

Recent Developments in the Spanish Economy & Funding Outlook

3 October, 2018

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Highlights

- ▶ Spain is in a sustained, competitive growth phase
 - ❑ Improved export competitiveness.
 - ❑ Sounder financial sector fosters efficient resource reallocation.
 - ❑ Labour-intensive, growth better diversified between internal and external demand.

- ▶ National deleveraging is progressing, enabled by solid and balanced growth with current account surplus.

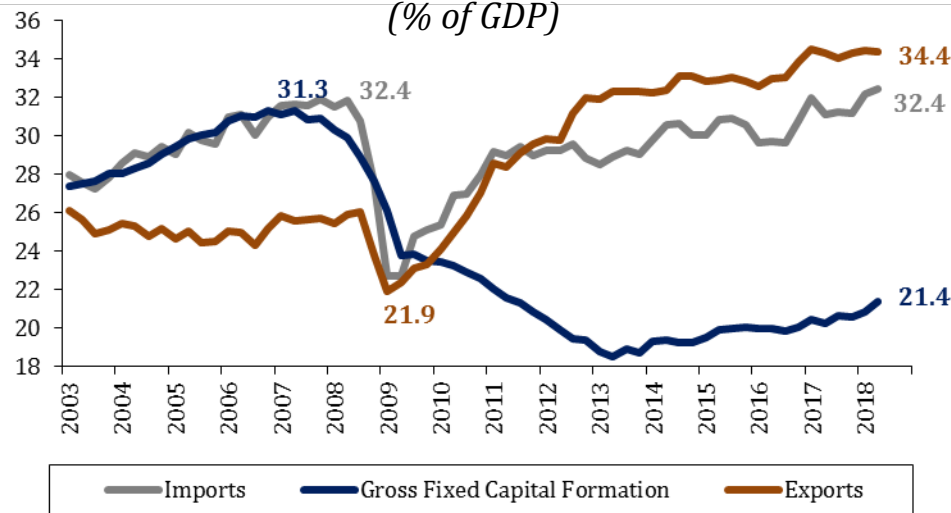
- ▶ Budget Law 2018 approved.
 - ❑ General Government deficit to be below 3% EU reference value.
 - ❑ Local authorities in surplus.
 - ❑ More fiscal space given to regions.

- ▶ After rating upgrades expect a widening and deepening of Spain's investor base, and an improvement in average quality of participants.

Spain's growth pattern

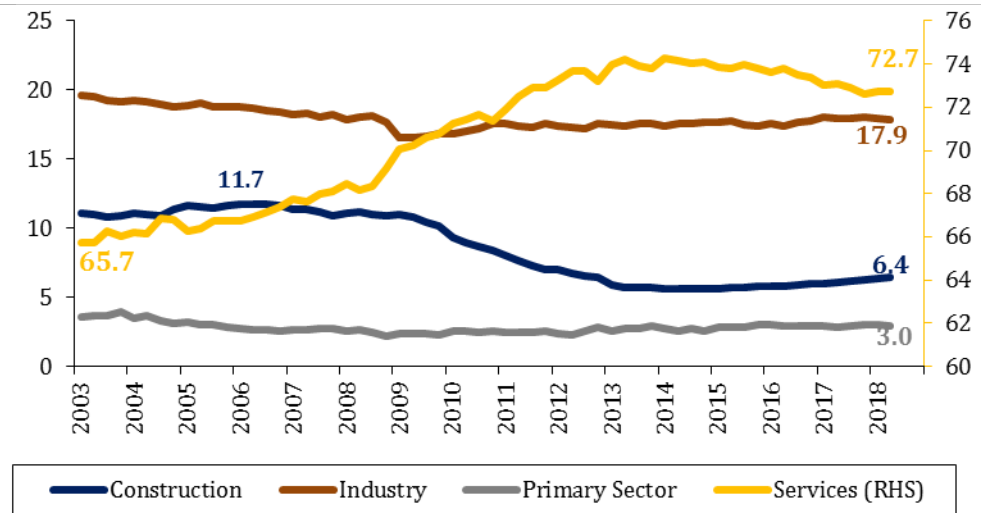
- ▶ The current expansion is labour-intensive and more balanced between internal and external demand.
- ▶ Less investment in construction, more exports, higher weight of services sector.
- ▶ Investment has converged to Euro Area average.

Exports and Imports of Goods and Services & Gross Fixed Capital Formation.
(% of GDP)



Source: Instituto Nacional de Estadística.

