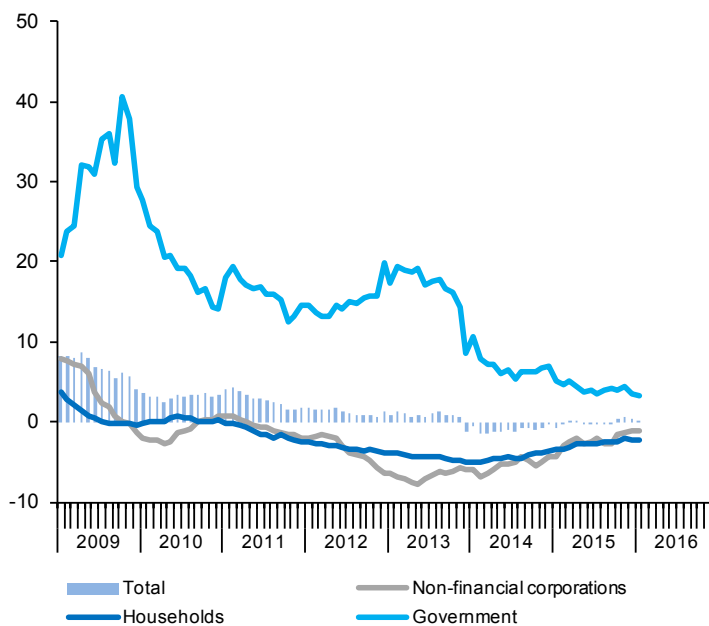


Table 20

Competitiveness indicators in relation to EMU

	Relative Unit Labour Costs in industry (Spain/EMU)			Harmonized Consumer Prices			Producer prices			Real Effective Exchange Rate in relation to developed countries
	Relative productivity	Relative wages	Relative ULC	Spain	EMU	Spain/EMU	Spain	EMU	Spain/EMU	
	1998=100			2015=100			2010=100			1999 I =100
2009	107.6	96.8	111.1	92.2	91.8	100.4	96.2	97.0	99.2	114.0
2010	106.1	89.8	118.2	94.1	93.3	100.9	100.0	100.0	100.0	112.8
2011	105.3	87.8	119.8	96.9	95.8	101.2	106.5	105.2	101.2	113.1
2012	102.7	88.2	116.5	99.3	98.2	101.1	110.1	107.9	102.0	111.6
2013	101.0	89.3	113.1	100.8	99.5	101.3	110.0	107.4	102.4	113.4
2014	100.5	90.3	111.4	100.6	99.8	100.8	108.4	105.8	102.4	112.4
2015	--	--	--	100.0	100.0	100.0	106.8	104.0	102.7	109.0
2016 (a)	--	--	--	97.4	98.8	98.6	102.5	101.3	101.2	107.8
2014 I	--	--	--	99.9	99.5	100.4	108.0	106.5	101.4	112.6
II	--	--	--	101.5	100.3	101.2	108.6	106.1	102.4	113.3
III	--	--	--	100.3	100.0	100.4	109.3	106.1	103.0	111.7
IV	--	--	--	100.7	100.1	100.7	107.7	105.3	102.3	111.8
2015 I	--	--	--	98.8	99.2	99.6	106.6	104.2	102.3	108.7
II	--	--	--	101.2	100.5	100.6	108.0	104.9	102.9	109.6
III	--	--	--	99.8	100.0	99.7	107.3	104.0	103.2	108.6
IV	--	--	--	100.3	100.2	100.0	105.2	102.8	102.4	109.0
2016 (a)	--	--	--	97.4	98.8	98.6	102.5	101.3	101.2	107.8
2015 Dec	--	--	--	100.1	100.2	99.9	104.7	102.1	102.5	108.8
2016 Jan	--	--	--	97.6	98.7	98.9	102.5	101.3	101.2	107.8
Feb	--	--	--	97.2	98.9	98.3	--	--	--	--
Annual percentage changes						Differential	Annual percentage changes		Differential	Annual
2009	-2.4	7.1	-8.9	-0.2	0.3	-0.5	-3.3	-4.5	1.2	-0.4
2010	-1.4	-7.2	6.3	2.0	1.6	0.4	3.9	3.1	0.9	-1.0
2011	-0.8	-2.2	1.4	3.0	2.7	0.3	6.5	5.2	1.3	0.2
2012	-2.4	0.4	-2.8	2.4	2.5	-0.1	3.4	2.6	0.8	-1.3
2013	-1.6	1.3	-2.9	1.5	1.3	0.2	-0.1	-0.4	0.4	1.5
2014	-0.5	1.0	-1.5	-0.2	0.3	-0.5	-1.5	-1.5	0.0	-0.9
2015	--	--	--	-0.6	0.2	-0.8	-1.5	-1.7	0.3	-3.0
2016 (b)	--	--	--	-0.7	0.1	-0.8	-3.7	-2.6	-1.1	-1.3
2014 I	--	--	--	0.0	0.7	-0.6	-2.6	-1.5	-1.1	-0.1
II	--	--	--	0.2	0.6	-0.4	-0.6	-1.1	0.5	-0.2
III	--	--	--	-0.4	0.4	-0.7	-0.9	-1.2	0.3	-1.3
IV	--	--	--	-0.6	0.2	-0.8	-1.7	-1.5	-0.2	-1.9
2015 I	--	--	--	-1.1	-0.3	-0.8	-1.3	-2.1	0.9	-3.4
II	--	--	--	-0.3	0.2	-0.5	-0.6	-1.1	0.5	-3.3
III	--	--	--	-0.6	0.1	-0.7	-1.8	-1.9	0.2	-2.8
IV	--	--	--	-0.5	0.2	-0.6	-2.3	-2.4	0.1	-2.6
2016 (b)	--	--	--	-1.4	-0.4	-1.0	-3.9	-2.8	-1.1	-0.8
2015 Dec	--	--	--	-0.1	0.2	-0.4	-1.9	-2.3	0.4	-2.3
2016 Jan	--	--	--	-0.4	0.3	-0.7	-3.6	-2.2	-1.3	-1.3
Feb	--	--	--	-1.0	-0.2	-0.8	--	--	--	--

