Spain's new economic growth model

November 2013

MINISTERIO
DE ECONOMÍA
Y COMPETITIVIDAD

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Overview

The foundations of the new economic growth model

The three pillars underpinning Spain's economic policy

1 **Commitment with the sustainability of public finances**

- Structural fiscal adjustment of 3.1% in 2012 according to the IMF
- All levels of public administration accounts are becoming sustainable
  - Deficit / GDP in 2012 (y-o-y change): central government 4.2% (–0.9pp), regions: 1.8% (–1.6pp), local entities: 0.2% (–0.3pp)
- Deficit target for the current year (6.5%) within reach and a credible path to bring deficit below 3% by 2016

2 **Clean up and recapitalization of banks leading to a strong financial system**

- Successful completion of the financial assistance programme for the recapitalization of financial institutions
- Increased coverage ratios to real estate and construction
  - Banks' exposure to real estate sector down by almost 50% in 2012
- More transparent and better equipped banks to finance real economy
  - Enhanced transparency framework and strengthened financial supervision

3 **Structural reforms to boost competitiveness and productivity**

- Labour market reform is behind the decline in unit labour costs and the change in labour market dynamics
  - Since 2009, Spain's ULC have declined by 7% vs Eurozone up by 3%
  - The latest Labour Force Survey (Q3-13) has confirmed job creation in the private sector for two consecutive quarters
- Orderly private sector deleveraging: -22.9pp of GDP (from 231.2% in June 2010 to 208.3% in Q2 2013)
- Trade balance surplus with the Eurozone and strong export performance: exports of goods +7% y-o-y from January to September 2013

Macroeconomic Scenario 2014
First Year of the Effective Recovery

The correction of imbalances continues in 2013 and 2014

- Official growth forecasts have been reviewed on the upside and unemployment figures on the downside, in line with the market consensus
- The external sector will spur growth while internal demand will further stabilize in 2014
- Spain's position as a net lender to the rest of the world continues to increase

(% yoy change)	2012	2013	2014
GDP	-1,6	-1,3	0,7
Private consumption	-2,8	-2,6	0,2
Public consumption	-4,8	-2,3	-2,9
Gross Fixed Capital Formation	-6,9	-6,1	0,2
National Demand (*)	-4,1	-3,2	-0,4
Exports of goods and services	2,1	5,7	5,5
Imports of goods and services	-5,7	-0,3	2,4
Net exports (*)	2,5	1,9	1,2
Net lending (+) / borrowing (-) with RoW (% of GDP)	-0,6	2,3	3,4
GDP deflator	0,0	1,0	1,3
Total employment (**)	-4,8	-3,4	-0,2
Unit Labour Costs	-3	-1,6	-0,6
Unemployment rate	25	26,6	25,9
Public Deficit (% of GDP)	-6,8	-6,5	-5,8

GDP growth (% yoy change)	2013	2014
Spanish Government (Sep. 2013)	-1.3	0.7
European Commission (Nov 2013)	-1.3	0.5
IMF (Aug. 2013)	-1.3	0.2
OECD (Nov 2013)	-1.3	0.5
National Consensus (Nov. 2013)	-1.3	0.8
International Consensus (Nov. 2013)	-1.3	0.5
Spanish Government (June 2013)	-1.3	0.5

Source: MINHAP, EC Spring Forecasts, IMF, OECD, FUNCAS, Consensus Forecasts

Spain's adjustment in an international context

Despite the recent turbulences, the Euro Area displays sound macroeconomic indicators

	Spain			Euro Area			USA			UK			Japan		
	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014	2012	2013	2014
GDP growth[1]	-1.4	-1.5	0.7	-0.7	-0.4	1.1	2.8	1.6	2.6	0.1	1.3	2.2	2.0	2.1	2
Inflation[1]	2.4	1.8	0.9	2.5	1.5	1.5	2.1	1.5	1.9	2.8	2.6	2.3	0.0	0.3	2.6
Unit Labour Costs[1]	-3.0	-1.6	-0.6	1.9	1.1	0.7	1.1	1.0	1.2	3.0	0.7	0.3	-1.5	-2.3	1.0
Public Deficit[2]	-6.8	-6.5	-5.8	-3.7	-3.1	-2.5	-9.1	-6.4	-5.7	-6.1	-6.4	-5.3	-9.6	-9.6	-7.2
Government Gross Debt[2]	85.9	94.2	98.9	92.6	95.5	95.9	102.7	106.0	107.3	88.7	94.3	96.9	238.0	246.7	247.1
Exports of Goods and Services[1]	2.1	5.7	5.5	2.5	1.3	4.2	3.5	3.0	5.6	2.3	1.5	4.1	-0.1	3.6	5.8
Current account[2]	-1.2	1.7	2.8	1.3	2.3	2.5	-2.7	-2.6	-2.7	-3.8	-4.3	-4.4	1.0	1.2	1.8

NOTES: (1) year-on year change; (2) % of GDP
Source: Spain's General Budget 2014, European Commission Autumn Forecasts 2013 and IMF Fiscal Monitor October 2013

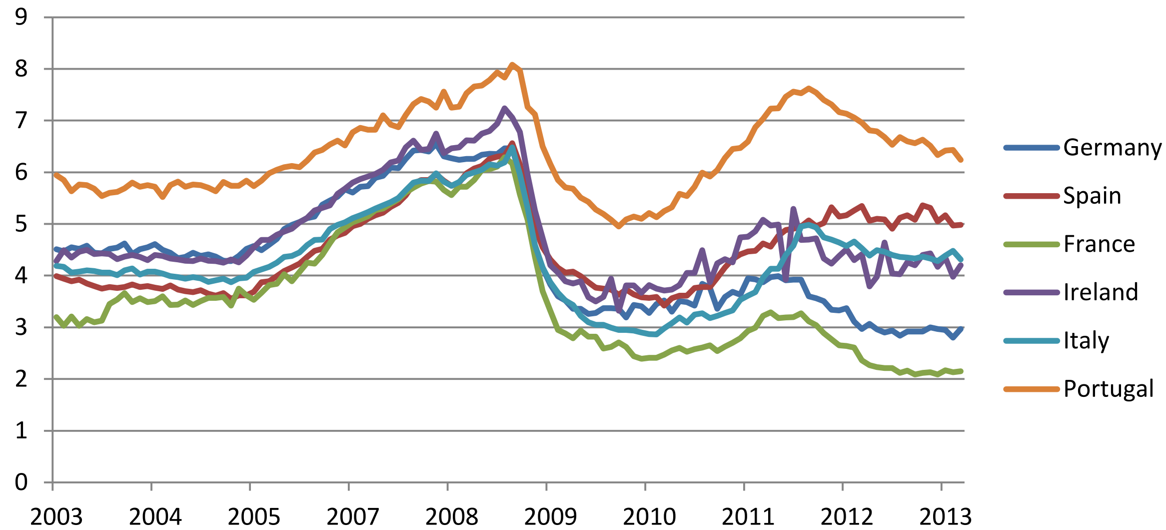
Remaining challenges at the EU-level

A credible commitment towards a robust and complete Banking Union is required to reduce fragmentation and to facilitate the flow of credit

Despite the advances in the institutional set up of the Euro area, fragmentation persists and there are asymmetries in SME access to credit

Genuine European banking union

Lending rates of new loans to Non-Financial corporations (Maturity up to 1 year, less than €1 million)



1
- **Single Supervisory Mechanism (operative on H2-2014)**
  - Comprehensive assessment: supervisory risk assessment, asset quality review and stress tests (H1-2014)
  - Capital backstops (in place before AQR and stress tests results)

2
- **Single Resolution Mechanism (agreement before year-end 2013)**
  - New EU-wide bank resolution rules (before year-end 2013)
  - Common scheme for resolution funding

3
- **Single Deposit Guarantee Scheme (to be discussed from 2014)**

Source: ECB

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Sustainability of Public Finances and Reform of the Public Sector

A clear Commitment with Fiscal Consolidation

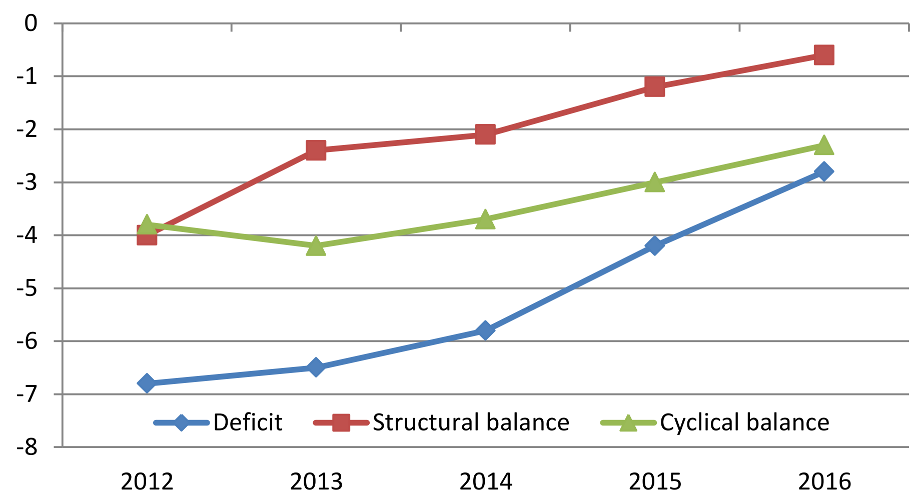
A credible medium-term fiscal path that strikes a reasonable balance between structural adjustment and support to growth

- Spain's 2012 deficit was 6.8% of GDP excluding one-off support to the financial sector. In structural terms and according to the IMF, Spain's fiscal effort was 3% of GDP; the highest amongst large developed economies
- The 2013 deficit target is in sight thanks to the consolidation measures that are being adopted
- The adjustment path to bring the public deficit below 3% has been extended by 2 years. However this does not imply a fiscal relaxation at all: the structural effort will remain substantial and the focus lies on the medium term
- The Draft Budget for 2014 further anchors financial sustainability
  - It continues the decreasing trend in public expenditure and contemplates selective tax breaks for entrepreneurs
  - The reduction of the deficit will no longer take place in a recessive context. The adjustment was frontloaded in 2012/2013 and is now more flexible, guaranteeing all along the sustainability of public finances
  - Tax collections in 2014 will increase by 2.4% on account of the increase in activity

The fiscal path for the public administrations (excl. one-offs)

(% of GDP)	2012	2013	2014	2015	2016
Central Government	-4.2	-3.8	-3.7	-2.9	-2.1
Autonomous Regions	-1.8	-1.3	-1.0	-0.7	-0.2
Local Governments	0.2	0.0	0.0	0.0	0.0
Social Security Administrations	-1.0	-1.4	-1.1	-0.6	-0.5
General Government	**-6.8**	**-6.5**	**-5.8**	**-4.2**	**-2.8**

Breakdown of Public Balance (% GDP)



1. *Ministry of Economy and Competitiveness.*

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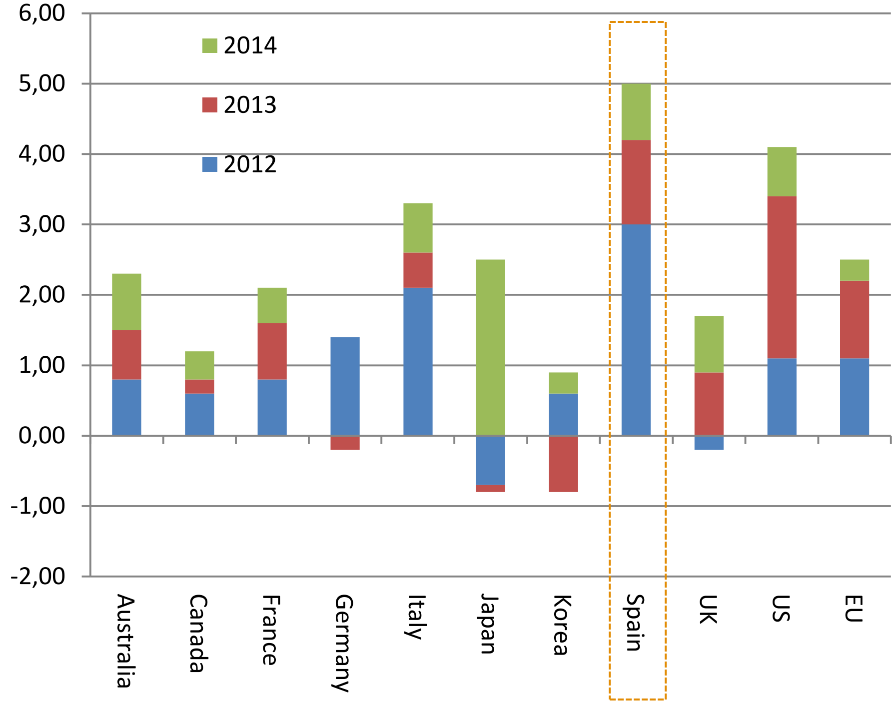
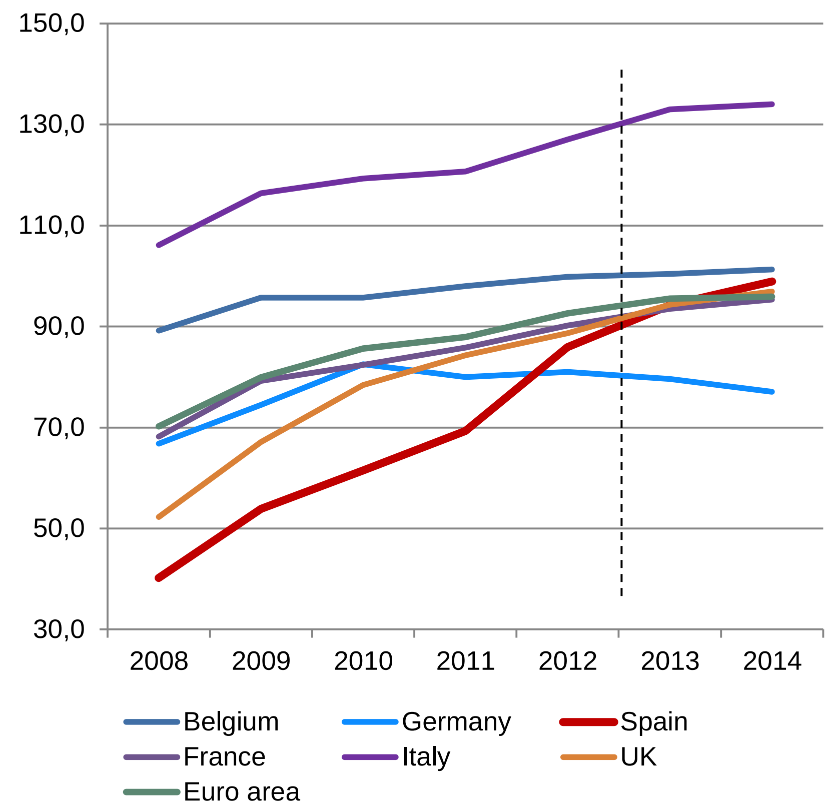
Structural fiscal efforts guarantee the sustainability of public finances