Gross Value Added.
(% of GDP)

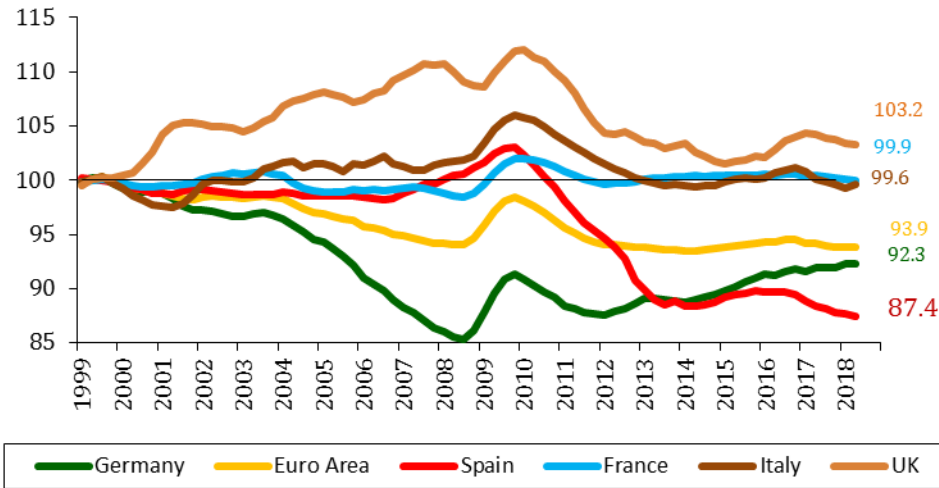


Source: Instituto Nacional de Estadística.

A labour-intensive recovery

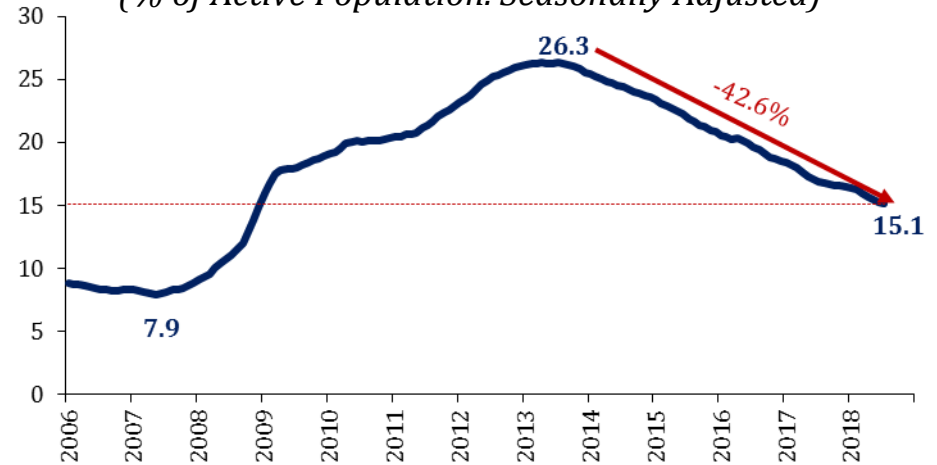
- ▶ Increased real labour productivity has led to enhanced competitiveness and more efficient allocation of labour.
- ▶ Falling unemployment fuels internal demand.

Real Unit Labour Costs.
(Index 1999=100, Smoothed)



Source: EUROSTAT.

Monthly Unemployment Rate.
(% of Active Population. Seasonally Adjusted)

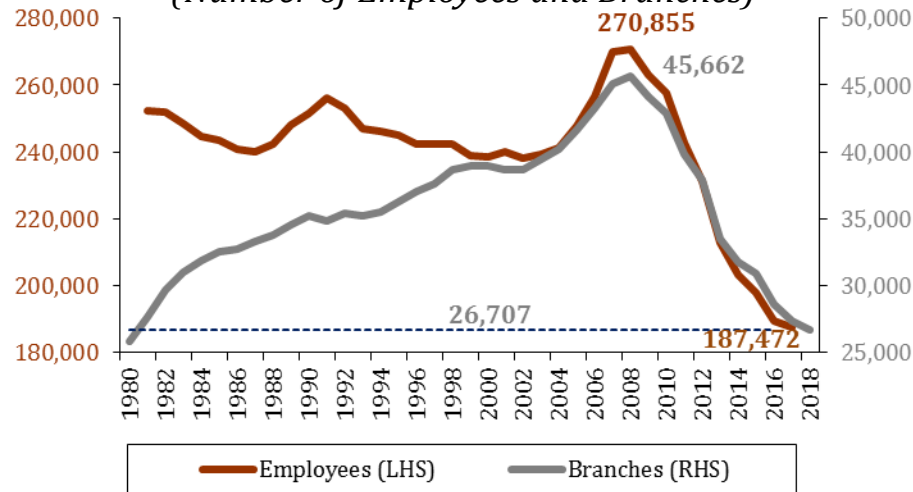


Source: EUROSTAT.