(a) Period with available data. (b) Growth of available period over the same period of the previous year.

Sources: Eurostat, Bank of Spain and Funcas.

Chart 20.1.- Relative Unit Labour Costs in industry (Spain/EMU)
1998=100

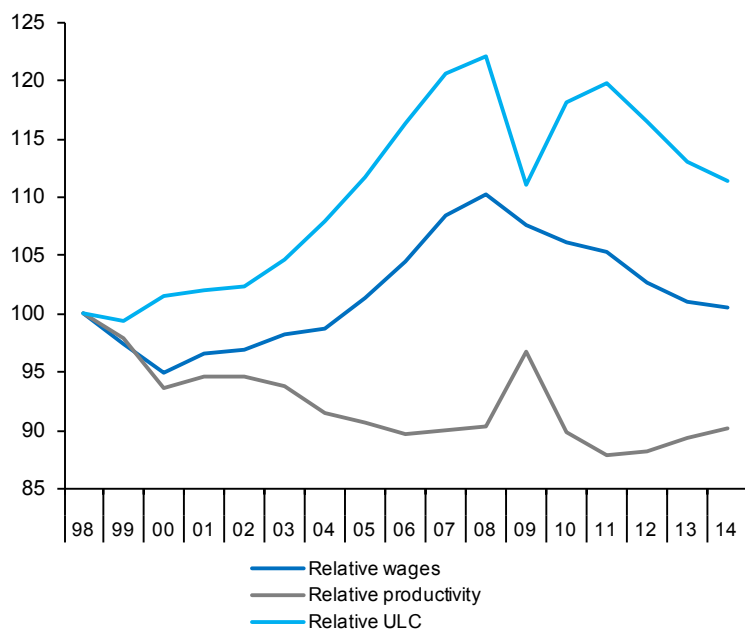


Chart 20.2.- Harmonized Consumer Prices
Annual growth in % and percentage points

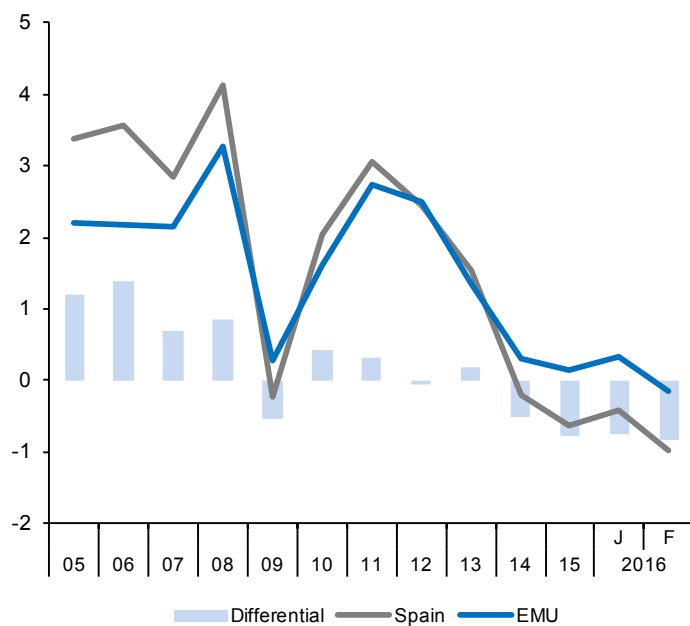


Table 21a

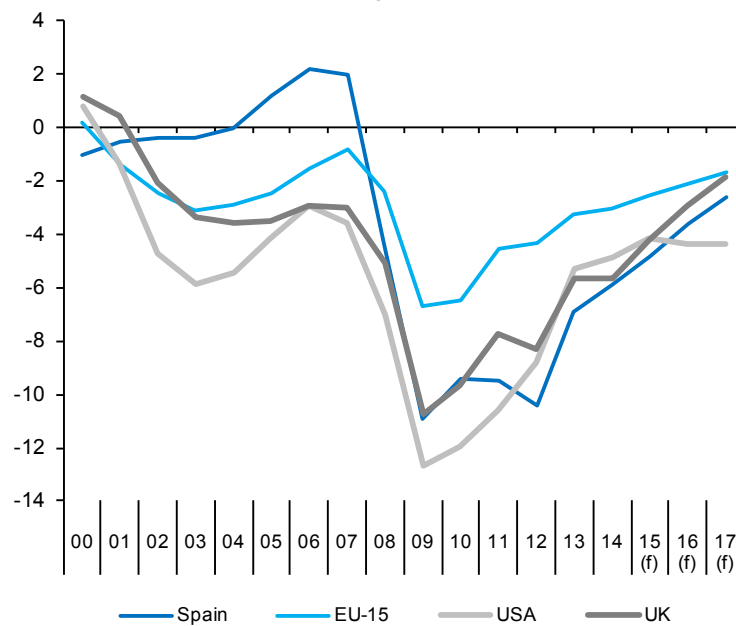
Imbalances: International comparison (I)

In blue: European Commission Forecasts

	Government net lending (+) or borrowing (-)				Government gross debt				Current Account Balance of Payments (National Accounts)			
	Spain	EU-15	USA	UK	Spain	EU-15	USA	UK	Spain	EU-15	USA	UK
Billions of national currency												
2005	11.2	-269.5	-542.8	-47.0	393.5	6844.8	8,496.5	552.0	-70.3	44.5	-737.7	-16.6
2006	22.1	-171.7	-410.6	-40.9	392.2	7,057.1	8,817.8	597.1	-90.7	27.8	-802.2	-32.3
2007	21.6	-100.5	-512.5	-44.4	383.8	7,135.0	9,267.3	646.2	-104.1	26.1	-718.1	-37.3
2008	-49.4	-285.2	-1,030.1	-76.9	439.8	7,572.7	10,720.2	786.3	-102.9	-80.2	-691.6	-55.2
2009	-118.2	-756.9	-1,824.2	-160.0	568.7	8,532.0	12,405.1	975.5	-46.5	14.0	-381.9	-45.2
2010	-101.4	-760.1	-1,793.9	-150.8	649.3	9,580.5	14,175.8	1,190.9	-42.0	33.8	-445.9	-43.5
2011	-101.3	-547.1	-1,644.6	-124.8	743.5	10,258.9	15,362.2	1,324.2	-35.3	72.5	-481.5	-27.4