IMF Projections of Change in Cyclically Adjusted Primary Balances



Change in cyclically adjusted primary balance of 5% of GDP from 2012 to 2014. The largest among G20 economies

Evolution of debt/GDP ratios of selected countries



Spain's debt/GDP ratio is increasing but sustainable. It is around levels close to the Eurozone average

Source: IMF, MINHAP and European Commission (Spring forecasts, 2013)

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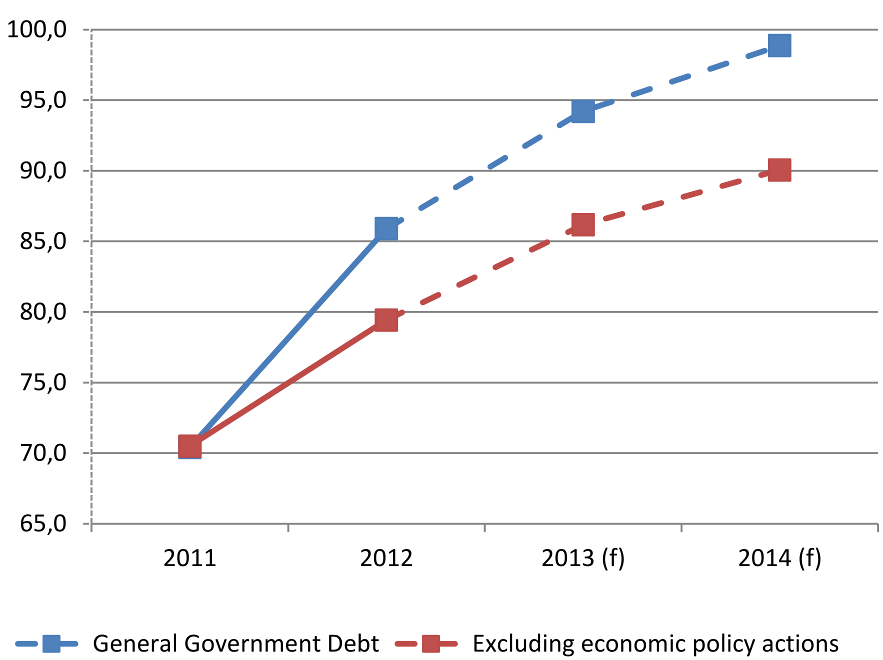
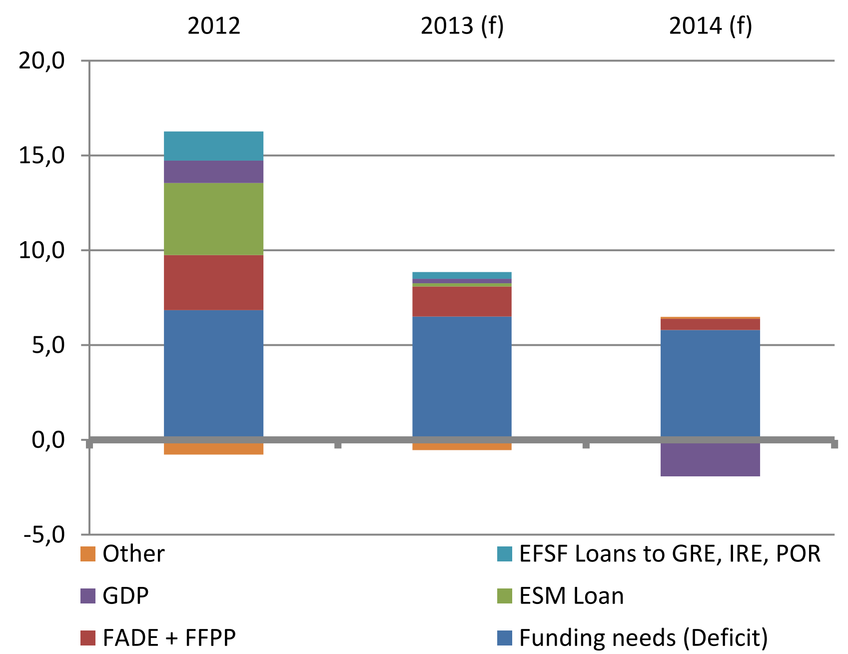
Debt dynamics in 2013 and 2014

General government debt (%GDP)



Factors behind the increase in debt/GDP

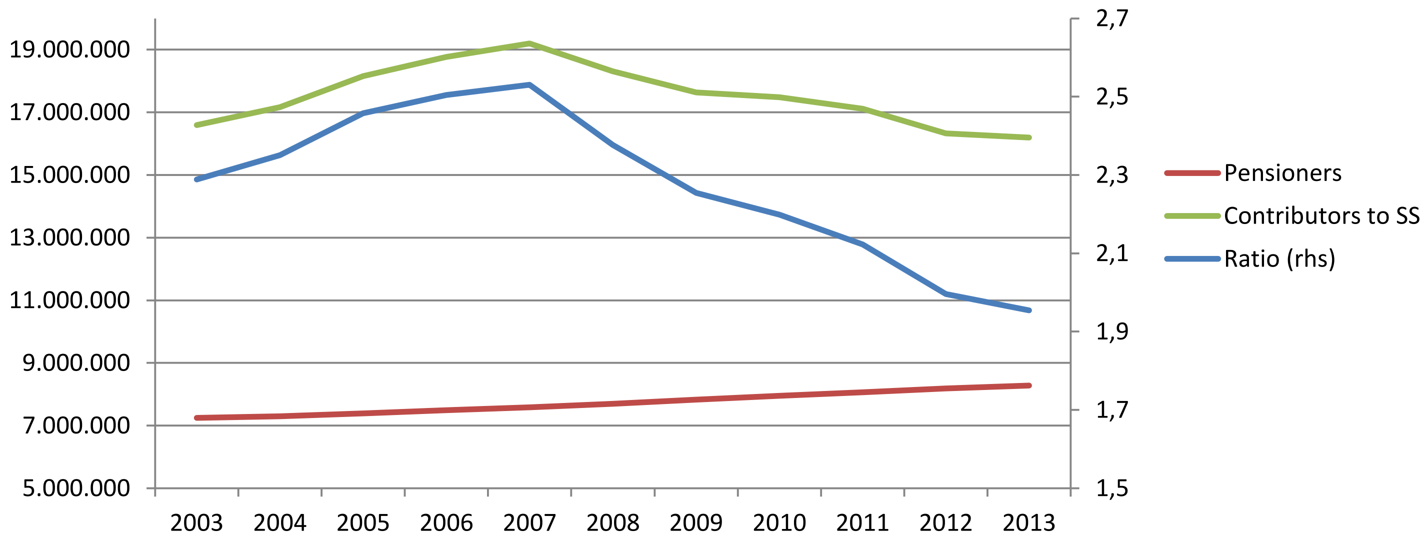


- Debt/GDP expected to reach 94.2% by year-end 2013 and 98.9% by year-end 2014
- Excluding explicit economic policy actions that do not arise from funding needs of the public sector, the ratio would be 90% in 2014
  - Explicit economic policy actions are one-offs such as FADE (electricity tariff deficit fund), FFPP (fund to pay arrears owed to suppliers), ESM loan (financial assistance programme) and guarantees for EFSF loans to Programme Countries (Ireland, Portugal, Greece)
- In 2014, GDP growth is expected to detract 1.9pp from the debt/GDP ratio for the first time since 2008

Source: IGAE, Spanish Treasury, Bank of Spain

A pension reform that guarantees the long term sustainability of the system

Pensioners and Contributors to the Social Security System



- In March 2013 a new law was approved to modify the retirement regime and to enable the continuation of activity after retirement
- The Pension System will be further reformed in order to guarantee its long-term sustainability. A group of experts on the sustainability factor has proposed a general de-linking of pensions from inflation and advocates for the introduction of two factors
  - Inter-generational factor: links pensions to life expectancy
  - Yearly update factor: links pensions to the income and expenditure of the pension system as a whole, the number of pensioners and the average pension due

Source: Ministerio Empleo y Seguridad Social

A new institutional and regulatory framework for all public administrations

Regions and local entities on track to meet 2013 deficit targets

- Regional governments posted a deficit of 1.76% of GDP in 2012, a modest deviation from the deficit target of 1.5% of GDP, 1.6pp less than last year's deficit thanks primarily to cuts in expenditures
- The structural fiscal framework has been strengthened through:
  - The approval of the Budgetary and Financial Stability Law
  - The creation of two funds to ensure adequate funding of local and regional governments

Budgetary and Financial Stability Law & Enhanced Transparency

- Fiscal discipline at all levels of the administration
- Early-warning system, enforcement and sanction procedures
- Transparency: monthly and quarterly reporting on budget execution. Submission of budgetary guidelines previous to the approval of regional budgets
- Assurance of compliance: coercive measures and enforced compliance
- Law for transparency in the public administrations: accountability & governance

Liquidity & Financing to Regions and Local Governments

- Fund for the Financing of Payments to Suppliers (FFPP):
  - Provides a financing vehicle to regional and local governments for the regularisation of arrears
    - Outstanding commercial debt owed to suppliers
  - Forcing fiscal adjustment at regional and local level. Subject to conditionality
  - Disbursed amounts:
    - Local Administrations: €9.3bn
    - Regional Administrations: €17.5bn
    - … and a €1.2bn increase in 2013
- Regional Liquidity Mechanism (FLA):
  - 9 of the 17 regions have adhered to the FLA
  - 2012: €16.6bn
  - 2013: €23.0bn (already computed in debt/GDP ratio)

A Thorough and Transparent Reform of the Banking Sector

Banking Sector Reform: A Transparent and Comprehensive Exercise

- Cleaning-up of balance sheets through increased provisioning requirements
  - The impact on profits and reserves of increased coverage requirements on exposures related to real estate developers has been of €78bn
- Identification of individual bank capital needs through evaluations from the IMF and **independent external evaluators**
  - 70% of the Spanish financial sector is sound and did not require additional capital
  - Capital needs concentrated on the 4 banks owned by the FROB (BFA-Bankia, Catalunya Bank, NCG Banco, Banco Valencia), which account for 18% of the system
- Recapitalisation, restructuring and resolution of the troubled banks with identified capital shortfalls
  - External financing by the ESM was available for banks unable to cover shortfalls privately
  - Total funds disbursed: €41.3bn; less than 4% of GDP
- Segregation of troubled real estate assets and their transfer to an external Asset Management Company (SAREB)
  - SAREB, with majority of private capital (55%), has received €50.5bn of foreclosed assets and risks linked to developers
- Regulatory reform focused on resolution, savings banks, enhanced transparency and minimum capital requirement for all banks

Early introduction of provisions foreseen in the future European Directive on Bank Recovery and Resolution currently under negotiation at the EU level

New Framework for Bank Restructuring and Resolution

- **Early intervention for mild difficulties**
- **Orderly resolution for non-viable institutions**
- **Restructuring measures for institutions with temporary troubles that can be solved with public support**

Successful completion of the Financial Assistance Programme

- After 18 months, the banking assisstance programme will be successfully closed in January 2014
- Spain’s exit will be clean and without further financial assistance
- Spain’s banks are strongly capitalized and in a comfortable position to face the upcoming ECB comprehensive assessment

Statement by the Eurogroup on Spain (14th November 2013)

We congratulated Spain on the successful implementation of its financial sector programme and the ambitious reform steps undertaken thus far…

We are fully supportive of Spain's decision not to request any successor ESM financial assistance following the programme exit in January 2014…

This is based on the fact that the ESM financial assistance and reform programme has proven to be successful in addressing financial sector vulnerabilities. The overall situation of the Spanish banking sector has significantly improved, including the access to funding markets of Spanish banks. In this respect, we also welcome the encouraging results of the recent forward-looking evaluation of the solvency of Spanish banks by the Banco de España. The process of bank restructuring is well underway and the burden-sharing exercise has been completed. We also noted with satisfaction that the regulatory and supervisory framework of the Spanish banking sector has been significantly strengthened, which translates into higher shock resilience of the banking sector….

