CNMV

Comisión Nacional del Mercado de Valores

CNMV BULLETIN

Quarter IV

2008

CNMV Bulletin

Quarter IV
2008

The CNMV publishes this Quarterly Bulletin to spread studies in order to contribute to the best knowledge of the Stock Markets and their regulation.

The opinions in these articles are exclusively from the authors and they do not have to be attributed to the CNMV.

The CNMV distributes its reports and publications via the Internet at www.cnmv.es

Publishing advice of the Quarterly Bulletin of the CNMV: Fernando Restoy (CNMV), Vicente Salas (Universidad de Zaragoza), Belén Villalonga (Harvard Business School) and Nieves García Santos (CNMV).

ISSN: 1988-253x

Table of contents

Acronyms

ACGR	Annual Corporate Governance Reports
AIAF	Asociación de Intermediarios de Activos Financieros/Spanish Brokers' Association
ASCRI	Asociación Española de Entidades de Capital-riesgo/Spanish association of venture capital firms
BME	Bolsas y Mercados Españoles
CEBS	Committee of European Banking Supervisors
CESR	Committee of European Securities Regulators
CNMV	Comisión Nacional del Mercado de Valores
DAC	Directive on Capital Requirements
DSI	Directive on Investment Services
EBITDA	Earnings Before Interests, Tax, Depreciation and Amortization
EC	European Commission
EFAMA	European Fund and Asset Management Association
ESI	Investment services company
ETF	Exchange Traded Funds
EU	European Union
EVCA	European Private Equity & Venture Capital Association
FIAMM	Money market fund
FIM	Securities investment fund
FRA	Forward Rate Agreement
GDP	Gross Domestic Product
IGBM	Índice General de la Bolsa de Madrid/Madrid Stock Exchange General Index
IIC	Collective Investment Schemes
IOSCO	International Organization of Securities Commissions
IPO	Initial Public Offerings
LMV	Ley del Mercado de Valores/ Securities Markets Law
MAB	Mercado Alternativo Bursátil/Alternative Stock Market
MEFF	Mercado Español de Futuros y Opciones Financieros/Spanish market in financial futures and options
MFAO	Mercado de Futuros del Aceite de Oliva/Olive oil futures market
MiFID	Markets in Financial Instruments Directive
OECD	Organization for Economic Co-operation and Development
PER	Price Earnings Ratio
RD	Royal Decree
RDL	Royal Decree Law
ROE	Return On Equity
SENAF	Sistema Electrónico de Negociación de Activos Financieros/An electronic trading platform for Spanish public debt
SGIIC	Collective investment scheme management company
SIBE	Sistema de Interconexión Bursátil Español/Spanish electronic market
SICAV	Open-end investment company
UCITS	Undertakings for Collective Investment in Transferable Securities

I Market survey (*)

(*) This article has been prepared by staff of the CNMV Research, Statistics and Publications Department.

1 Overview

Salient developments in the year's second half[1] were the gathering worldwide slowdown and the September collapse of several North American institutions, adding a new twist to the financial crisis. The deceleration in output, which in some leading industrialized economies has already hardened into recession, has been accompanied by a sharp upswing in unemployment and, in recent weeks, the easing of inflationary pressures as crude prices trend lower. The international financial crisis took a new turn for the worse last September with the failure of various North American institutions. Not only was government intervention called for in some cases, but concerns were voiced about the very sustainability of the financial system. Leading central banks reacted to this renewed instability with cash injections and substantial cuts in leading interest rates. At the same time, almost all the developed countries launched a battery of action plans to ensure the stability of their national financial systems and protect both the credit cycle and the real economy.

Against this backdrop, short-term rates began to escalate in main economic areas, after a relative settled third-quarter period, as far as record highs around mid-October. However, official rate cuts in Europe and the United States prompted a renewed run-down which eased tensions on interbank markets. Meantime, long government yields headed gradually lower in Europe, the United States and Japan, more intensely in the closing quarter in tune with shifting expectations for official rates. Credit risk indicators revealed an across-the-board increase in its market price, somewhat sharper in the U.S. than in the euro area, which bore little relation to issuers' credit quality.