2012	-108.9	-536.1	-1,424.2	-138.5	890.7	10,893.7	16,557.3	1,421.1	-4.6	160.5	-468.2	-54.7
2013	-71.2	-409.5	-881.9	-98.5	966.0	11,242.5	17,459.9	1,496.2	15.2	197.3	-395.8	-77.9
2014	-61.3	-385.9	-842.2	-103.0	1,033.7	11,788.4	18,178.6	1,602.4	10.3	228.9	-401.1	-92.9
2015	-52.4	-339.8	-750.7	-78.9	1,089.4	12,158.9	18,960.5	1,658.1	16.6	299.5	-592.5	-93.6
2016	-40.7	-292.6	-814.4	-56.4	1,135.8	12,402.4	19,924.9	1,721.5	16.2	312.0	-583.7	-91.7
2017	-30.1	-236.4	-859.0	-37.9	1,165.9	12,660.9	20,934.0	1,774.8	15.4	307.9	-634.7	-87.2
Percentage of GDP												
2005	1.2	-2.5	-4.1	-3.5	42.3	63.4	64.9	41.5	-7.6	0.4	-5.6	-1.2
2006	2.2	-1.5	-3.0	-2.9	38.9	62.0	63.6	42.4	-9.0	0.2	-5.8	-2.3
2007	2.0	-0.8	-3.5	-3.0	35.5	59.6	64.0	43.5	-9.6	0.2	-5.0	-2.5
2008	-4.4	-2.4	-7.0	-5.1	39.4	63.5	72.8	51.7	-9.2	-0.7	-4.7	-3.6
2009	-11.0	-6.7	-12.7	-10.8	52.7	75.4	86.0	65.7	-4.3	0.1	-2.6	-3.0
2010	-9.4	-6.5	-12.0	-9.7	60.1	81.3	94.7	76.6	-3.9	0.3	-3.0	-2.8
2011	-9.5	-4.5	-10.6	-7.7	69.5	84.7	99.0	81.8	-3.3	0.6	-3.1	-1.7
2012	-10.4	-4.3	-8.8	-8.3	85.4	88.2	102.5	85.3	-0.4	1.3	-2.9	-3.3
2013	-6.9	-3.3	-5.3	-5.7	93.7	90.3	104.8	86.2	1.5	1.6	-2.4	-4.5
2014	-5.9	-3.0	-4.9	-5.7	99.3	91.8	104.8	88.2	1.0	1.8	-2.3	-5.1
2015	-4.8	-2.5	-4.2	-4.2	100.7	90.4	105.6	88.6	1.5	2.2	-3.3	-5.0
2016	-3.6	-2.1	-4.3	-2.9	101.2	89.9	106.3	89.1	1.4	2.3	-3.1	-4.7
2017	-2.6	-1.7	-4.4	-1.9	100.1	88.7	106.4	88.2	1.3	2.2	-3.2	-4.3