Spain is a living example that EU-IMF adjustment programms are successful provided there is a strong ownership and genuine commitment to reforms. We commend the Spanish people for their efforts and achievements under difficult circumstances. The success of the Spanish financial assistance programme also clearly illustrates our resolve to work together to ensure the cohesion and stability of the euro area.

Asset Management Company: Sareb

Segregation and transfer to an Asset Management Company of troubled assets from banks that have received public support

Assets	Liabilities
▪ Transfer of assets from Group 1 and Group 2 banks completed: • Foreclosed RE assets with net accounting value < €100.000 • Loans to RE developers > €250.000 of net accounting value	▪ Equity approx. 8% of total assets ▪ Majority holding by private investors (55%) ▪ Sources of funding: 1. State-guaranteed senior debt issued in exchange of assets received 2. Subordinated debt and common equity
TOTAL ASSETS → €55.5bn	

- 28 equity holders, of which 27 are private investors and include domestic and foreign banks and insurance companies
  - The only public shareholder is FROB, with a 45% stake
- Equity: €4.8bn (25% share capital / 75% subordinated debt)
- Business plan with a 15 year horizon
- Expected RoE of approx. 13 –14% under conservative assumptions.
- Transferred assets: €50.5bn, for a gross book value of €106.6bn, implying an overall average discount close to 52%
- A total of around 200.000 assets have been transferred:
  - Foreclosed real estate assets → 107.000 assets for a value €11.3bn
  - Loans to real estate developers → 90.500 assets for a value of €39.4bn

- Sareb's activity
  - Nearly 4.500 Real Estate assets sold till mid-October 2013.
  - *Wholesale disposals and activity* are picking up
    - 14th November: Sareb sold its interest of €90m in bilateral loans to Metrovacesa
    - 14th November: disposal of €233m of loans collateralized with commercial real estate, called project Abacus.
    - 6th August: project Bull: Sareb creates an SPV with an institutional investor to sell together a portfolio valued at €100m consisting of 939 homes and annexes and a commercial real estate asset

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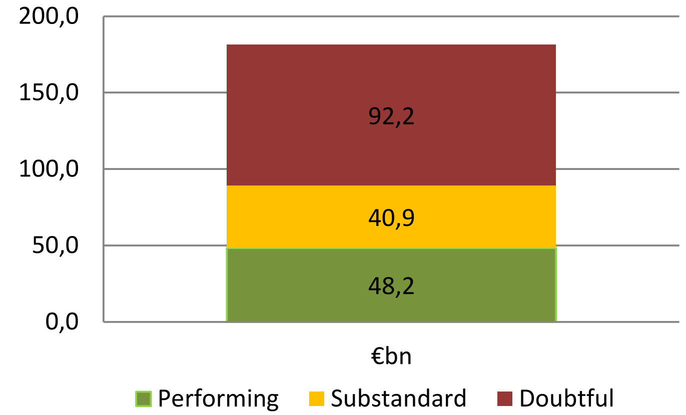
Enhanced Transparency in Refinancing Requirements

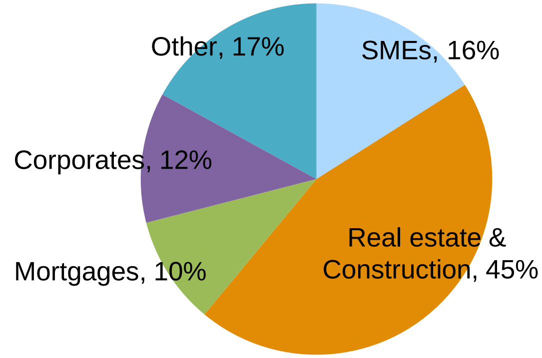
Spain is leading the field in best practice transparency frameworks and is well ahead its European partners

- Disclosure requirements have been enhanced and harmonized for all entities on key areas of their portfolios such as restructured and refinanced loans, NPL's, asset quality across asset classes, sectorial concentration and etc.
- In September 2013, restructured and refinanced operations amount to €181bn, around 12% of the total domestic loan portfolio
- c73% of the refinanced portfolio considered doubtful or substandard, and hence already provisioned
- The remaining 27% of the portfolio are performing loans
- 45% of the refinanced portfolio is related to real estate developers and construction. These exposures were significantly provisioned in 2012
- The Oliver Wyman stress test already took refinanced and restructured loans into account:
  - It specifically considered refinanced loans: the default rates of non-doubtful refinanced exposures were adjusted. This increased the estimated capital needs
  - These assumptions were more conservative than current developments, as actual figures and data prove

Restructured & refinanced loans in Sept 2013



Breakdown of restructured and refinanced loans

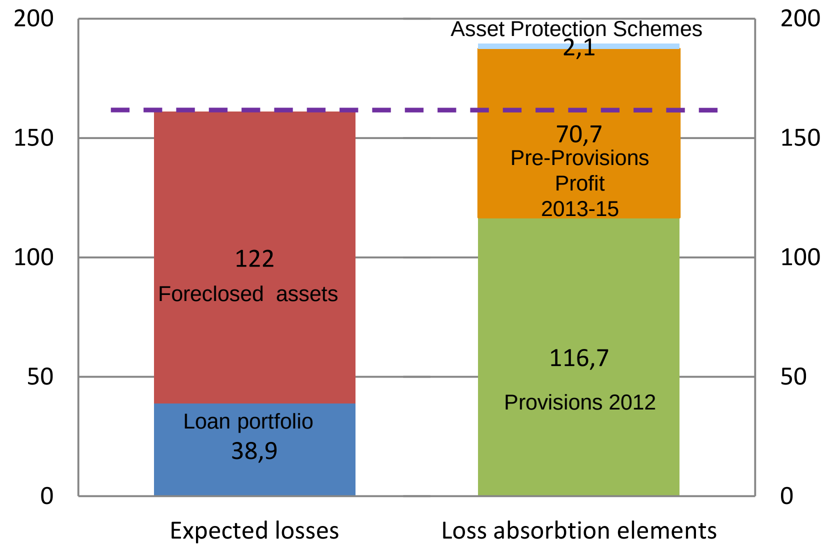


Bank of Spain has homogenised the classification criteria of restructured and refinanced loans across banks to ensure adequate provisioning

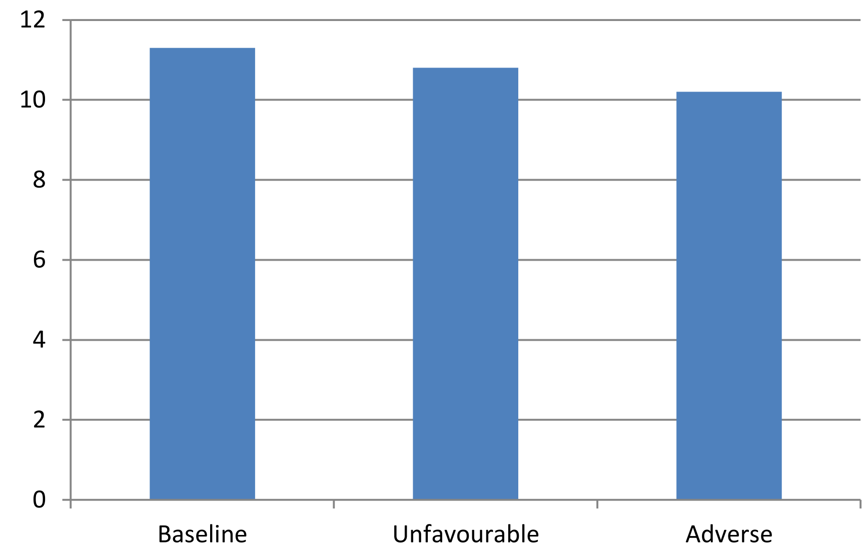
Source: Bank of Spain.

A strengthened supervisory framework

Results in the adverse scenario (€bn)



CET1 ratio under the three scenarios in 2015 (%)



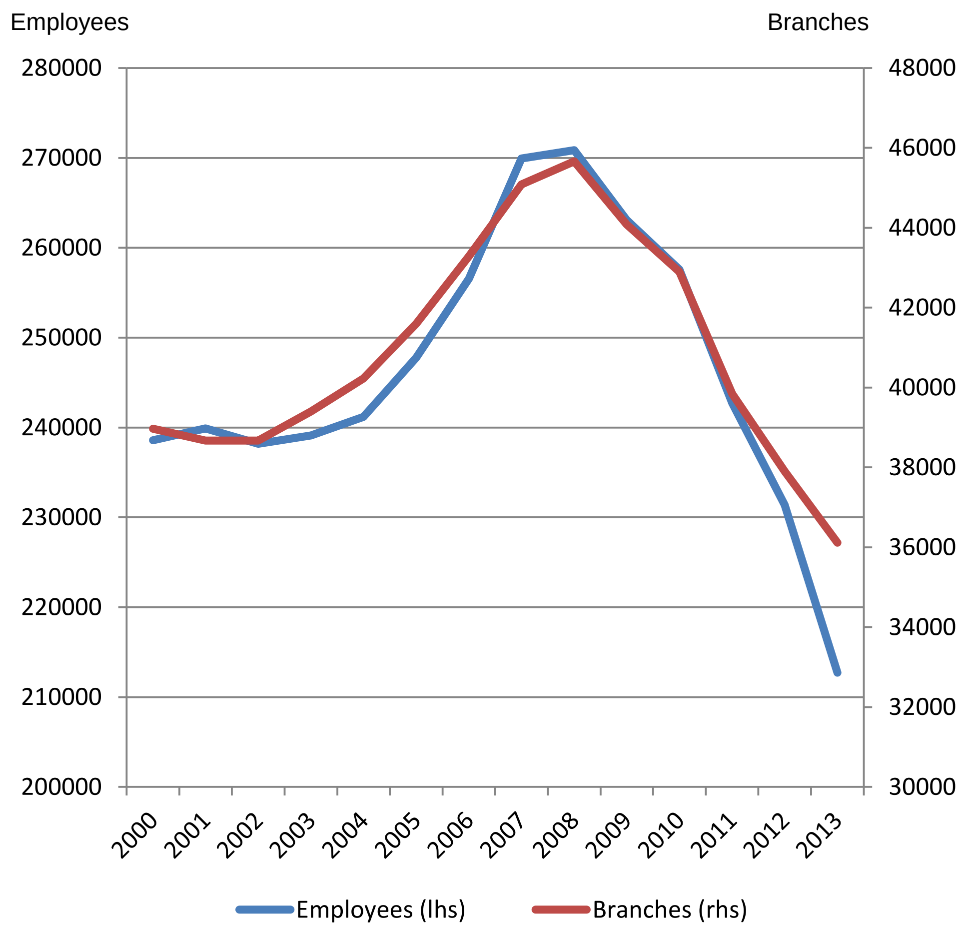
- Bank of Spain has developed a new supervisory tool, the *Forward Looking Exercise on Spanish Banks*, to gauge their solvency in different stressed scenarios
  - The tool adds to the enhanced transparency of the banking system and has received input from independent evaluators
- Main findings (November 2013): the solvency of Spanish banks is comfortably above regulatory capital requirements
  - Even on the worst case scenario projected for 2013-15
    - Expected losses will be fully covered with exiting provisions and operating profits
    - CET1 ratios will be above 10% in 2015

Source: Bank of Spain.

A significant Capacity Adjustment has already occurred

Sharp reduction in number of branches and number of employees in the financial sector

Adjustment in Deposit Taking Institutions



- The Spanish financial sector has wound down most of the excess capacity built up during the housing boom
  - 20% reduction in employees and in number of branches from the peak in 2008
- The recapitalisation exercise entails further downsizing, with marked increases on the efficiency ratios of the sector
- Sizeable reduction in the number of institutions
  - Total number has decreased from 50 in 2009 to 12 in 2012
  - Former saving banks model from 45 to 7 entities that have been transformed into banks
- Legislation to improve, strengthen and clarify the governance structure of former savings banks and of commercial banks controlled by them

Source: Bank of Spain.