Banking sector adjustment

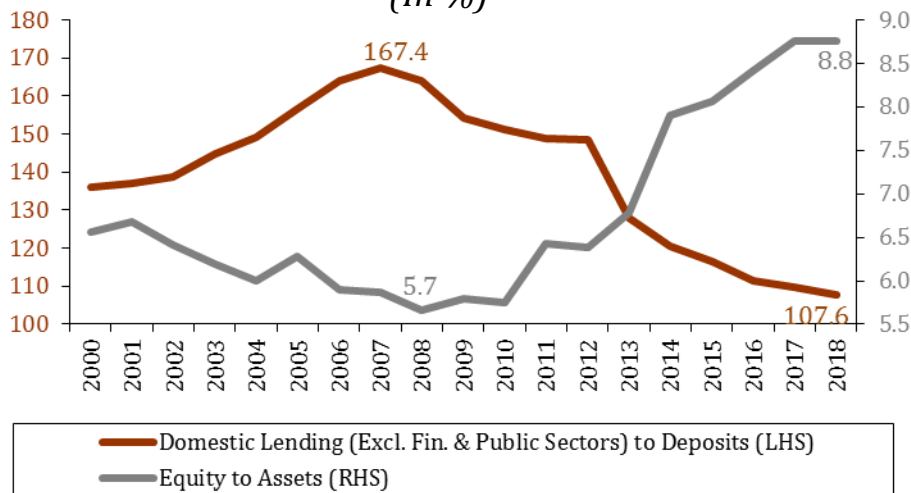
- ▶ Adjustment of the banking sector:
 - ❑ Downsizing & loss recognition.
 - ❑ Enhanced capitalisation and profitability.
- ▶ Strong improvement in NPLs: harmonised NPL ratio below Euro Area average.

Adjustment in Deposit Taking Institutions
(Number of Employees and Branches)



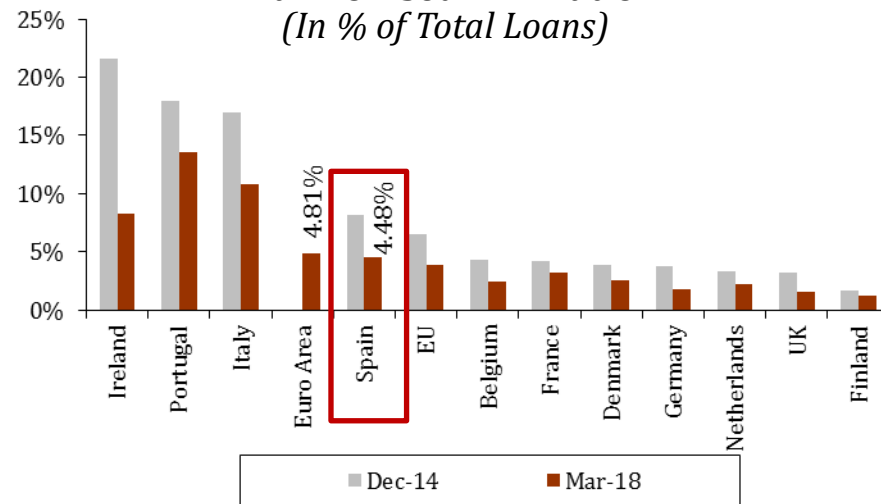
Source: Bank of Spain.

Loan-to-Deposits & Equity to Assets.
(In %)



Source: Bank of Spain.

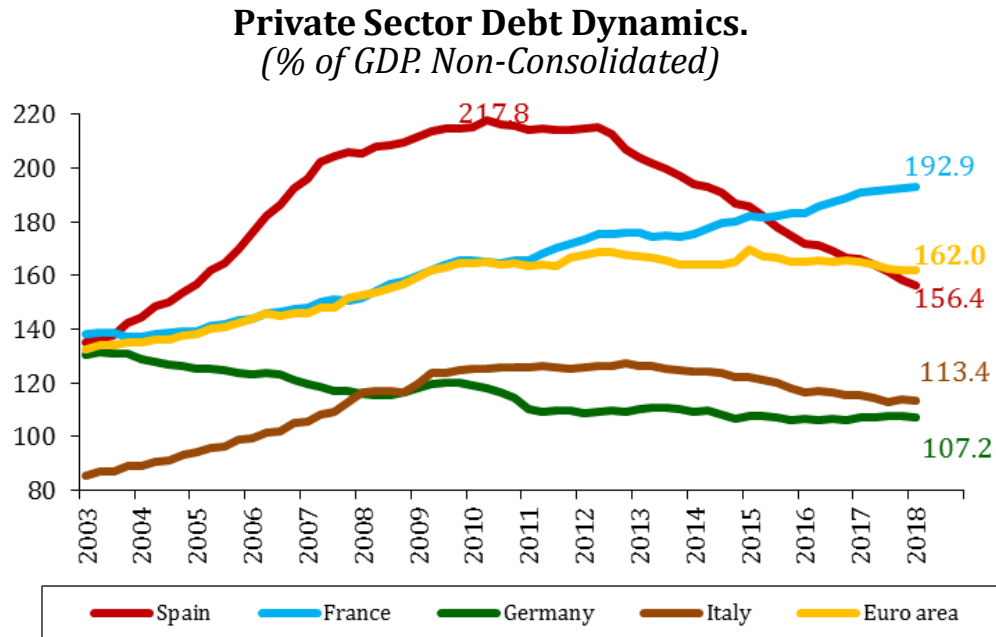
Harmonised NPL Ratio.
(In % of Total Loans)



Source: EBA. Risk Dashboard Interactive Tool.