Currency markets were also prey to heightened volatility in the year's last months. The yen chalked up major gains against both the U.S. dollar and the euro due to the unwinding of carry trade positions. And the dollar too staged a strong second-half comeback as expectations grew of rate cuts in the euro area.

Main stock market indices registered record losses in the third and fourth quarters of 2008. Equity prices on almost all leading developed-world bourses closed more than 40% down on their start-out levels, while in some emerging economies the year-long fall exceeded 60%. In parallel, stock market volatilities climbed to unprecedented heights (between 70% and 80%), and have only now begun to die down slightly. Price-earnings ratios (P/E), meantime, continued their descent on all world exchanges.

These trends were more or less mirrored in Spain with a few local exceptions. On the growth score, the announcement of the first quarterly decline in GDP (for the third quarter of 2008) was only the beginning, and the latest indicators point to a

1 The closing date for this report is December 15. Figures for the fourth quarter of 2008 or the full-year period are accordingly up to that date unless otherwise indicated.

more profound downturn in economic activity which will likely be accompanied by faster rising unemployment and lower inflationary pressures.

Finally, after the government's approval of a series of measures to ensure the stability of the financial system, main equity and bond market indicators have performed in line with other international benchmarks. Interest rates fell significantly in the year's closing quarter in both short- and long-term debt markets, reflecting both revised expectations for ECB monetary policy and the easing of inflation. The other salient development was the rise in credit risk premiums affecting both corporate and government issuers. Equity markets, meantime, have posted year-long losses of over 40%, compounded by an unprecedented upswing in volatility. Most heavily penalised were the financial sector and other sectors exposed directly to housing investment. Electronic market turnover, which had trended lower all year in line with prices, stabilised in the closing quarter, allowing the year to end on a more dynamic note in volume terms at least.

Summary of financial indicators

TABLE 1

	Q1 08	Q2 08	Q3 08	Q4*08
Short-term interest rates (%)[1]				
Official interest rate	4.00	4.00	4.25	2.50
Euribor 3 month	4.74	4.94	5.02	3.52
Euribor 12 month	4.73	5.35	5.38	3.67
Exchange rates[2]				
Dollar/euro	1.42	1.58	1.43	1.35
Yen/euro	163.55	166.44	150.47	122.42
Credit risk premiums: BBB-AAA spread (basis points)[3]				
Euro area				
3 year	32	109	139	288
5 year	45	143	183	320
10 year	71	175	191	306
U.S.				
3 year	70	191	227	297
5 year	80	234	265	288
10 year	98	228	283	314
Equity markets				
Performance of main world stock indices (%)[4]				
Euro Stoxx 50	-17.5	-7.6	-9.4	-20.8
Dow Jones	-7.6	-7.4	-4.4	-21.1
Nikkei	-18.2	7.6	-16.5	-23.0
Other indices (%)				
Merval (Argentina)	-2.2	0.2	-24.2	-30.2
Bovespa (Brazil)	-4.6	6.6	-23.8	-22.6
Shanghai Comp (China)	-34.0	-21.2	-16.2	-14.4
BSE (India)	-26.2	-14.6	-4.8	-25.1
Spanish stock market				
Ibex 35 (%)	-12.6	-9.2	-8.8	-17.9
P/E of Ibex 35[5]	11.55	10.35	9.57	8.21
Volatility of Ibex 35 (%)[6]	31.19	22.98	31.26	63.25
SIBE trading volumes[7]	6,144.1	4,953.9	4,334.3	4,437.6

Source: CNMV, Thomson Datastream, Reuters, Banco de España, Bolsa de Madrid, MEFF and AIAF.

* Latest available data at the time of preparing this report.

1 Monthly average of daily data. The official interest rate corresponds to the marginal rate at weekly auctions at the period close. Data for the fourth quarter correspond to the average from 1/12 to 15/12.

2 Data at period end. Data for the fourth quarter of 2008 correspond to 15 December.

3 Monthly average of daily data. Data for the fourth quarter 2008 run from 1/12 to 15/12.

4 Cumulative quarterly change in each period; up to 15 December in the case of the fourth quarter.

5 Price-earnings ratio. Data for the fourth quarter 2008 correspond to 15 December.

6 Implied at-the-money (ATM) volatility on nearest expiry at period end. Data for the fourth quarter 2008 correspond to 1 October to 15 December.