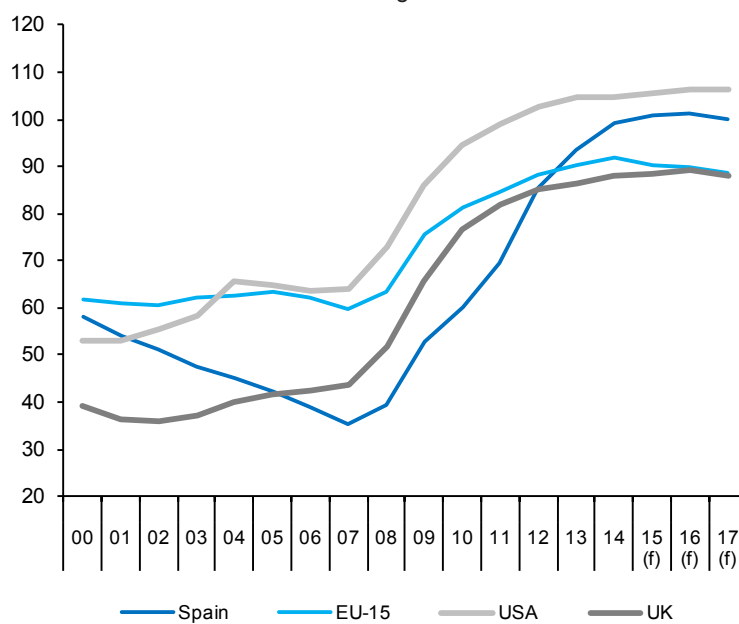
Source: European Commission.

Chart 21a.1.- Government deficit
Percentage of GDP



(f) European Commission forecast.

Chart 21a.2.- Government gross debt
Percentage of GDP



(f) European Commission forecast.

Table 21b

Imbalances: International comparison (II)

	Household debt (a)				Non-financial corporations debt (a)				Financial corporations debt (a)			
	Spain	EMU-19	USA	UK	Spain	EMU-19	USA	UK	Spain	EMU-19	USA	UK
Billions of national currency												
2005	653.5	4,710.5	11,953.6	1,189.8	925.0	7,668.9	8,166.4	1,121.7	541.5	8,325.8	13,721.0	2,381.7
2006	780.7	5,117.6	13,238.1	1,310.9	1,158.8	8,312.1	8,990.7	1,219.6	771.2	9,212.2	15,124.7	2,619.8
2007	876.6	5,483.4	14,156.6	1,426.4	1,344.5	9,131.2	10,111.4	1,299.9	1,000.0	10,426.3	17,303.5	3,125.7
2008	914.0	5,746.0	14,015.0	1,477.0	1,422.6	9,780.8	10,687.1	1,500.7	1,068.0	11,435.1	18,003.2	3,614.5
2009	906.2	5,888.2	13,762.5	1,473.8	1,406.1	9,722.7	10,136.2	1,434.2	1,147.5	11,924.4	16,537.3	3,593.5
2010	902.5	6,023.1	13,508.6	1,476.9	1,429.4	10,006.8	9,964.0	1,401.7	1,141.4	12,120.3	15,297.6	3,728.5
2011	875.2	6,121.0	13,296.6	1,486.7	1,415.7	10,191.3	10,254.4	1,423.8	1,153.8	12,702.9	14,901.6	3,645.7
2012	838.2	6,202.5	13,354.7	1,509.2	1,310.4	10,331.0	10,781.2	1,486.9	1,182.1	13,075.1	14,700.1	3,707.4
2013	790.8	6,149.7	13,502.0	1,525.5	1,235.3	10,264.5	11,304.7	1,374.8	992.9	12,235.3	14,907.9	3,586.3
2014	754.0	6,185.5	13,875.4	1,567.0	1,167.7	10,624.1	12,004.7	1,396.9	922.9	12,675.7	15,231.9	3,672.1
2015 Q3(b)	734.2	6,182.2	14,101.5	1,574.6	1,147.2	10,903.9	12,621.4	1,371.2	872.7	12,649.0	15,348.5	3,649.3
Percentage of GDP												
2005	70.2	55.7	91.3	89.4	99.4	90.6	62.4	84.3	58.2	98.4	104.8	179.0
2006	77.5	57.5	95.5	93.2	115.0	93.3	64.9	86.7	76.5	103.5	109.2	186.2
2007	81.1	58.3	97.8	96.1	124.4	97.1	69.8	87.6	92.5	110.9	119.5	210.6
2008	81.9	59.6	95.2	97.2	127.5	101.5	72.6	98.8	95.7	118.7	122.3	237.9
2009	84.0	63.4	95.4	99.2	130.3	104.7	70.3	96.5	106.3	128.4	114.7	241.9
2010	83.5	63.1	90.3	94.9	132.2	104.8	66.6	90.1	105.6	127.0	102.2	239.7
2011	81.8	62.5	85.7	91.8	132.3	104.0	66.1	87.9	107.8	129.6	96.0	225.1
2012	80.4	63.1	82.7	90.6	125.6	105.0	66.7	89.3	113.4	132.9	91.0	222.6
2013	76.7	61.9	81.0	87.9	119.8	103.3	67.8	79.2	96.3	123.2	89.5	206.7
2014	72.4	61.2	80.0	86.3	112.2	105.1	69.2	76.9	88.6	125.4	87.8	202.2
2015 Q3(b)	67.9	59.6	78.4	83.5	106.1	105.1	70.2	72.7	80.7	121.9	85.4	193.5