Private deleveraging

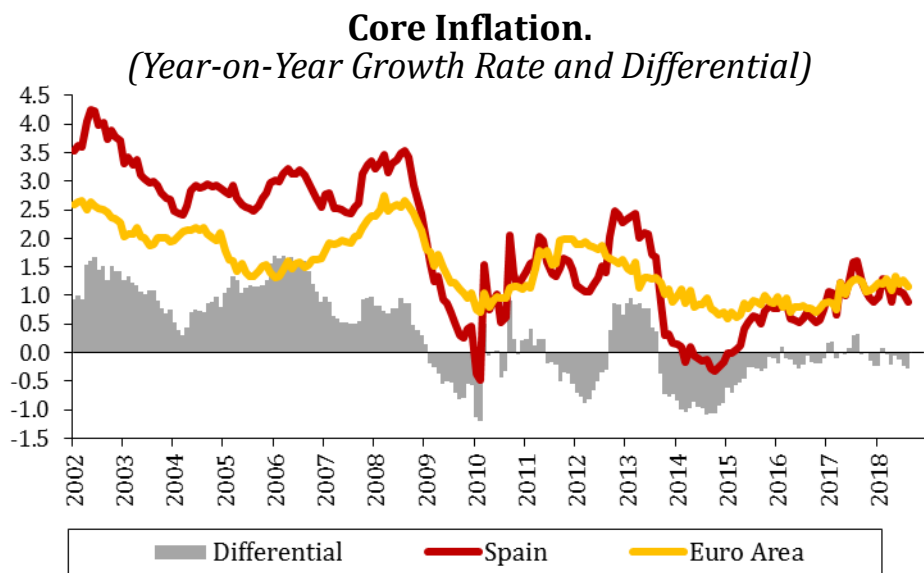
► Since 2010Q2, private sector debt decreased by 61.4pp of GDP → households & nonfinancial corporations' leverage below Euro Area average.



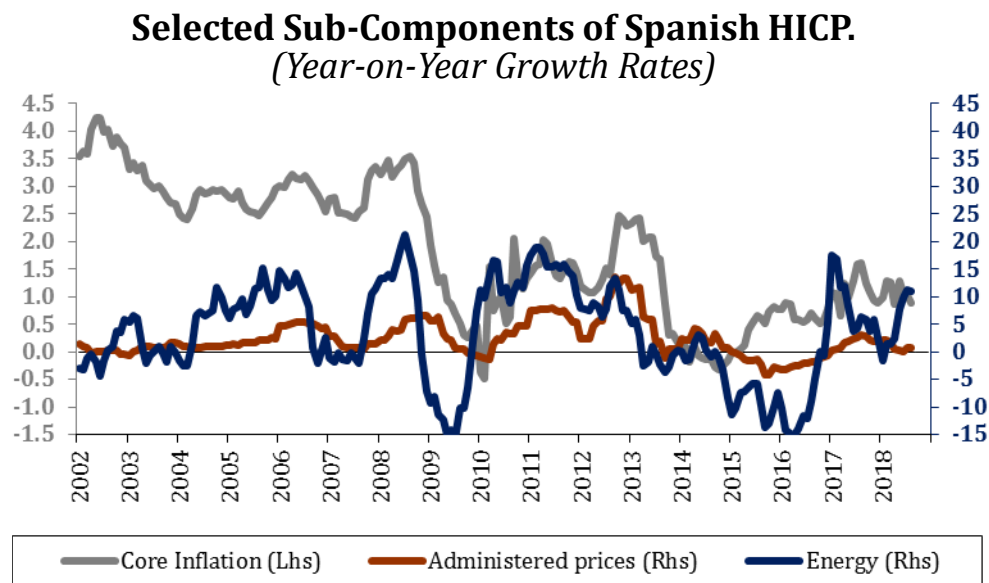
Sources: EUROSTAT, Banco de España and Instituto Nacional de Estadística.

Core inflation has converged to Euro Area levels

- ▶ Spanish core inflation broadly in line with Euro Area average.
 - ❑ Wage inflation and administered prices stable despite strong employment creation.
 - ❑ Energy remains a major contributor to shifts in headline inflation.



Source: EUROSTAT.

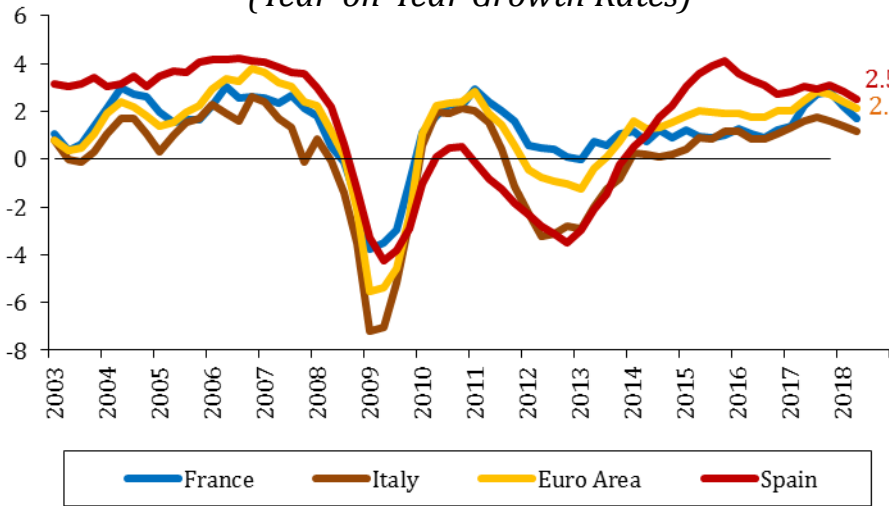


Source: EUROSTAT.