Far Reaching Structural Reforms

An ambitious reforms agenda

The 2012 set of reforms aimed at increasing the flexibility and competitiveness of the Economy

2012

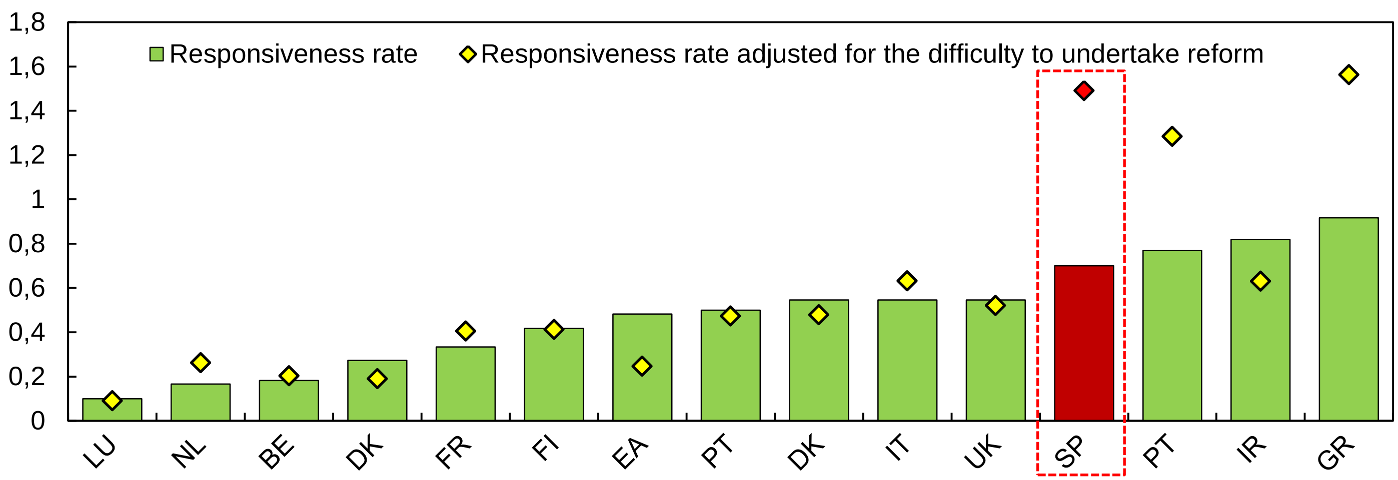
Labour Market Reform

- Objective: to foster wage moderation and job creation
- Firm-level wage bargaining prevails over national, regional or sector agreements
- Collective dismissals without administrative authorization are allowed for firms posting falling profits for three or more consecutive quarters. Convergence of dismissals costs with the EU average
  - Unjustified dismissal: severance pay of 33 days per year worked up to 24 months
  - Justified dismissal: severance pay of 20 days per year, up to 12 months
- Clarification of objective causes for justified dismissals
- Creation of a new permanent contract directed at SMEs

Other Structural Reforms

- Retail sector: liberalization of opening hours and elimination of restrictions on sale activities
- Liberalization of the Housing rental market
- Health and Education. Streamlining and cost reduction in order to increase efficiency

Recognized strong implementation record of structural reforms



NOTE: Higher number = stronger commitment. Source: OECD

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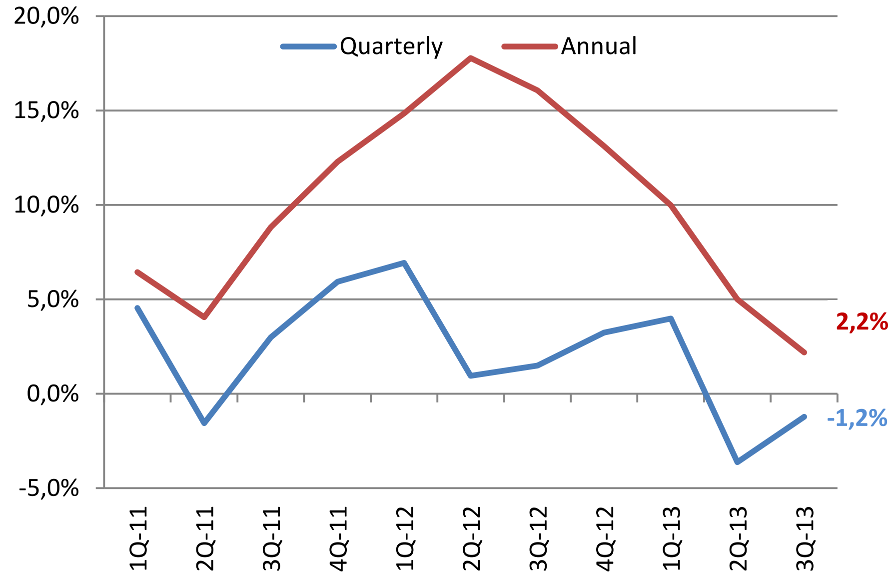
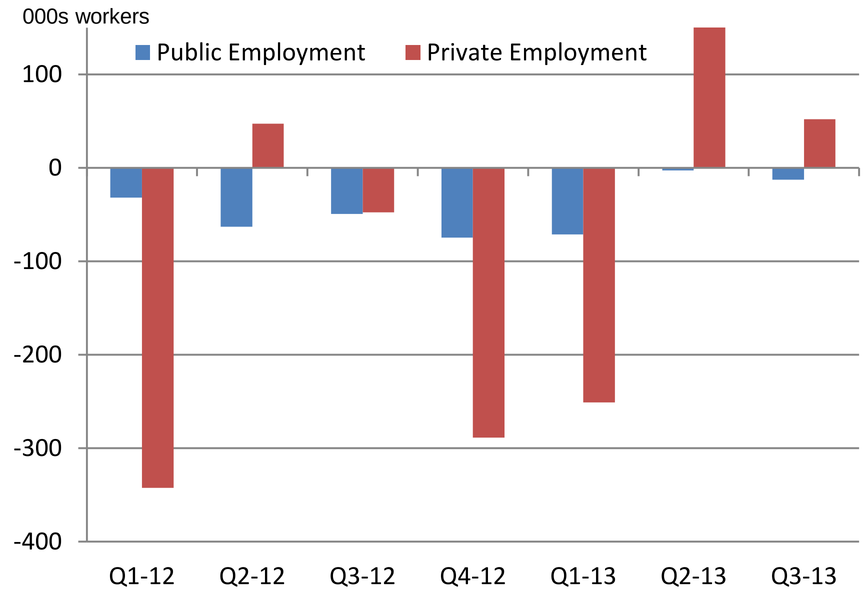
Stabilisation of labour market dynamics

Change in unemployment (%, y-o-y, q-o-q)



Quarterly change in employment



- Data from the latest Labour Force Survey (Q3 2013) indicates that:
  - ➢ Employment in the private sector has increased by over 200,000 in the last two quarters
    - ✓ The largest increase in private sector employment since 2007
  - ➢ Unemployment has fallen by almost 300,000 in the last two quarters.
    - ✓ The decrease in Q2 was the single second largest quarterly decrease since records are kept
    - ✓ The decrease in Q3 has been the best figure for a third quarter since 2005 (when Spain was growing close to 4%)
- After this reform, the Spanish economy will create employment with GDP growth rates of around 1%-1.2%, according to the Ministry of Economy's own estimates. Significantly below the figure before the reform, which was above 2%

SOURCE: Labour Force Survey, INE

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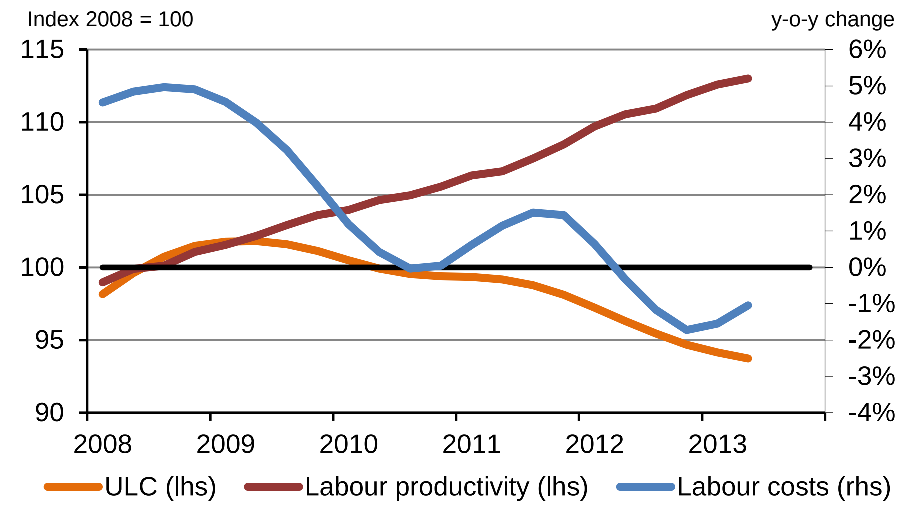
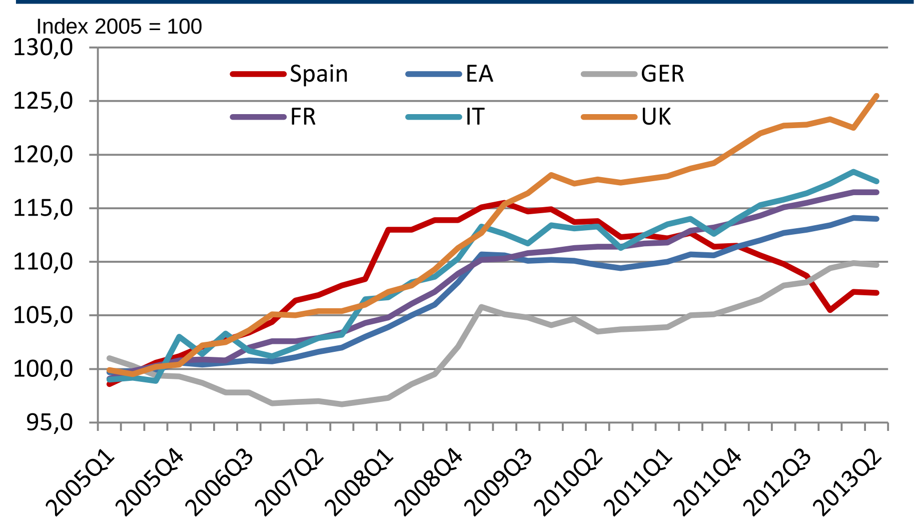
Increased Competitiveness and Declining Labour Costs

- Total labour costs in 2012 dropped by 0.6%, compared to the 1.2% increase registered in 2011
  - The trend in 2013 continues with a 0.3% decrease in Q2
- Wage costs, which had been moderating since the labour market reform was implemented, fell by 0.6% in Q2-13
- This has had a positive effect on unit labour costs which have been on a downward trend since 2009
- The declining unit labour costs are boosting competitiveness
  - ULCs have decreased by 3.0% in 2012. So far in 2013 they are falling by 2.6% y-o-y

Unit Labour Costs & Productivity and Labour Costs



Evolution of ULCs in the largest European economies



Source: Eurostat; Ministry of Economy and Competitiveness.

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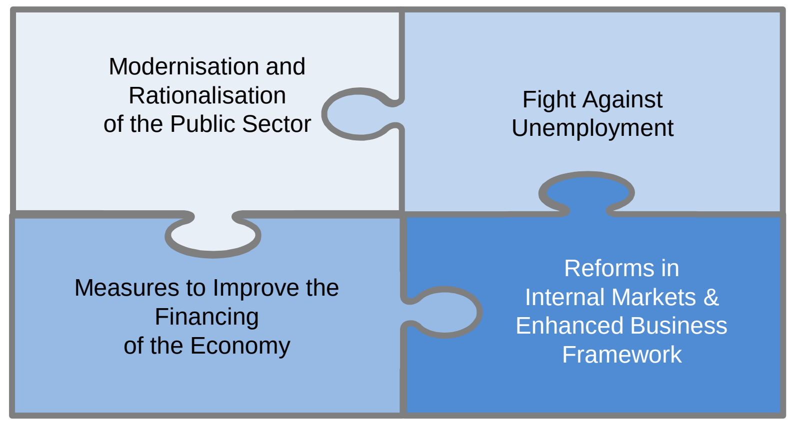
The Reforms Programme goes on

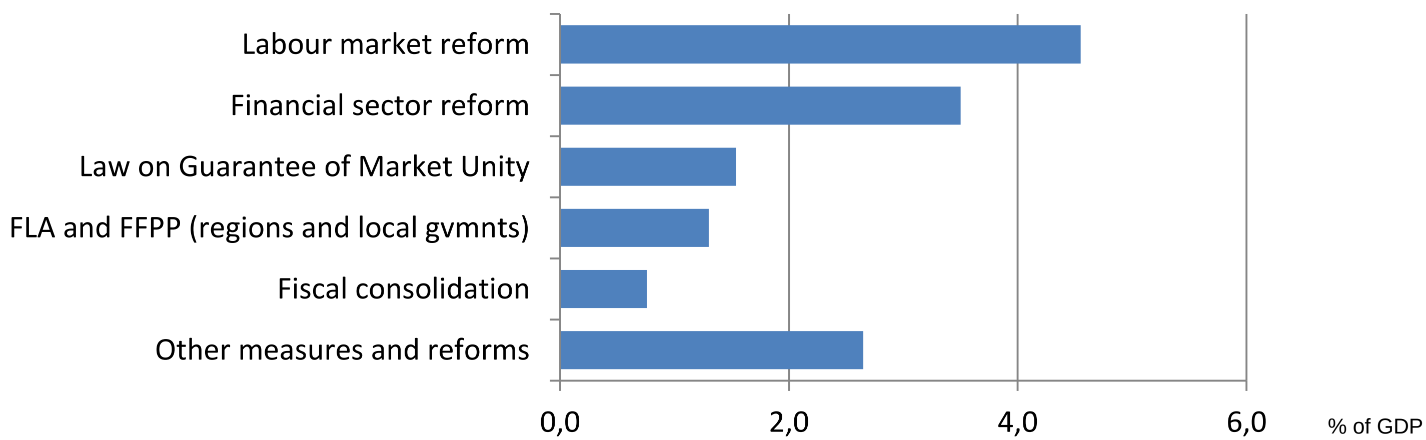
- The National Reforms Programme details the structural reforms road-map and aims to increase the flexibility and competitiveness of the Spanish economy

2013

National Reforms Programme



Over the next 10 years, the impact of the structural reforms (NRP 2013) is expected to exceed 14 p.p. of GDP



Source: Ministry of Economy.

Modernization and Rationalization of the Public Sector

Improved governance practices

- Law of Transparency, Access to Public Information and Good Governance of all Public Administrations
- Creation of the Independent Authority of Fiscal Responsibility which shall ensure the compliance of the principle of Budgetary Stability at every level of the Administration.
  - To be set-up before year-end 2013.