(a) Loans and securities other than shares, excluding financial derivatives. (b) EMU-19 and United Kingdom: First quarter 2015.

Sources: Eurostat, European Central Bank and Federal Reserve.

Chart 21b.1.- Household debt
Percentage of GDP

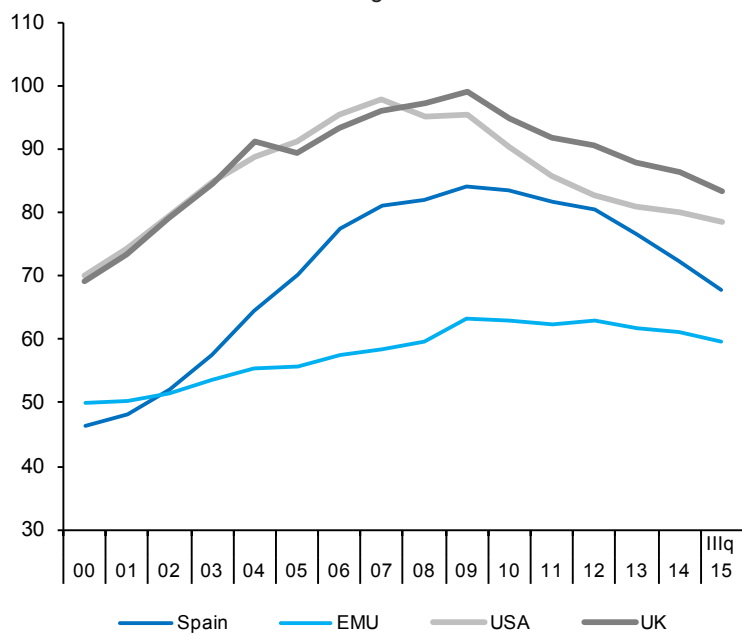
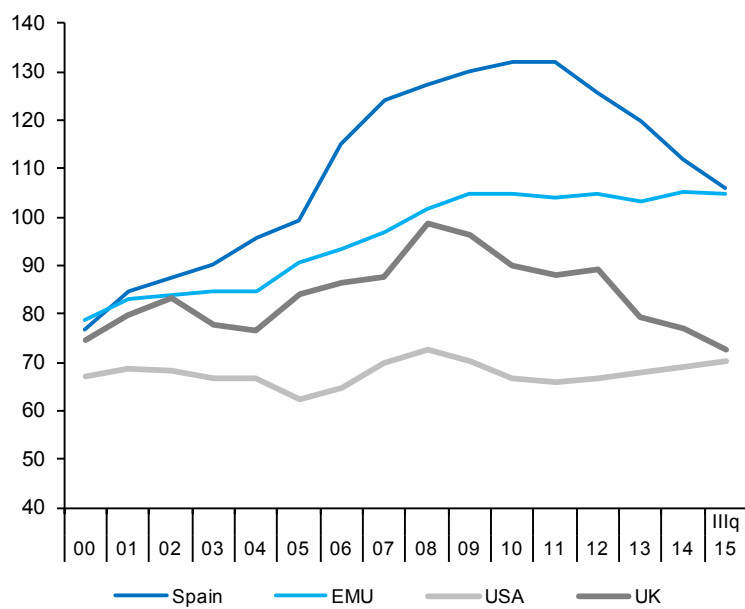