Result: persistent growth with current account surplus

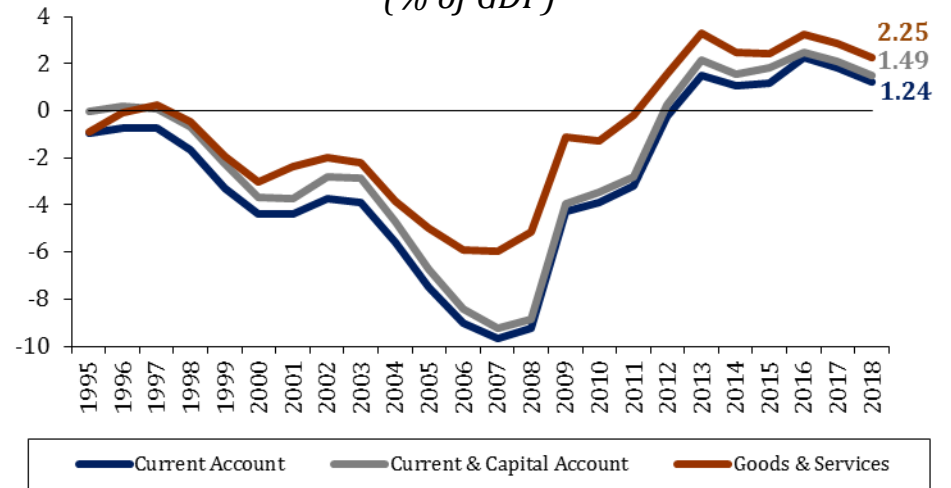
- ▶ Current account surplus synchronous with economic growth → growth better diversified: internal and external demand.
- ▶ Exports better diversified – geographically, by type of product. Proven resilience to strong Euro.

GDP Growth vs. Peers.
(Year-on-Year Growth Rates)



Source: Eurostat.

Current Account & Goods and Services Balance.
(% of GDP)



Source: Instituto Nacional de Estadística and Bank of Spain.

Macroeconomic scenario 2018-2021

- Growth to continue through internal and external demand.

Macroeconomic scenario (YoY growth rates in percent)									
	2015	2016	2017	2018	Q1	Q2	2019	2020	2021
Private consumption expenditure	3.0	2.9	2.5	2.4	3.1	2.3	1.9	1.8	1.7
General Government consumption expenditure	2.0	1.0	1.9	1.5	2.4	1.9	1.4	1.2	1.2
Gross Fixed Capital Formation	6.7	2.9	4.8	4.2	3.9	7.7	4.0	3.8	3.7
National Demand (Contribution to GDP Growth)	3.9	2.4	2.9	2.5	3.1	3.3	2.2	2.0	2.0
Exports of goods and services	4.2	5.2	5.2	4.7	3.4	2.3	4.5	4.2	3.8
Imports of goods and services	5.4	2.9	5.6	4.6	4.7	5.2	4.2	3.9	3.7
External demand (Contribution to GDP Growth)	-0.3	0.8	0.1	0.2	-0.3	-0.8	0.2	0.2	0.1
Gross Domestic Product	3.6	3.2	3.0	2.7	2.8	2.5	2.4	2.2	2.1

Other variables									
	2015	2016	2017	2018	Q1	Q2	2019	2020	2021
Unemployment rate (in % of Active Population)	22.1	19.6	17.2	15.5	16.7	15.3	13.8	12.3	11.0
Full-time Equiv. Employment (YoY Growth)	3.3	3.0	2.9	2.5	2.6	2.5	2.2	2.1	2.0
Net lending(+)/borrowing(-) with RoW (% of GDP)	1.7	2.4	2.2	1.6	2.1	1.8	1.5	1.4	1.3
Private Consumption deflator (YoY Growth)	-0.2	0.0	1.6	1.7	1.0	1.4	1.6	1.7	1.7
Headline Balance General Gov't (in % of GDP)*	-5.3	-4.5	-3.1	-2.7	-2.96	-2.71	-1.8	-1.1	-0.4
USD/€ exchange rate**	1.1	1.1	1.13	1.2	1.23	1.19	1.2	1.2	1.2
Euro Area GDP growth (YoY growth)**	1.9	1.9	2.5	2.4	2.4	2.1	2.0	1.8	1.8
Oil prices (Brent, USD/barrel)**	52.2	43.3	54.3	67.7	66.8	74.5	63.9	63.9	63.9

* Including Financial Sector One-Offs

** Stability Programme Update 2018-2021.

Shaded areas are realisations. In white, forecasts contained in the Macroeconomic Scenario 2018-2021, July Update.
2018Q2 Quarterly National Accounts data are flash estimates.

Sources: Ministerio de Economía y Empresa and Ministerio de Hacienda.