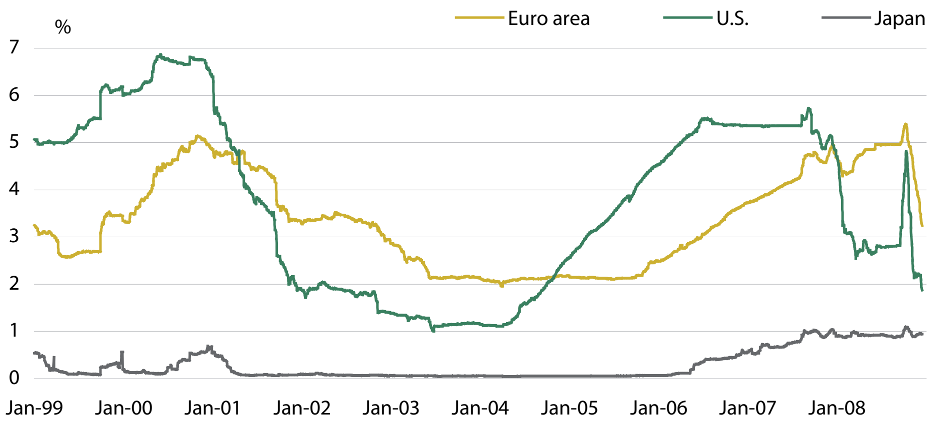
7 Daily average in million euros. Data for the fourth quarter 2008 correspond to the period to 30 November.

2 International financial background

2.1 Short-term rates

World money markets managed a fairly even third-quarter performance until the month of September, when the failure of major U.S. financial institutions forced a number of official bail-out operations and sowed widespread unease about the stability of the financial system. Short-term rates moved sharply higher in main world zones, especially the United States, until the mid-October announcement of a string of government measures and action plans and, above all, coordinated action by the central banks, which stepped in with new liquidity injections and leading rate cuts, set money-market rates on a renewed downward course.

Three-month interest rates[1] FIGURE 1



Source: Thomson Datastream.

1 Data to 15 December.

The ECB, which as recently as July had hiked its main refinancing rate from 4.0% to 4.25% to stave off inflation, announced three successive cuts (one in coordinated fashion with other central banks) which lowered it to 3.75% in October, 3.25% in November and 2.5% in the month of December. These moves were a response to the worsening financial crisis, the downturn in activity and the improved outlook for inflation with crude prices progressively softening. In interbank markets, rates began to fall a few days after the official cut, and though it would be untrue to say that things are back to normal, the tensions are appreciably less. This calmer mood is evidenced by the large drop in spreads between non transferable deposits and repos (on medium and long bonds) as of their mid-October peak, though note that the level remains high[2].

2 The mid-December spread at the three-month maturity was around 120 basis points (compared to the high of 184 basis points registered in mid-October).

Short-term interest rates [1]

TABLE 2

%	Dec 04	Dec 05	Dec 06	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08[2]
Euro area								
Official [3]	2.00	2.25	3.50	4.00	4.00	4.00	4.25	2.50
3 month	2.17	2.47	3.69	4.84	4.59	4.94	5.02	3.52
6 month	2.21	2.60	3.79	4.81	4.59	5.08	5.22	3.59
12 month	2.30	2.79	3.93	4.79	4.59	5.35	5.38	3.67
U.S.								
Official [4]	2.25	4.25	5.25	4.25	2.25	2.00	2.00	1.00[6]
3 month	2.50	4.49	5.36	4.97	2.78	2.76	3.11	2.11
6 month	2.72	4.67	5.35	4.82	2.68	3.09	3.33	2.47
12 month	3.02	4.84	5.24	4.42	2.51	3.41	3.36	2.64
Japan								
Official [5]	0.15	0.15	0.25	0.50	0.50	0.50	0.50	0.30
3 month	0.05	0.07	0.56	0.98	0.96	0.92	0.92	0.95
6 month	0.07	0.08	0.63	1.03	1.02	1.01	1.00	1.04
12 month	0.09	0.12	0.74	1.10	1.11	1.14	1.18	1.14

Source: Thomson Datastream.