Draft Law on the rationalization and sustainability of the local administrations

- The Law will focus on the structure of the local administration, targeting fiscal balance, greater efficiency and the professionalization of the political and administrative functions.
- Four main objectives:
  - To clarify local responsibilities in order to avoid duplicities and overlaps,
  - To rationalize the organizational structure,
  - To ensure financial and fiscal discipline, and
  - To promote a business friendly regulation

Measures to improve the financing of the economy

- A number of measures have been launched to mitigate the effects of credit restriction and to increase the range and flexibility of the financing sources available to companies, with particular attention to companies in internationalisation stages and SMEs

- Main measures:
  - Securities markets: launching an alternative fixed income market (MARF), decreasing administrative burdens in security issuances, facilitating the movement between alternative (MAB) and organized stock markets
  - Venture capital: reform of the Law of Venture Capital entities, launching of FOND-ICO Global and the National Network of Business Incubators, reinforcement of business angels
  - Modification of the Insolvency Law.
  - Banking Channel: ICO lines (€ 22 bn), commitment by banks to increase SME financing by € 10bn in 2013
  - Loan Guarantees: reinforcement of the mutual guarantee system, CESCE line, ICO-CAF facility

New Law on the Financial Sector (Q4-13)

- Review of the regulations of private equity practices / markets
- Risk weighting for SME loans
- 3-month notice period for reductions in credit
- Introduction of regulation for innovative financing instruments (e.g. *Crowdfunding*)

Fight against unemployment

Reform of active labour market and improvement of the employability and skills of the unemployed

- Plan of Employment Policies 2013 (Q2)
- Pluri-annual Strategy for Employment Activation 2014-2016 (Q4 2013)
- Implementation Strategy of the dual vocational training system (2013-2015)
- Entrepreneurship and Youth Employment Strategy 2013-2016
- Reform of certificates of professional competence
- New management system of unemployment benefits
- Creation of a Single Gateway for Employment and improvement of public-private partnerships

Reforms in Internal Markets and Enhanced Business Framework

Law on Entrepreneurial Support and Internationalization

- Supports a favorable environment for entrepreneurs and the development and internationalization of companies
  - Entrepreneur of limited liability
  - Less red tape: setting up of limited liability companies without public deeds in 24 hours and reduced bureaucratic procedures through “Access Points for the Entrepreneur”
  - Fostering “second chances”: out-of-court resolution mechanisms
- Fiscal support for entrepreneurs:
  - Cash VAT
  - New tax deductions: profit reinvestments, R&D+I, etc.
- Measures to improve entrepreneurship financing :
  - Fewer constraints to issue in the Alternative Fixed Income Market (MARF)
  - More flexible conditions for refinancing agreements
  - New financing instruments for the internationalization of companies
- Measures to spur entrepreneurial growth: elimination of binding municipal licenses and fewer obstacles for public tender participation
- Measures to foster the internationalization of the Spanish economy: fixed income instruments for internationalization, privatization of CESCE (Spain’s export-credit insurance agency), and trade finance facilities

Reforms in Internal Markets and Enhanced Business Framework (continued)

Law on the liberalization of Professional Services and Professional Organizations

- To remove unnecessary barriers to professional access and exercise, and to boost competitiveness. To reduce the number of regulated professions. Draft law approved on 2nd August

Law on Guarantee of Market Unity

- A new regulatory model based on the principles of free establishment and free movement of goods and services throughout the Spanish territory

Law on Des-indexation of the Spanish Economy

- To foster competitiveness by promoting indexation mechanisms other than the automatic indexation to the general CPI (January 2014)

Reform of the Energy Sector

- To achieve the long term sustainability of Spain's power system by anticipating economic, technological and demand changes, as well as increasing competition and the security of the supply
  - Measures to achieve a balance between revenues and costs of the electricity system

New Code of Corporate Governance

- To improve Spain's framework of corporate governance according to the highest international standards

Reactivation of the Residential Housing Market

- A new visa regime for non-residents to attract investments

Spain’s new economic growth model

Economic policy strategy is behind the on-going adjustment

Historical imbalances are being corrected continuously

		2011	2012	2013	
PUBLIC SECTOR	Public Deficit, excl. financial sector one-offs (% GDP)	9.07%	6.84%	-3.58% Q2	Control of public finances
LABOUR MARKET	Wage increase agreed in collective wage agreements (y-o-y change)	2.1%	1.2 %	0.58% Aug	Wage moderation and productivity
	Unit labour costs. Total economy (y-o-y growth)	-1.0%	-3.0%	-2.3% Q2	
	Productivity per employee. (y-o-y growth)	2.3%	3.3%	2.2% Q2	
	Total labour cost (y-o-y growth)	1.2%	-0.6%	-0.8% H1	
EXTERNAL SECTOR	Current account balance (% GDP)	-3.5%	-1.1%	0.6% Aug	Competitiveness, Product and geographical diversification
	Net Lending(+)/Borrowing(-) vs RoW (% GDP)	-3.0%	-0.6%	1.5% Aug	
	Exports of goods (y-o-y growth)	15.6%	3.8%	6.1% Aug	
	Trade balance (€ bn)	-42.3	-25.8	-4.1 Aug	
	Share of exports to Euro Area	53%	49%	48%	
	Share of exports to non Euro Area	47%	51%	52%	
	Trade balance with Eurozone (€ bn)	1.636	7.777	11.4	
FINANCIAL SECTOR	Provisions; Impairment losses on assets (€ bn)	125.3	192.6	190.5	Sounder and more solvent financial system
	Net equity, adjustments and provisions (€ bn)	363.4	405.2	424.4 Aug	
	Provision coverage over credits	7.0%	11.9%	2.8% Aug	
PRIVATE SECTOR DEBT	Gross debt. Non financial corporates and households (% GDP)	224%	214%	209% Q1	Deleveraging via debt reduction
	Gross debt. Non financial corporates (% GDP)	140.5%	132.7%	128.3% H1	
	Gross debt. Households. (% GDP)	83.6%	81.4%	79.9% H1	
HOUSING	Price of Housing per sq m (y-o-y growth)	1,702	1,531	1,482	Adjustment in housing market

Source: MINHAP, Banco de España, Spanish Customs, Ministerio de Fomento, Eurostat, INE.

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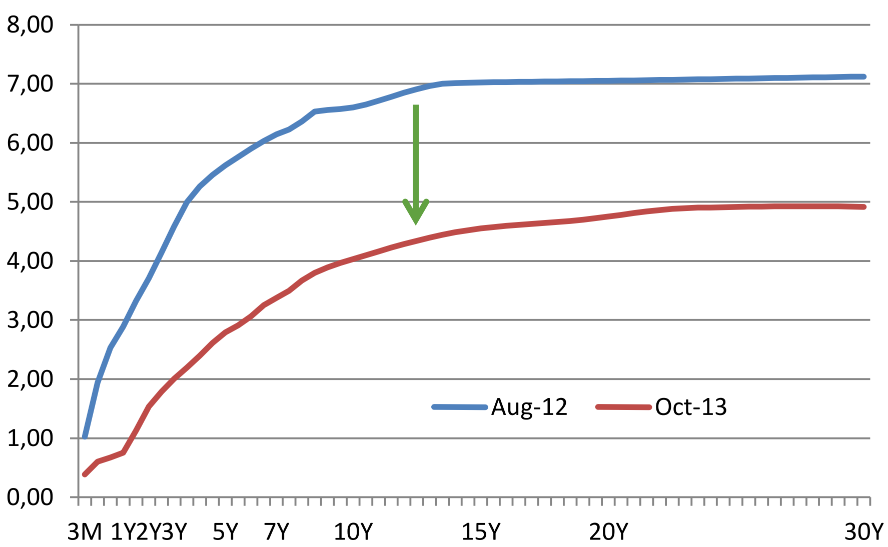
Macroeconomic and financial conditions have stabilized

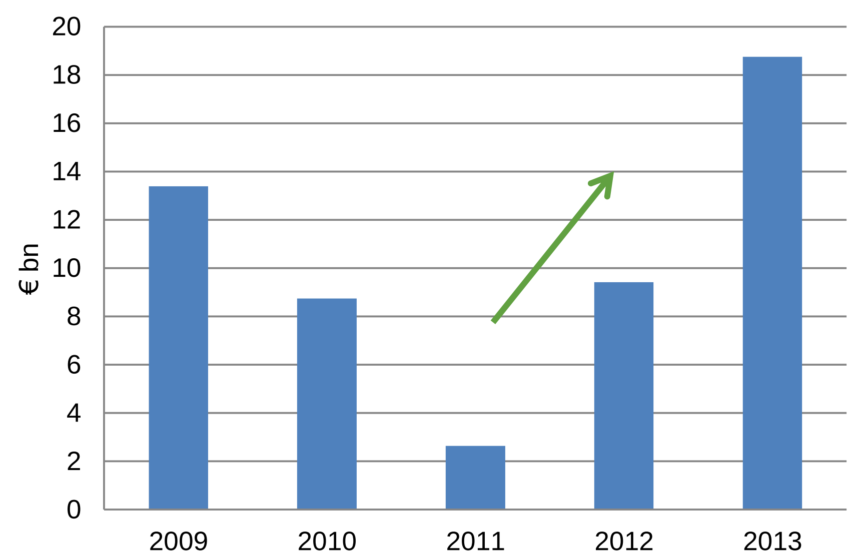
Improved sentiment visible across markets and asset classes

- Flow indicators are pointing to the right direction, this will enable the on-going correction of stock imbalances
- Imports of goods have grown so far in 2013 in real terms by over 2% against a 7% decrease in the first 3 quarters of 2012. This indicates that domestic demand is stabilising
- Inbound foreign direct investment (FDI) has increased considerably in recent months
- Improved confidence is visible in the debt markets since the summer of 2012 with a considerable decrease in financing costs for the Treasury
- Household and corporate deposits in financial institutions are in a positive trend as confidence in retail channels has improved

Changes in Spain's yield curve



FDI flows (January to August of each year)



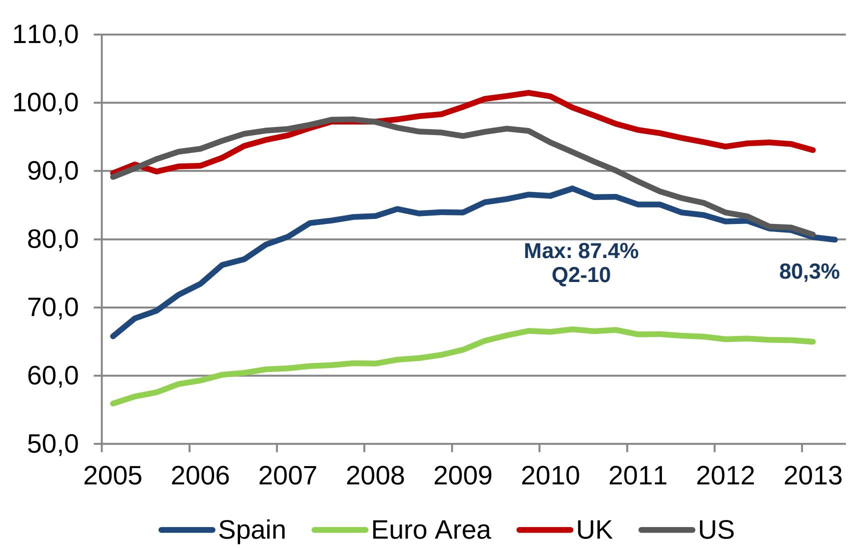
Source: Bank of Spain.

The Private Sector is Deleveraging at a Fast Pace

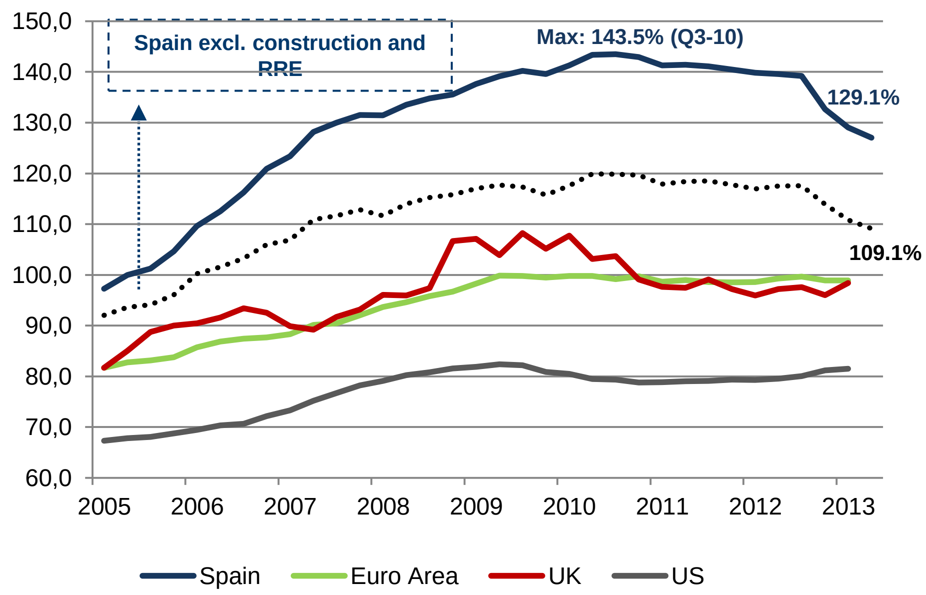
Resources redeployed away from construction and real estate and into healthier sectors

- Total private sector gross debt has fallen from 231.2% of GDP in June 2010 to 208.3% of GDP in Q2 2013
  - Both household debt and nonfinancial companies debt is significantly falling
  - Households' debt is in line with EU average, 80% of GDP
- The indebtedness of the construction and real estate companies explains most of the difference in the leverage ratios vs. other economies

Indebtedness Ratios of Households



Indebtedness Ratios of Non-Financial Corporations



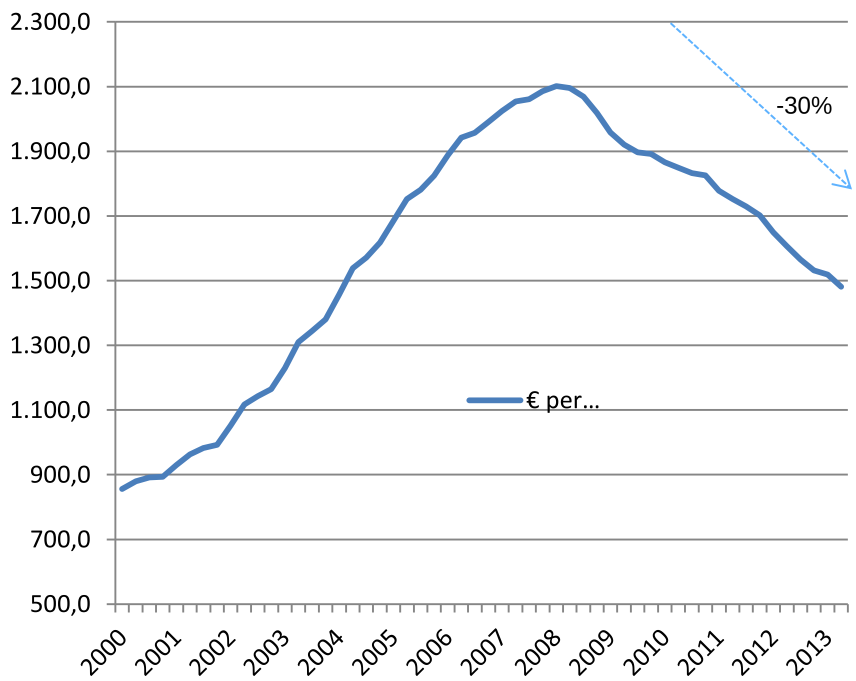
Source: Bank of Spain.