Chart 21b.2.- Non-financial corporations debt
Percentage of GDP



KEY FACTS: 50 FINANCIAL SYSTEM INDICATORS – FUNCAS

Updated: March 15th, 2016

Highlights

Indicator	Last value available	Corresponding to:
Bank lending to other resident sectors (monthly average % var.)	-1.2	December 2015
Other resident sectors' deposits in credit institutions (monthly average % var.)	0.7	December 2015
Doubtful loans (monthly % var.)	-3.1	December 2015
Recourse to the Eurosystem (Eurozone financial institutions, million euros)	303,418	February 2016
Recourse to the Eurosystem (Spanish financial institutions, million euros)	132,395	February 2016
Recourse to the Eurosystem (Spanish financial institutions million euros)- Main L/T refinancing operations	7,173	February 2016
Operating expenses/gross operating income ratio (%)	49.02	September 2015
Customer deposits/employees ratio (thousand euros)	6,174.30	September 2015
Customer deposits/branches ratio (thousand euros)	40,263.86	September 2015
Branches/institutions ratio	144.33	September 2015

A. Money and interest rates

Indicator	Source:	Average 2000-2013	2014	2015	2016 February	2016 March	Definition and calculation
1. Monetary Supply (% chg.)	ECB	5.6	3.8	4.7	-	-	M3 aggregate change (non-stationary)
2. Three-month interbank interest rate	Bank of Spain	2.49	0.21	-0.02	-0.20	-0.23	Daily data average
3. One-year Euribor interest rate (from 1994)	Bank of Spain	2.76	0.48	0.17	-0.02	-0.02	End-of-month data
4. Ten-year Treasury bonds interest rate (from 1998)	Bank of Spain	4.6	2.7	1.7	1.5	1.5	Market interest rate (not exclusively between account holders)
5. Corporate bonds average interest rate	Bank of Spain	4.5	2.3	2.2	1.95	-	End-of-month straight bonds average interest rate (> 2 years) in the AIAF market

Comment on "Money and Interest Rates:" The 3-month interbank rate has fallen to -0.23% and the 1-year Euribor remains at -0.02% in the first fortnight of March. The ECB has announced new expansionary monetary policy measures, including a cut on interest rates and a wider asset purchase program. As for the Spanish 10-year bond yield, it has remained at 1.5%.

B. Financial markets

Indicator	Source:	Average 1999-2012	2013	2014	2015 December	2016 January	Definition and calculation
6. Outright spot treasury bills transactions trade ratio	Bank of Spain	29.6	82.9	75.6	81.37	78.43	(Traded amount/ outstanding balance) x100 in the market (not exclusively between account holders)
7. Outright spot government bonds transactions trade ratio	Bank of Spain	78.9	61.2	73.2	50.15	56.82	(Traded amount/ outstanding balance) x100 in the market (not exclusively between account holders)
8. Outright forward treasury bills transactions trade ratio	Bank of Spain	0.7	1.8	2.6	0.46	0.40	(Traded amount/ outstanding balance) x100 in the market (not exclusively between account holders)
9. Outright forward government bonds transactions trade ratio	Bank of Spain	4.4	3.2	4.6	1.67	1.14	(Traded amount/ outstanding balance) in the market (not exclusively between account holders)
10. Three-month maturity treasury bills interest rate	Bank of Spain	2.4	0.2	0.1	0.1	0.1	Outright transactions in the market (not exclusively between account holders)
11. Government bonds yield index (Dec1987=100)	Bank of Spain	565.2	846.3	1,037.9	1,058.2	1,070.1	Outright transactions in the market (not exclusively between account holders)
12. Madrid Stock Exchange Capitalization (monthly average % chg.)	Bank of Spain and Madrid Stock Exchange	0.4	2.3	0.6	-6.7	-7.2	Change in the total number of resident companies
13. Stock market trading volume. Stock trading volume (monthly average % var.)	Bank of Spain and Madrid Stock Exchange	4.2	6.9	7.0	-3.8	9.9	Stock market trading volume. Stock trading volume: change in total trading volume
14. Madrid Stock Exchange general index (Dec1985=100)	Bank of Spain and Madrid Stock Exchange	1,026.5	1,012.0	1,042.5	965.13	909.17 ^(a)	Base 1985=100
15. Ibex-35 (Dec1989=3000)	Bank of Spain and Madrid Stock Exchange	9,864.5	8,715.6	10,528.8	9,544.2	8,988.3 ^(a)	Base dec1989=3000
16. Madrid Stock Exchange PER ratio (share value/ profitability)	Bank of Spain and Madrid Stock Exchange	15.6	33.1	26.1	15.41	33.4 ^(a)	Madrid Stock Exchange Ratio "share value/ capital profitability"