1 Average daily data except official rates, which correspond to the last day of the period (15 December).

2 Average data from 1 to 15 December.

3 Marginal rate at weekly auctions.

4 Federal funds rate.

5 Monetary policy rate.

6 The table does not include the latest U.S. rates cut from 1.0% to 0.25%, which occurred after the closing date for this report (15 December). Nor is reference made in our analysis to the ensuing financial market developments.

In the United States, the Federal Reserve's October rate cuts (from 2.0% to 1.5% then to 1.0%) passed through to interbank market borrowing rates. Reductions were largest in the shortest maturities, precisely those which had spiked most sharply. By mid-December, three-month rates had fallen three percentage points to just under 2%, while six-month rates were down by 2.2 points to 2.2%.

As to expectations, three-month forwards (FRAs) signal more cuts to come in both the euro area and United States, which will be steeper in the former (around half a point) than in the latter case (around a quarter of a point).

Three-month forward rates (FRAs) [1]

TABLE 3

%	Dec 04	Dec 05	Dec 06	Dec 07	Feb 08	Jun 08	Sep 08	Dec 08[2]
Euro area								
Spot	2.16	2.49	3.73	4.68	4.73	4.95	5.28	3.24
FRA 3x6	2.23	2.74	3.94	4.52	4.43	5.17	4.84	2.67
FRA 6x9	2.36	2.91	4.07	4.42	4.14	5.21	4.38	2.48
FRA 9x12	2.49	3.00	4.13	4.33	3.96	5.26	4.13	2.53
FRA 12x15	2.64	3.07	4.13	4.30	3.80	5.23	3.99	2.73
U.S.								
Spot	2.56	4.54	5.36	4.70	2.69	2.78	4.05	1.87
FRA 3x6	2.95	4.81	5.31	4.15	2.24	2.96	3.30	1.58
FRA 6x9	3.22	4.84	5.21	3.69	2.12	3.19	2.91	1.60
FRA 9x12	3.41	4.81	5.06	3.45	2.18	3.34	2.94	1.67
FRA 12x15	3.57	4.76	4.94	3.36	2.23	3.56	3.03	1.79

Source: Thomson Datastream.

1 Data at period end.

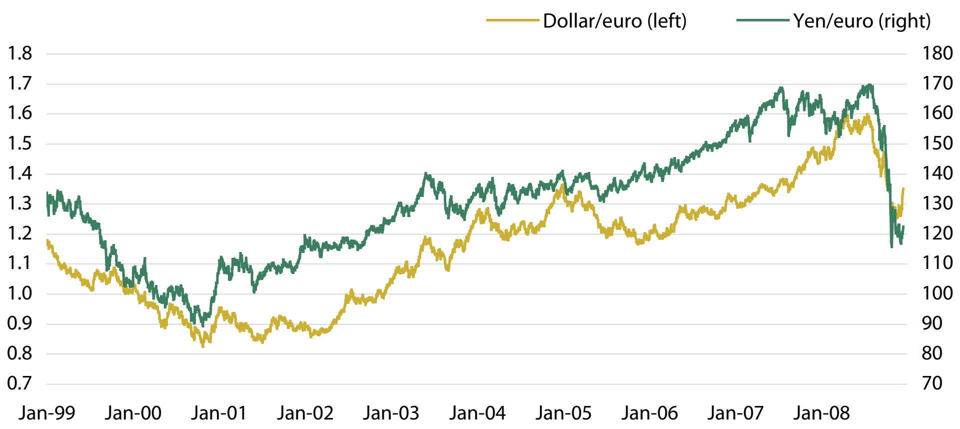
2 Data corresponding to 15 December.