The Real Estate Sector has Accelerated its Adjustment

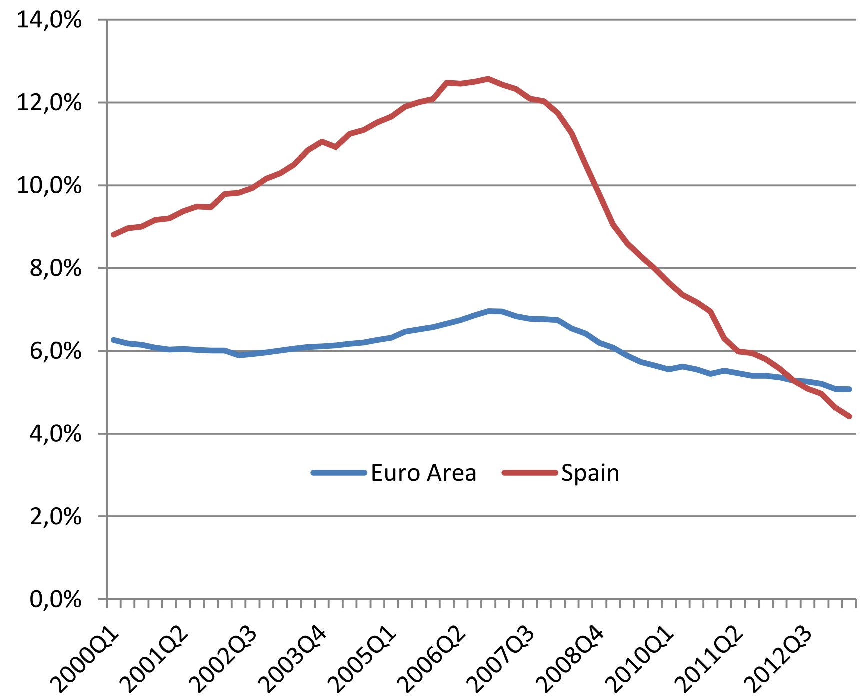
Real estate prices have already fallen by c. 30% from their peak

- The largest annual decrease so far occurred in 2012 with a correction in prices of nearly 10%
- On average, nominal house prices are at 2004 levels; adjustment more intense around most populated and coastal provinces
- Residential construction investment has declined sharply and is now below the Euro Area average
  - The contribution to GDP from residential construction will be less negative going forward

Housing prices declining



Investment in Residential Housing as % of GDP



Source: Ministerio de Fomento, Eurostat

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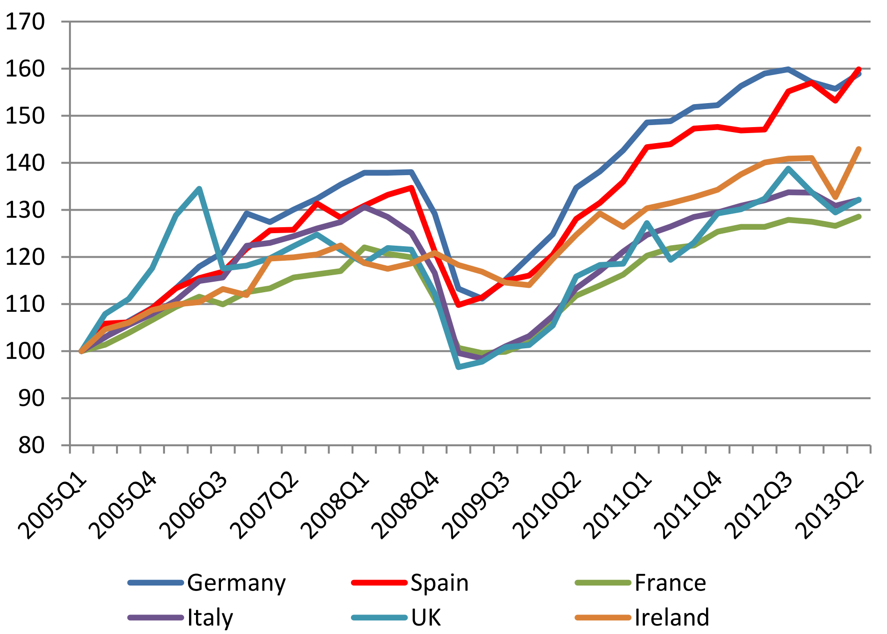
Strong performance of the External Sector

Wage moderation has resulted in a competitiveness based expansion of exports

- Despite the global economic slowdown, from January to September, exports of goods have increased by 7% in real terms (well above last year's increase during the same period; 1.6%)
- Exports of non-tourist services, mainly due to professional services and services to firms, have outpaced exports of goods and tourist services

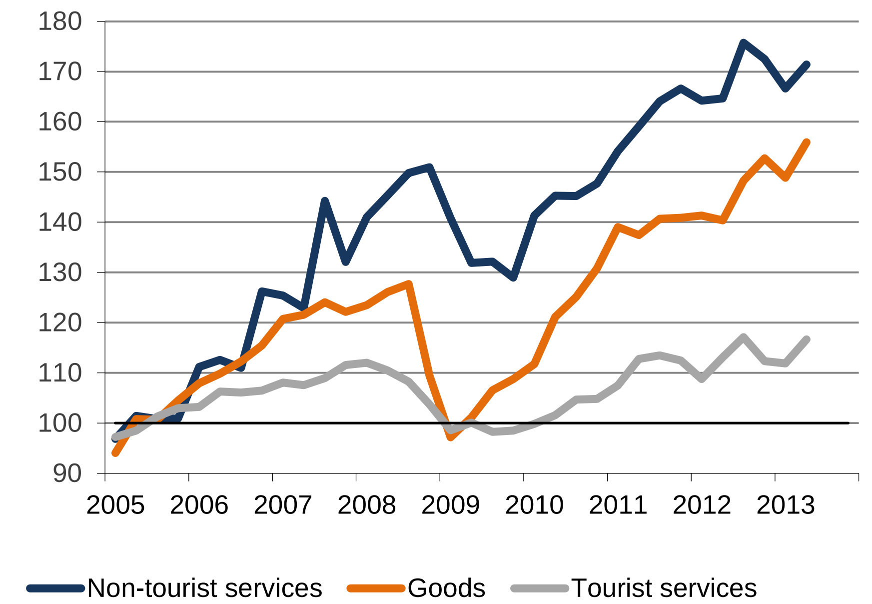
Exports of Goods and Services

Index, 2005=100



Breakdown of Exports of Goods and Services

Index, 2005=100



Source: Eurostat; Instituto Nacional de Estadística.

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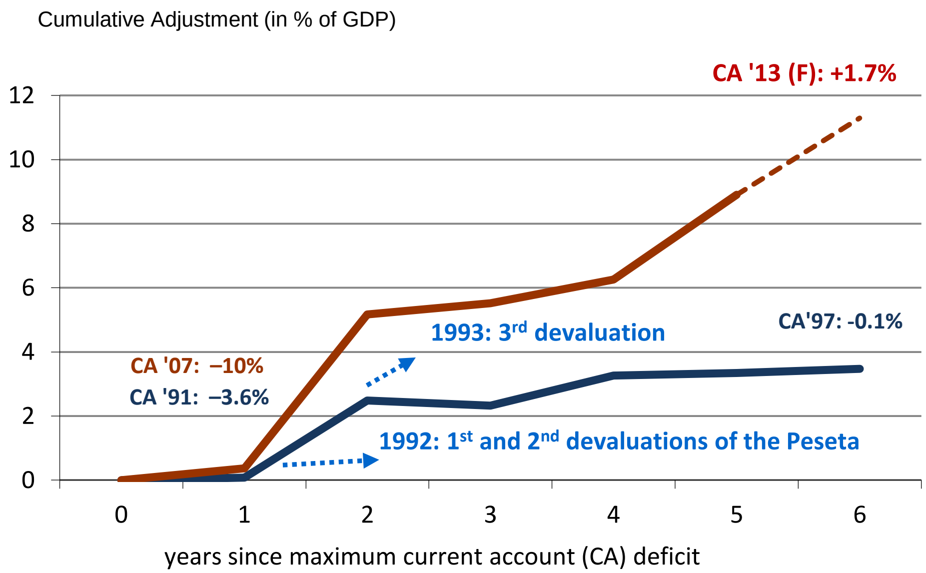
External Imbalances are being Corrected

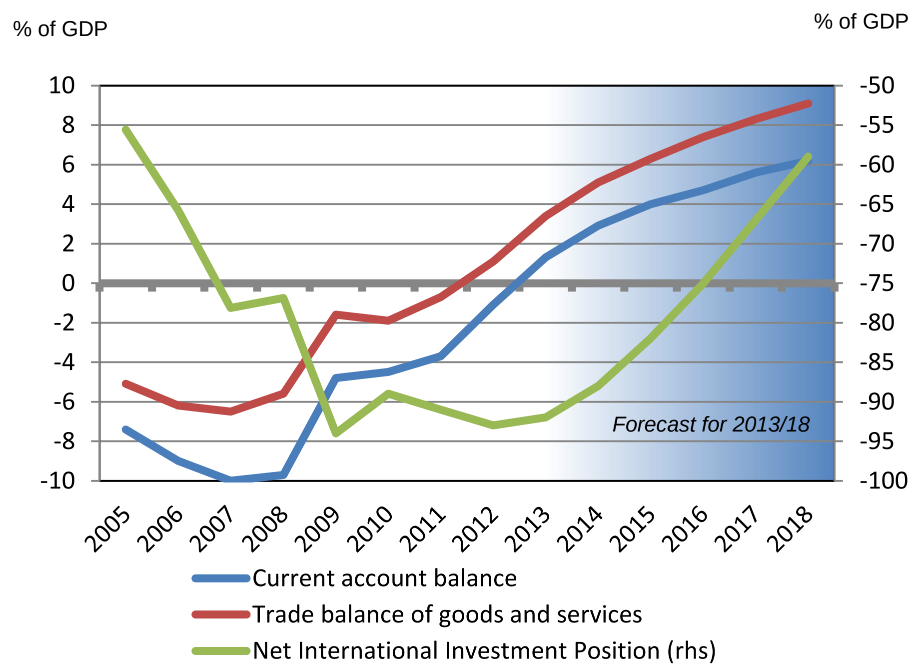
Spain will have a surplus in its current account by year-end 2013

- From 2007 to 2013 the adjustment in the current account will be of almost 12% of GDP
  - The Current Account is in surplus since H2-2012. This will enable Spain to decrease its net external indebtedness
- The correction in the current account is of a structural nature and is due to competiveness gains stemming from an internal devaluation. The adjustment is more sustainable than the one achieved by exchange rate devaluations in the ‘90s
- Product diversification and product quality have resulted in a higher resilience of exports to the economic cycle
  - Geographical diversification of goods exports: exports to non-EU economies account for more than 40%
  - Product diversification: the range of exports has increased particularly in higher value added goods and services