B. Financial markets (continued)

Indicator	Source:	Average 1999-2012	2013	2014	2015 December	2016 January	Definition and calculation
17. Long-term bonds. Stock trading volume (% chg.)	Bank of Spain and Madrid Stock Exchange	3.7	10.6	7.4	-87.5	61.5	Variation for all stocks
18. Commercial paper. Trading balance (% chg.)	Bank of Spain and AIAF	2.3	10.9	-1.3	2.0	-1.1	AIAF fixed-income market
19. Commercial paper. Three-month interest rate	Bank of Spain and AIAF	2.8	2.4	0.6	0.2	0.3	AIAF fixed-income market
20. IBEX-35 financial futures concluded transactions (% chg.)	Bank of Spain	0.7	6.4	4.3	9.6	9.4	IBEX-35 shares concluded transactions
21. IBEX-35 financial options concluded transactions (% chg.)	Bank of Spain	9.0	6.7	6.4	122.2	-38.4	IBEX-35 shares concluded transactions

(a) Last data published: March 15th, 2016

Comment on "Financial Markets:": During January, there was a decrease in transactions with outright spot T-bills and an increase in spot government bonds transactions, which stood at 78.4% and 56.8%, respectively. The stock market keeps on falling, with the IBEX-35 down to 8,988 points, and the General Index of the Madrid Stock Exchange to 909. Additionally, there was an increase of 9.4% in financial IBEX-35 futures transactions and a fall of 38.4% in transactions with IBEX-35 financial options.

C. Financial Savings and Debt

Indicator	Source:	Average 2007-2012	2013	2014	2015 Q 2	2015 Q 3	Definition and calculation
22. Net Financial Savings/GDP (National Economy)	Bank of Spain	-5.3	2.1	1.0	1.6	2.1	Difference between financial assets and financial liabilities flows over GDP
23. Net Financial Savings/GDP (Households and non-profit institutions)	Bank of Spain	0.7	3.7	3.1	3.5	3.3	Difference between financial assets and financial liabilities flows over GDP
24. Debt in securities (other than shares) and loans/GDP (National Economy)	Bank of Spain	276.4	315.4	319.1	306.7	305.2	Public debt, non-financial companies debt and households and non-profit institutions debt over GDP

C. Financial Savings and Debt (continued)

Indicator	Source:	Average 2007-2012	2013	2014	2015 Q 2	2015 Q 3	Definition and calculation
25. Debt in securities (other than shares) and loans/GDP (Households and non-profit institutions)	Bank of Spain	82.1	76.7	72.4	70.6	68.6	Households and non-profit institutions debt over GDP
26. Households and non-profit institutions balance: financial assets (quarterly average % chg.)	Bank of Spain	1.9	6.8	4.8	0.2	-1.8	Total assets percentage change (financial balance)
27. Households and non-profit institutions balance: financial liabilities (quarterly average % chg.)	Bank of Spain	3.5	-5.3	-3.8	0.1	-1.6	Total liabilities percentage change (financial balance)

Comment on "Financial Savings and Debt:" During 2015Q3, there was an increase in financial savings to GDP in the overall economy that reached 2.1% of GDP. There was a fall in the financial savings rate of households from 3.5% in 2015Q2 to 3.3% in 2015Q3. The debt to GDP ratio fell from 70.6% to 68.6% in the same period. Finally, the stock of financial assets on households' balance sheets registered a fall of 1.8%, and there was also a 1.6% decrease in the stock of financial liabilities.

D. Credit institutions. Business Development

Indicator	Source:	Average 1999-2012	2013	2014	2015 November	2015 December	Definition and calculation
28. Bank lending to other resident sectors (monthly average % var.)	Bank of Spain	10.8	-9.5	-4.6	0.5	-1.2	Lending to the private sector percentage change for the sum of banks, savings banks and credit unions
29. Other resident sectors' deposits in credit institutions (monthly average % var.)	Bank of Spain	9.9	1.3	-1.5	0.1	0.7	Deposits percentage change for the sum of banks, savings banks and credit unions
30. Debt securities (monthly average % var.)	Bank of Spain	11.3	-5.1	1.2	-1.1	-5.3	Asset-side debt securities percentage change for the sum of banks, savings banks and credit unions
31. Shares and equity (monthly average % var.)	Bank of Spain	15.5	8.9	-6.8	0.5	-0.6	Asset-side equity and shares percentage change for the sum of banks, savings banks and credit unions
32. Credit institutions. Net position (difference between assets from credit institutions and liabilities with credit institutions) (% of total assets)	Bank of Spain	-1.3	-5.9	-5.9	-5.5	-5.2	Difference between the asset-side and liability-side "Credit System" item as a proxy of the net position in the interbank market (month-end)