Fiscal policy framework

- ▶ General Government deficit expected below 3% by end 2018.
- ▶ Deficit in Social Security System expected to fall by two thirds by 2020.

Net Lending(+)/Borrowing. (% of GDP)											
	2011*	2012	2013	2014	2015	2016	2017	Forecast			
								2018	2019	2020	2021
Central Government	-3.6	-7.9	-4.8	-3.7	-2.8	-2.6	-1.89	--	-0.4	-0.1	0.0
Autonomous Regions	-5.1	-1.9	-1.6	-1.8	-1.7	-0.9	-0.36	--	-0.3	-0.1	0.0
Local Governments	-0.8	0.3	0.6	0.5	0.4	0.6	0.61	--	0.0	0.0	0.0
Social Security	-0.1	-1.0	-1.1	-1.0	-1.2	-1.6	-1.44	--	-1.1	-0.9	-0.4
General Government	-9.64	-10.47	-6.99	-5.97	-5.27	-4.47	-3.08	-2.7	-1.8	-1.1	-0.4

* Figures affected by the Negative impact of the Settlement System.

Excluding the impact of the Settlement System Autonomous Regions' deficit was 0.55% of GDP lower in 2010 and 1.77% of GDP in 2011.

In the case of Local Governments the impact of the Settlement System amounted to 0.13% of GDP in 2010 and to 0.39% of GDP in 2011.

Both yearly amounts would add to the headline Central Government figures.

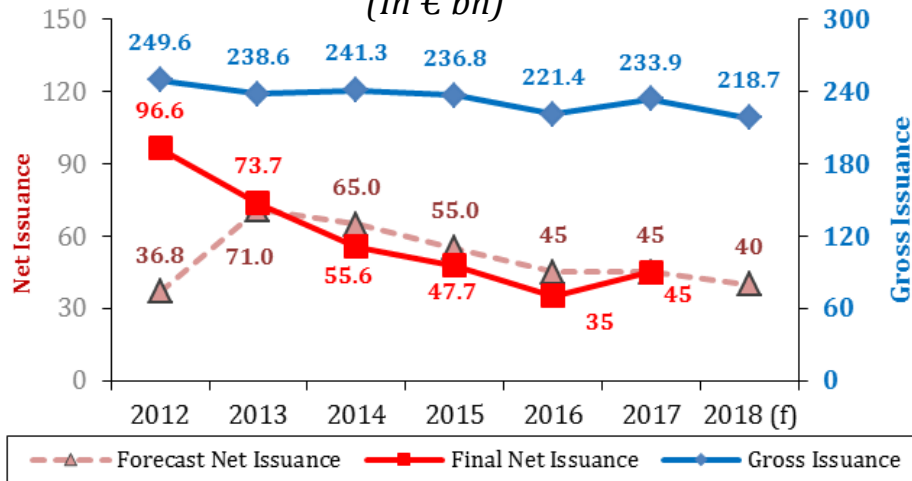
Source: Ministerio de Hacienda.

Forecasts are those contained in the Budgetary Stability Objectives.

The Treasury's funding programme in 2018

- ▶ Net issuance of €40 bn in 2018; programme includes loan to Social Security.
- ▶ Total issuance up to October 3rd: €170.4 bn, 77.9% of the funding programme
 - ❑ Medium- and long-term: €110.4 bn (82.2%), and
 - ❑ Short-term (Letras del Tesoro): €60.0 bn (71.1%).

The Treasury's Funding Programmes Since 2012
(In € bn)



Source: Secretaría General del Tesoro y Financiación Internacional.

Funding Programme in 2018

(In billion euros and in effective terms)	End 2017	Forecast 2018
Total Net Issuance	45.031	40.000
Total Gross Issuance	233.900	218.687
<i>Medium- and Long-term</i>		
Gross Issuance ¹	139.462	134.310
Amortisation ¹	90.903	86.310
Net Issuance ¹	48.559	45.000
<i>Letras del Tesoro</i>		
Gross Issuance	94.439	84.377
Amortisation	97.966	89.377
Net Issuance	-3.528	-5.000

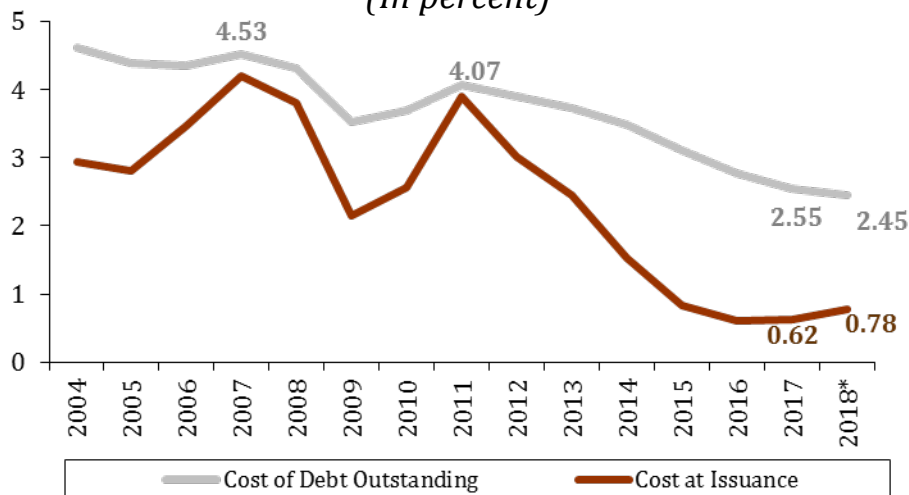
¹ Includes debt in other currencies, Bonos y Obligaciones, loans and assumed debts.