Current Account Balance and its Adjustment



Current Account Balance, Trade Balance, NIIP



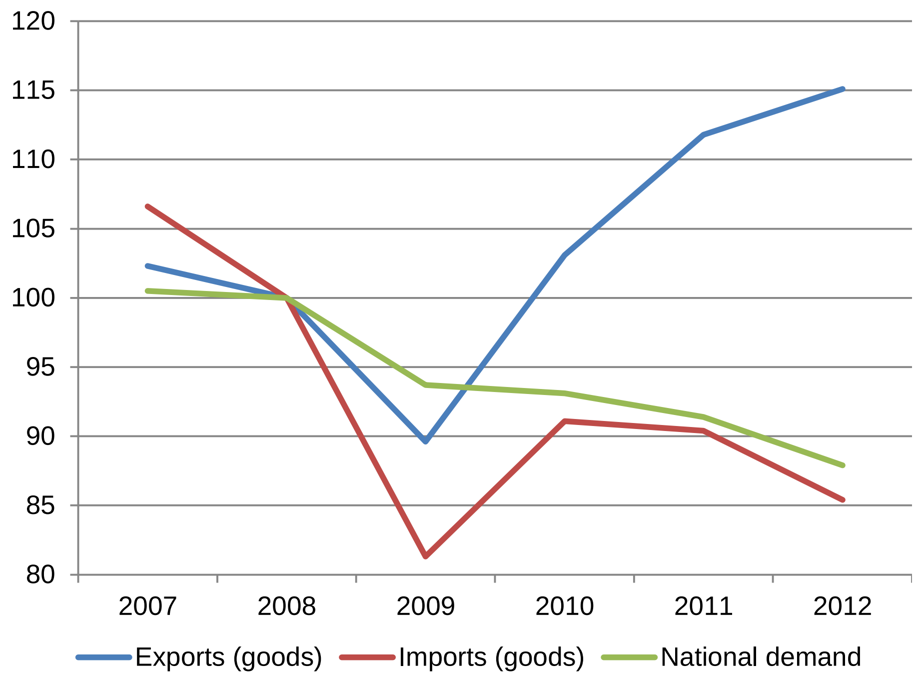
Source: Bank of Spain. European Commission, IMF

Export-led recovery supported by a structural correction in the current account

- While the 2009 correction in Spain's current account was due to a decrease in imports and in internal demand, the correction in 2012 and 2013 is mainly due to strong export performance
- Spain's exports now represent around 33% of GDP and the performance is amongst the best in the EU
- Spain is shifting away from domestic sources of growth and into and export-led model. Spain's new economic model prevents boom-burst cycles and makes credit fuelled housing and consumer booms unlikely to materialise any time soon

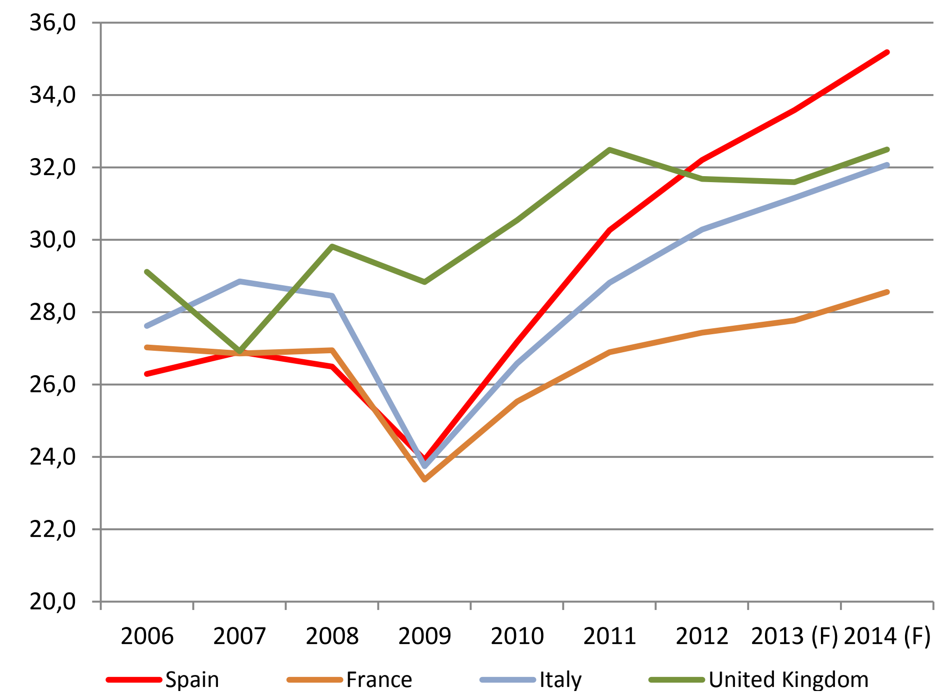
Evolution of Exports, Imports and National Demand

Index, 2008 = 100



Exports of goods and services in selected countries

% GDP



Source: Ministry of Economy and Competitiveness, Eurostat

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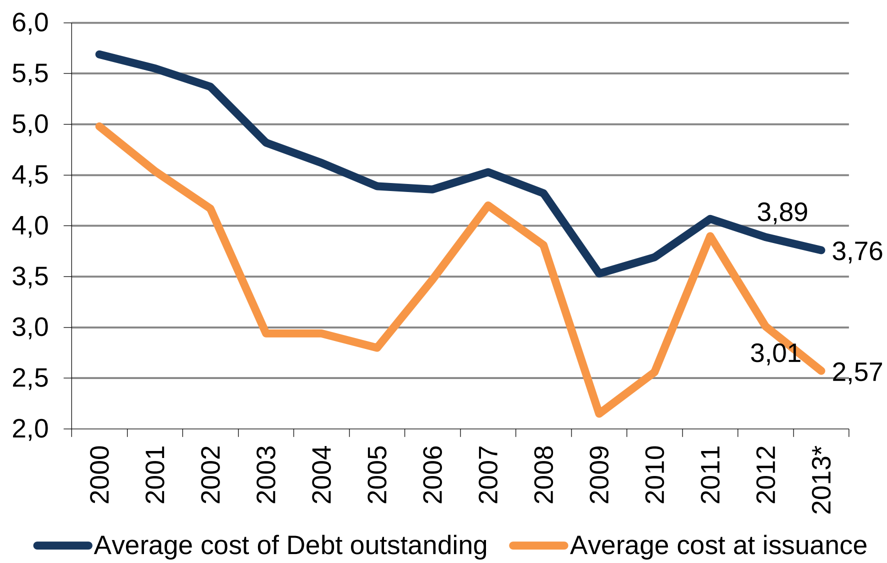
Appendix: Funding and Debt Management

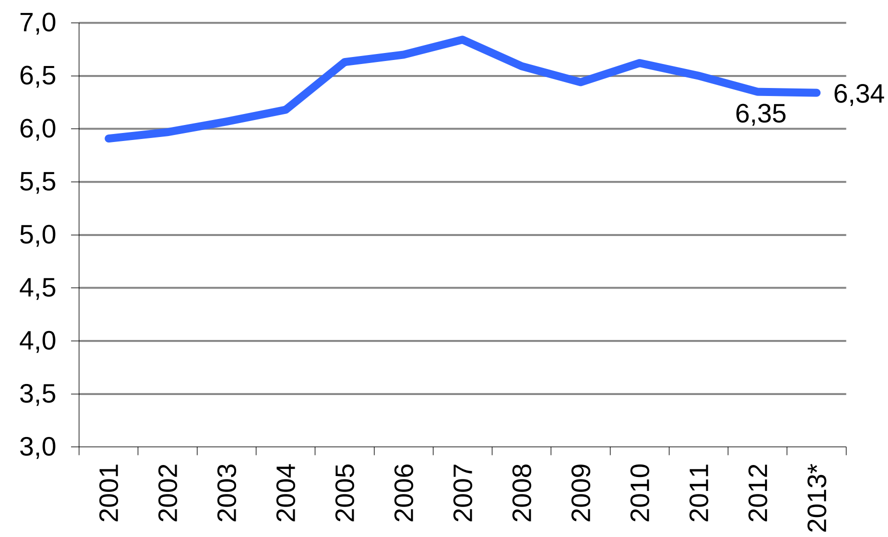
Financial flexibility and resilience during the crisis

- Despite volatility in European public debt markets, the Treasury is financing itself adequately. Average cost at issuance and average cost of debt outstanding at historically low levels
- Average life of the debt portfolio has declined in the last year, mitigated by the ESM loan (12.5 years average life) but at 6.3 years its remains longer than rating peers. This insulates against sudden increases in interest rates

Cost of Debt Outstanding and Cost at Issuance
(As of 31 October 2013, in %)



Average Life
(As of 31 October 2013, in years)



Source: General Secretariat of the Treasury and Financial Policy.

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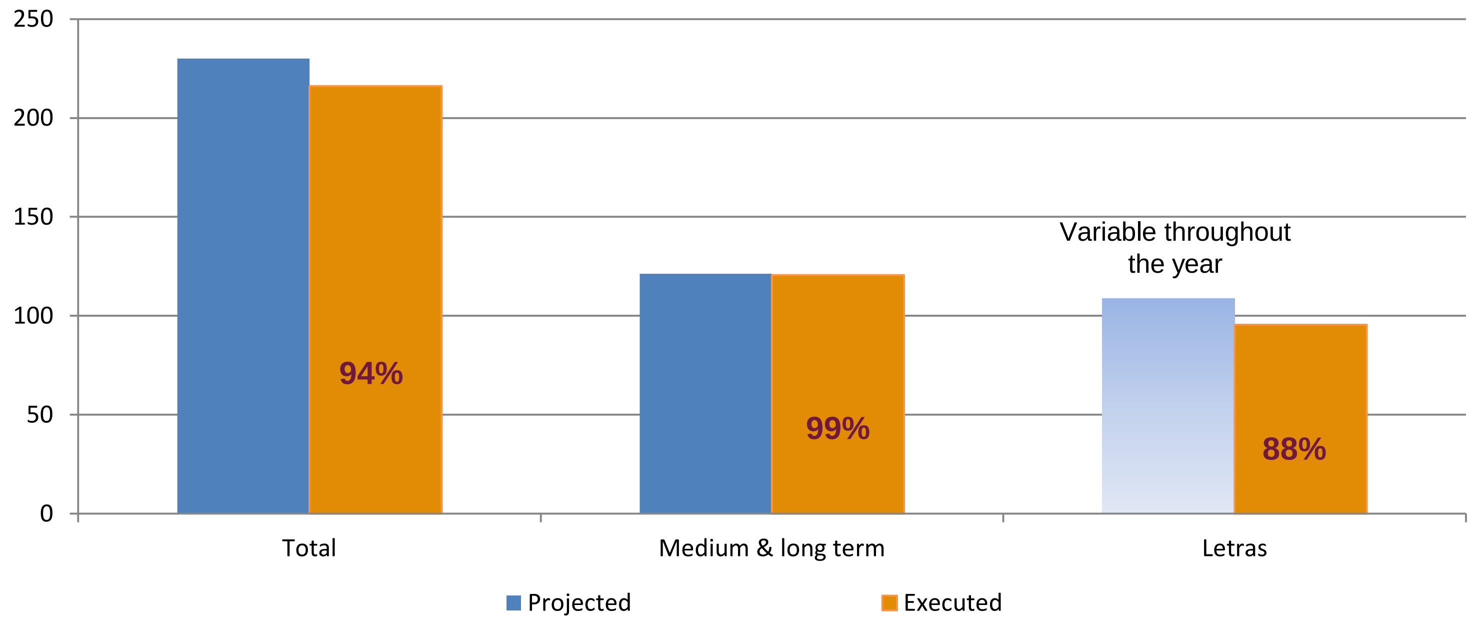
Funding programme for the virtually completed

- The Spanish Treasury has funded €120,6bn (99.4%) of the maximum expected amount of medium- and long-term gross issuance of €121.3bn
- Including T-Bills, the Spanish Treasury has issued €216bn so far in 2013, 94% of the overall programme

Funding Programme. 2013 *(Gross issuance, in billion Euros, as of 21 Nov 2013)*

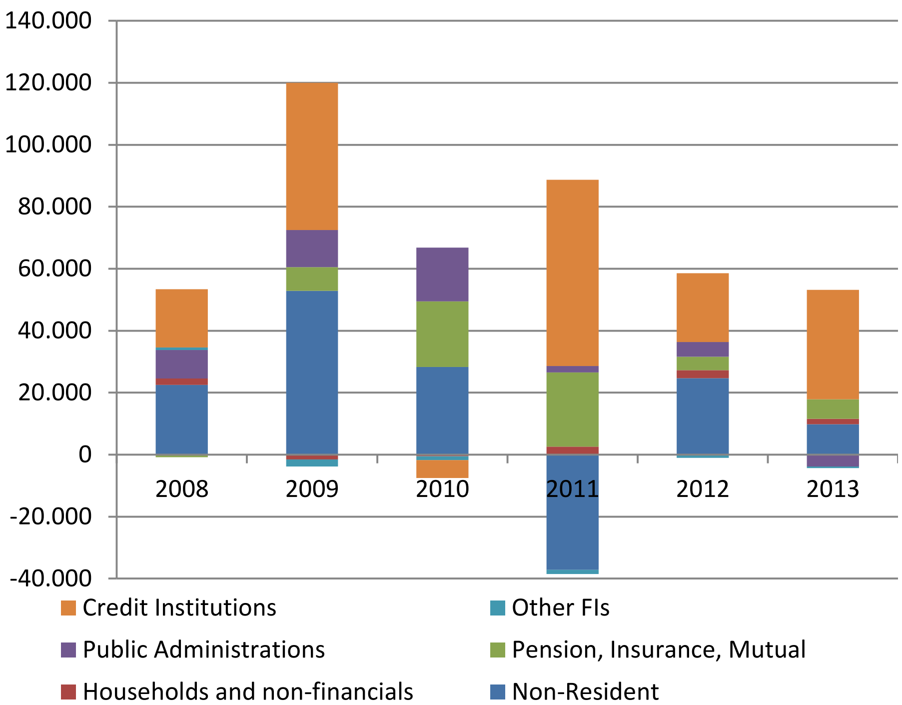


Source: General Secretariat of the Treasury and Financial Policy.