D. Credit institutions. Business Development (continued)

Indicator	Source:	Average 1999-2012	2013	2014	2015 November	2015 December	Definition and calculation
33. Doubtful loans (monthly average % var.)	Bank of Spain	37.9	17.8	-12.7	-1.5	-3.1	Doubtful loans. Percentage change for the sum of banks, savings banks and credit unions.
34. Assets sold under repurchase (monthly average % var.)	Bank of Spain	-2.1	6.5	-6.1	3.9	-1.8	Liability-side assets sold under repurchase. Percentage change for the sum of banks, savings banks and credit unions.
35. Equity capital (monthly average % var.)	Bank of Spain	10.1	19.6	-1.1	0.5	-1.1	Equity percentage change for the sum of banks, savings banks and credit unions.

Comment on "Credit institutions. Business Development:" The latest available data as of December 2015 show a decrease in bank credit to the private sector of 1.2%. Data also show an increase in financial institutions deposit-taking from the previous month of 0.7%. Holdings of debt securities decreased by 5.3%, while shares and equity fell 0.6%. Also, doubtful loans decreased 3.1% compared to the previous month.

E. Credit institutions. Market Structure and Eurosystem Refinancing

Indicator	Source:	Average 2000-2012	2013	2014	2015 June	2015 September	Definition and calculation
36. Number of Spanish credit institutions	Bank of Spain	206	155	138	133	135	Total number of banks, savings banks and credit unions operating in Spanish territory
37. Number of foreign credit institutions operating in Spain	Bank of Spain	64	86	86	83	81	Total number of foreign credit institutions operating in Spanish territory
38. Number of employees	Bank of Spain	249,001	212,998	203,305	-	-	Total number of employees in the banking sector
39. Number of branches	Bank of Spain	40,630	33,527	31,999	31,412	31,176	Total number of branches in the banking sector
40. Recourse to the Eurosystem (total Eurozone financial institutions) (Euro millions)	Bank of Spain	373,328	665,849	506,285	411,245	303,418 ^(a)	Open market operations and ECB standing facilities. Eurozone total
41. Recourse to the Eurosystem (total Spanish financial institutions) (Euro millions)	Bank of Spain	41,806	201,865	141,338	132,123	132,395 ^(a)	Open market operations and ECB standing facilities. Spain total

E. Credit institutions. Market Structure and Eurosystem Refinancing (continued)

Indicator	Source:	Average 2000-2012	2013	2014	2015 June	2015 September	Definition and calculation
42. Recourse to the Eurosystem (total Spanish financial institutions): main long term refinancing operations (Euro millions)	Bank of Spain	21,288	19,833	21,115	27,164	7,173 ^(a)	Open market operations: main long term refinancing operations. Spain total

(a) Last data published: February 2016.

Comment on "Credit institutions. Market Structure and Eurosystem Refinancing:" In February 2016, recourse to Eurosystem funding by Spanish credit institutions accounted for 43.6% of net total funds borrowed from the ECB by the Eurozone. There has been a 1.96 billion euro decrease in the recourse to the Eurosystem by Spanish banks from January.

F. Credit institutions. Efficiency and Productivity, Risk and Profitability

Indicator	Source:	Average 2000-2012	2013	2014	2015 June	2015 September	Definition and calculation
43. "Operating expenses/gross operating income" of Spain ratio	Bank of Spain	52.27	48.25	47.27	48.47	49.02	Operational efficiency indicator. Numerator and denominator are obtained directly from credit institutions' P&L accounts
44. "Customer deposits/employees" ratio (Euro thousands)	Bank of Spain	2,899.17	5,426.09	5,892.09	5,615.85	6,174.30	Productivity indicator (business by employee)
45. "Customer deposits/branches" ratio (Euro thousands)	Bank of Spain	20,102.13	34,472.09	40,119.97	36,139.85	40,263.86	Productivity indicator (business by branch)
46. "Branches/institutions" ratio	Bank of Spain	199.04	216.30	142.85	146.26	144.33	Network expansion indicator
47. "Employees/branches" ratio	Bank of Spain	6.1	6.3	6.8	6.47	6.52	Branch size indicator
48. Equity capital (monthly average % var.)	Bank of Spain	0.12	0.16	0.07	0.17	0.26	Credit institutions equity capital variation indicator
49. ROA	Bank of Spain	0.75	0.13	0.49	0.47	0.47	Profitability indicator, defined as the "pre-tax profit/average total assets"
50. ROE	Bank of Spain	11.20	1.88	6.46	5.93	5.91	Profitability indicator, defined as the "pre-tax profit/equity capital"

Comment on "Credit institutions. Efficiency and Productivity, Risk and Profitability:" In September 2015, most of the profitability and efficiency indicators improved for Spanish banks. Productivity indicators have also improved since the restructuring process of the Spanish banking sector was implemented.

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