Source: Secretaría General del Tesoro y Financiación Internacional.

Cost and life of debt: a longer portfolio at historically low rates

- ▶ Average cost of debt outstanding at historic low (2.45%).
- ▶ Slight increase in cost of 2018 YTD issuance due to longer tenors issued in 2018.
- ▶ Since 2013 average life of debt outstanding increased from 6.20 years to 7.5 years.

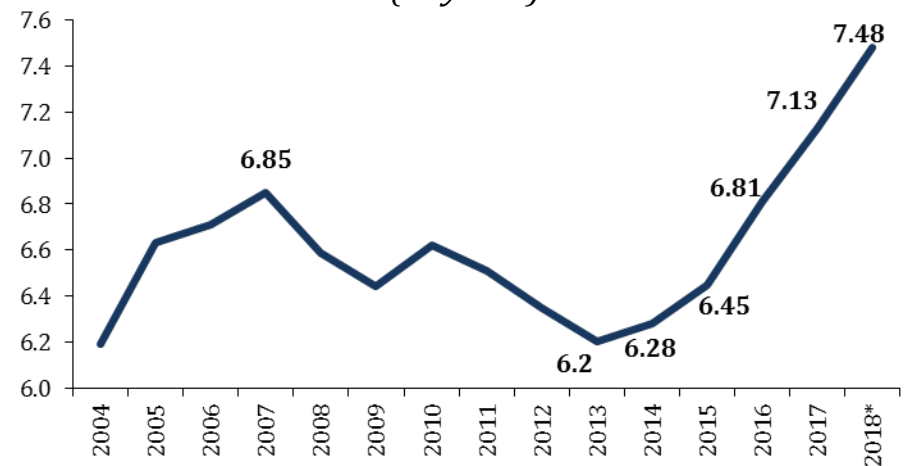
Cost of Debt Outstanding and Cost at Issuance
(In percent)



Source: Secretaría General del Tesoro y Financiación Internacional.

*As of 03/10/2018

Average Life of Debt Outstanding
(In years)

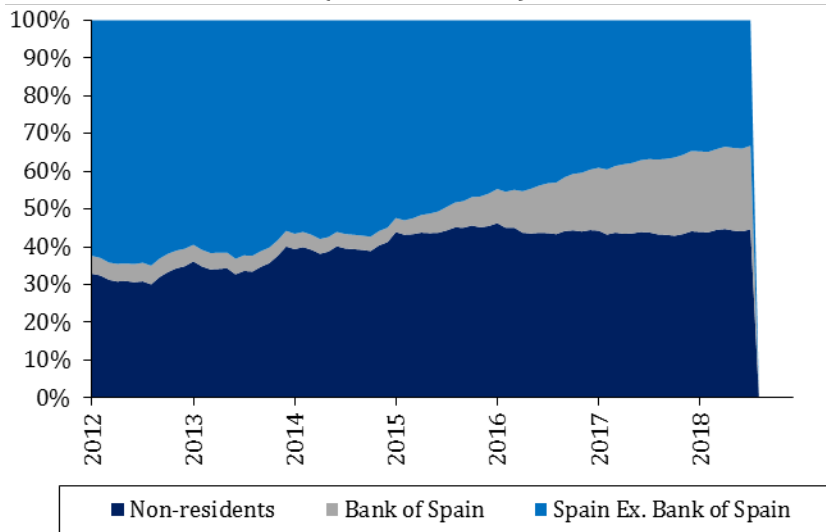


Source: Secretaría General del Tesoro y Financiación Internacional.

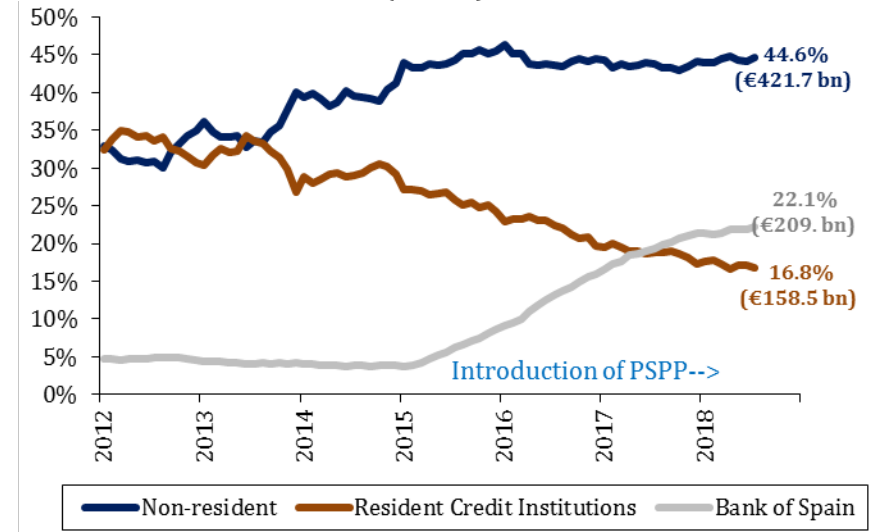
Recent trends in investor base

- ▶ Non-residents continue to be the leading investors with a stable share around 44.6%.
- ▶ Spanish banks have been reducing their absolute and relative holdings of Spanish bonds.
- ▶ This move has been compensated by the increase in Bank of Spain's holdings to 22.1%.