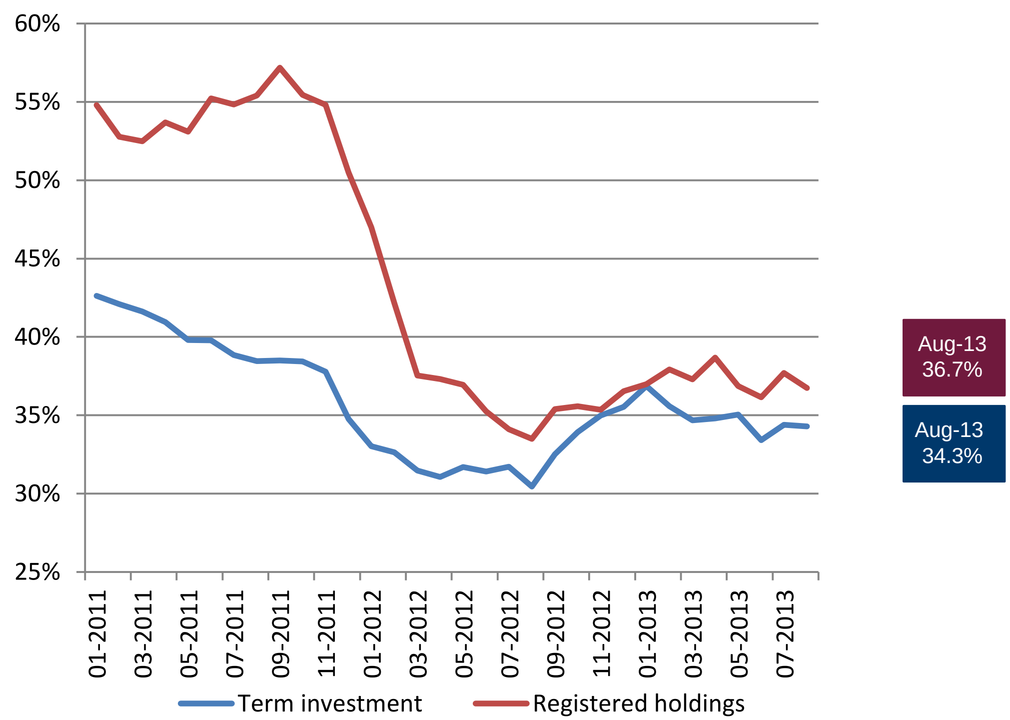
Non-resident demand has picked-up

- In contrast to the sharp decrease in registered holdings of bonds in the first half of last year, non-resident demand has picked up in recent months up €58.3bn vs. August 2012
- Up to August 2013, term investment of non-residents has stabilised and reaches €227.8bn

Change in Holdings of Non-Resident Investors (Term Investment. € bn)



Non-Resident Holdings of Unstripped Government Debt (As a % of total)

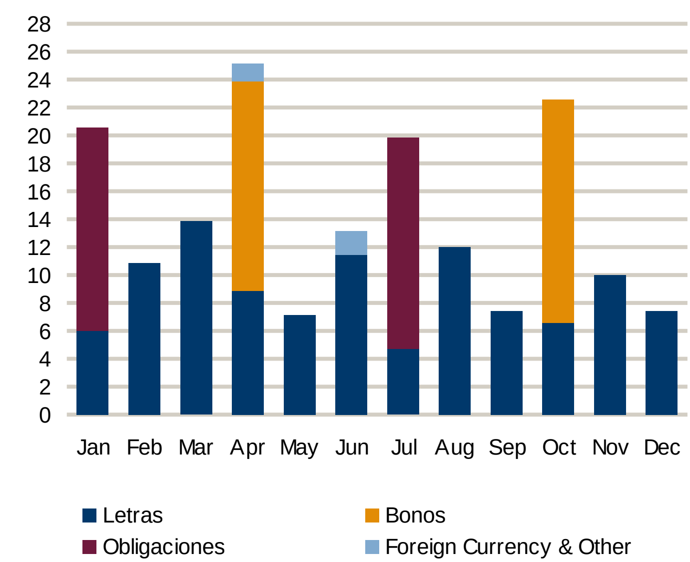


Source: General Secretariat of the Treasury and Financial Policy .
** As of 31st July 2013 / 31st August 2013.*

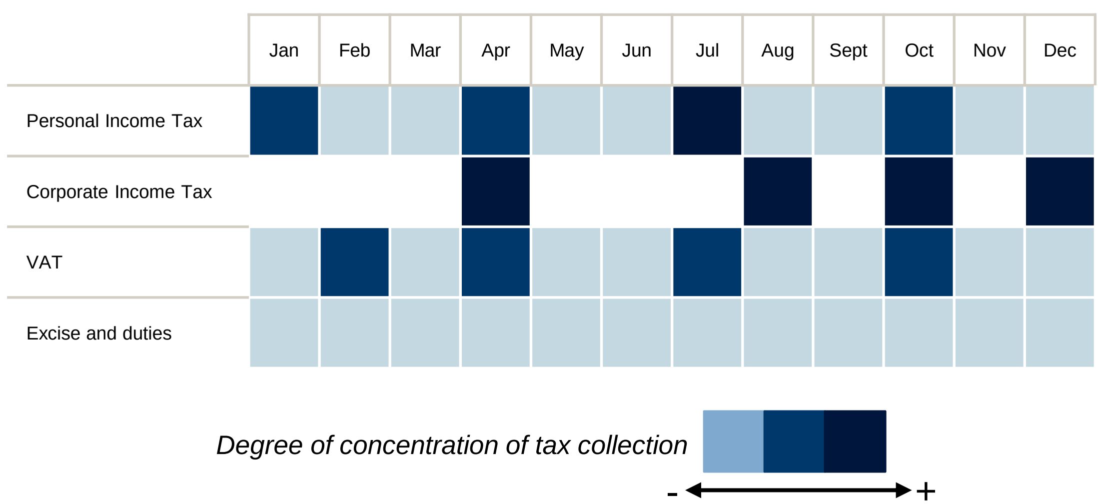
A Prudent Debt Management Strategy

- Redemption dates of medium- and long-term bonds (principal and coupons) match the biggest inflows of tax revenues
- Excess liquidity is lent in the money market each month through repo auctions
- Liquidity lines with banks provide an additional buffer

Monthly Debt Maturity Profile in 2013



Administrative Distribution of Tax Collection



Source: General Secretariat of the Treasury and Financial Policy .

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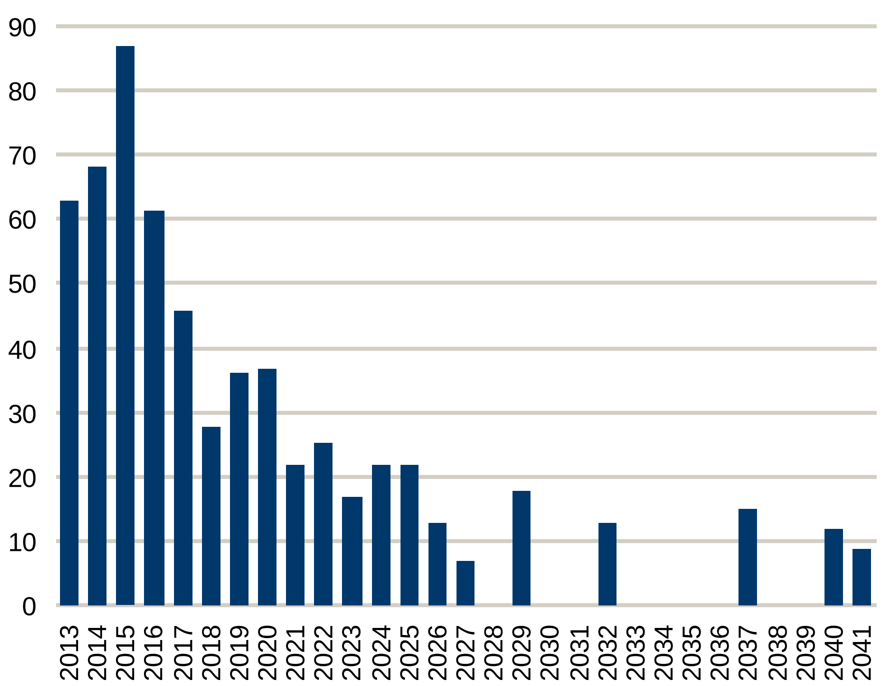
Risk and Refinancing Measures

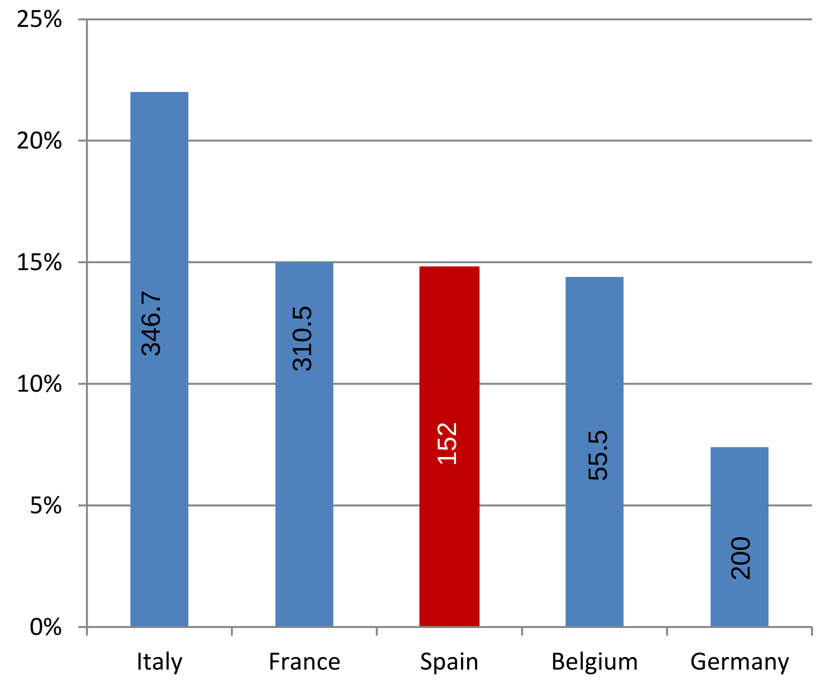
- Redemptions of Euro-denominated debt remain well in line with those of peers

Maturity Profile of Medium- and Long-Term Bonds (€ bn)



Source: General Secretariat of the Treasury and Financial Policy .

October 2013 to September 2014 Redemptions (Percentage of Estimated GDP 2013)



Source: Spanish Treasury for Spain, and Bloomberg for other countries.

Long 30-year Bono: €4bn, 5.15% due Oct-2044

Key summary details	
Amount:	€4.0bn
Issue date:	9-Oct-2013
Maturity date:	31- Oct- 2044
Coupon:	5.15%
Re-offer spread vs. ms:	+250bp
Re-offer yield:	5.213%

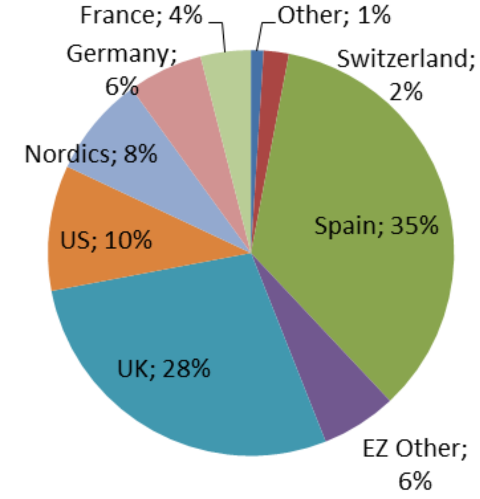
Spain's 2013 funding programme	
Total programme:	€230bn
Completed:	€191.2bn / 83%
Medium & long term programme:	€121.3bn
Completed:	€109.3bn / 90%

Over €10.6bn of investor demand

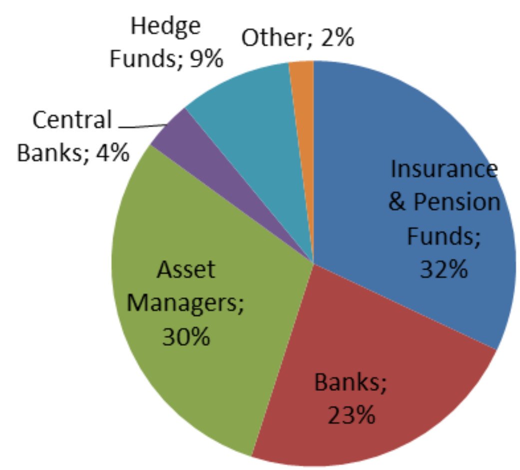
- On the 9th October 2013, Spain's Tesoro successfully priced its new long 30-year benchmark: €4bn size, 5.15% coupon, Oct-2044 maturity
  - The deal was priced with a small concession of 15bp vs the outstanding 2041 *Bono*
- This new issue is the Kingdom of Spain's first 30-year syndicated bond since September 2009.
  - The deal is the fifth syndicated transaction of the year, following two €7bn 10-year bonds in January and May, a USD2bn 5-year in February and a €3.5bn 15-year bond in July
- The new bond was officially announced on Tuesday 8th October and priced on Wednesday afternoon
- The orderbook for the transaction exceeded €10.6bn
- Over 230 investors participated in the transaction; 65% international
- With this syndicated transaction, **Spain has already completed over 90% of its medium- and long-term funding programme for 2013**

This new deal is Spain's comeback in the 30-year tenor. The bond further evidences that Spain has full market access to the long-end of the curve

Breakdown by region



Breakdown by investor type



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