Holdings of Letras & Bonos and Obligaciones del Estado (% Structure) **Holdings of Letras & Bonos and Obligaciones del Estado (€ mn)**



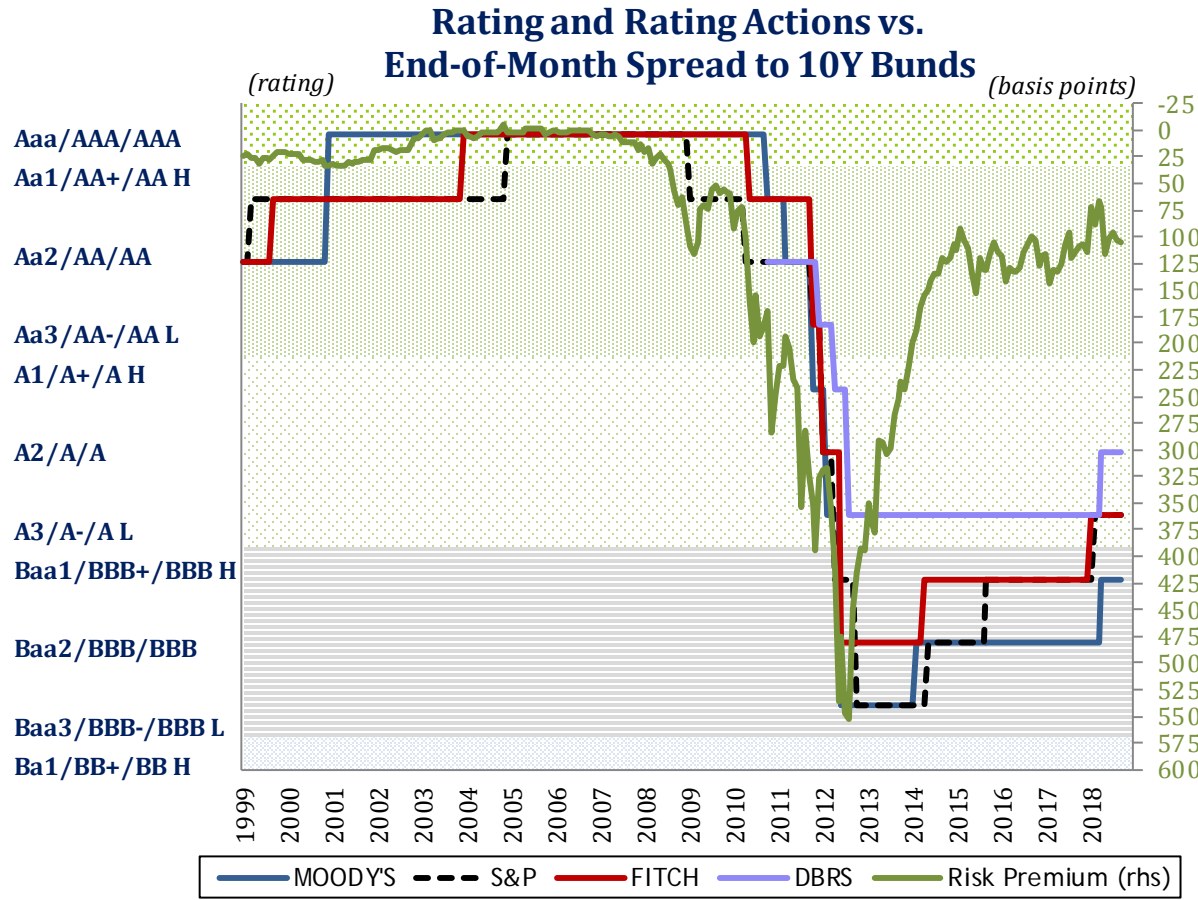
Source: Bank of Spain.
(2012-2015 IBERCLEAR data / 2016- Securities Holdings Statistics)



Source: Bank of Spain.
(2012-2015 IBERCLEAR data / 2016- Securities Holdings Statistics)

Ratings

► Expecting more foreign investors after recent upgrades: A- positive outlook (S&P), A- stable outlook (Fitch), A stable outlook (DBRS), Baa1 stable (Moody's).



	Fitch	S&P	DBRS	Moody's
January	19			
February				
March		23		
April			6	13
May				
June				
July	13			
August				
September		21	28	
October				5
November				
December				

Thank you for your attention

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