2.2 Exchange rates

Foreign exchange markets lived though a second-half period of extreme turbulence, especially intense in the case of the yen which advanced strongly against both the euro and dollar. The Japanese currency appreciated from its August maximum of around 170 yens to 120 yens/euro in mid-December, and gained against the dollar by a rather more subdued 110 to 90 yens. One of the main factors driving this trend has been the close-out of carry trade positions (when investors simultaneously borrow in a low-yielding currency to fund the acquisition of assets denominated in other, high-yielding currencies). In today's leveraged setting, investors with debt in yens are opting to unwind their positions, i.e., buying yens to return their loans, in the process driving up the price of the Japanese currency.

The dollar too has made headway against from the euro in the past few weeks. The reason here could be revised expectations about the interest-rate spread between both zones as new ECB rate cuts come onto the horizon. By mid-December, the exchange rate was down to around 1.3 dollars/euro, a far cry from the mid-year highs of 1.6 dollars/euro.

Euro/dollar and euro/yen exchange rates[1] FIGURE 2



Source: Thomson Datastream.

1 Data to 15 December.

2.3 Long-term interest rates

Long government bond yields headed lower in all geographical areas in the third and fourth quarters of 2008. The run-down was initially sharper in the euro area, especially in three- and five-year terms, as a result of the changed outlook for ECB refinancing rates and the easing-off of inflationary pressures. However, U.S. yields began to drop more quickly from end November to mid December, with the end result likely to be a similar-size movement in both world zones.

In the euro area, the average monthly yield of three- and five-year governments was down to 2.6% by mid-December, almost two points less than June levels (see table 4). In the United States, three-year T-bonds were yielding 1.1% on average by mid-December (3.1% in June) while five-year instruments were down to 1.6% (3.5%

in June). Ten-year rates also fell on both sides of the Atlantic, albeit to a somewhat smaller extent.

Medium and long government bond yields[1] TABLE 4

%	Dec 05	Dec 06	Dec 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08[2]
Euro area								
3 year	na	3.74	3.85	3.85	3.35	4.56	3.87	2.58
5 year	na	3.74	3.92	3.92	3.35	4.55	3.87	2.58
10 year	na	3.80	4.28	4.28	3.87	4.56	4.18	3.15
U.S.								
3 year	4.39	4.57	3.11	3.11	1.74	3.07	2.35	1.08
5 year	4.41	4.51	3.51	3.51	2.49	3.48	2.87	1.60
10 year	4.47	4.57	4.19	4.19	3.69	4.12	3.68	2.65
Japan								
3 year	0.47	0.94	0.82	0.82	0.59	1.06	0.86	0.72
5 year	0.87	1.21	1.07	1.07	0.78	1.38	1.08	0.89
10 year	1.56	1.65	1.54	1.54	1.31	1.67	1.47	1.41

Source: Bloomberg.

na: not available.

1 Monthly average of daily data.

2 Average data from 1 to 15 December, except euro area to 11 December.

Japan too saw a substantial reduction in government bond yields, especially at the shorter end of the curve. Note however that the decrease was less than in the U.S. or Europe due to their lower start-out level.

In fixed-income markets, the keynote in both the U.S. and Europe was the tougher financing conditions facing corporate issuers. Table 5 shows how credit risk premiums (measured via BBB-AAA credit spreads) have risen significantly for both types of borrower across all featured maturities, albeit with some variations. In Europe, the bulge in BBB-AAA spreads between June and December was most pronounced in three- and five-year instruments, at almost 180 basis points, while in the United States it was in the 10-year term that they widened most appreciably: 174 basis points difference between June and November with some slight relief over the first fortnight in December.

Leading credit risk indices (CDX and Itraxx) also touched new highs in the case of both top-rated issuers (investment grade[3]) and those of lower credit quality (crossover[4]). Companies' growing difficulties in coaxing out profits have eroded entities' credit risk profile, and this is reflected in the price of their debt instruments.

3 An issuer or a given issue is termed investment grade when its credit rating is above a preset threshold, currently BBB- or higher in the case of S&P and Baa3 or higher in the case of Moody´s.

4 An issuer or a given issue is termed crossover when the rating one agency assigns it is on the lowest rung within investment grade and the rating assigned it by a second agency is outside the investment grade range.

Credit risk premiums: BBB-AAA spread [1] TABLE 5

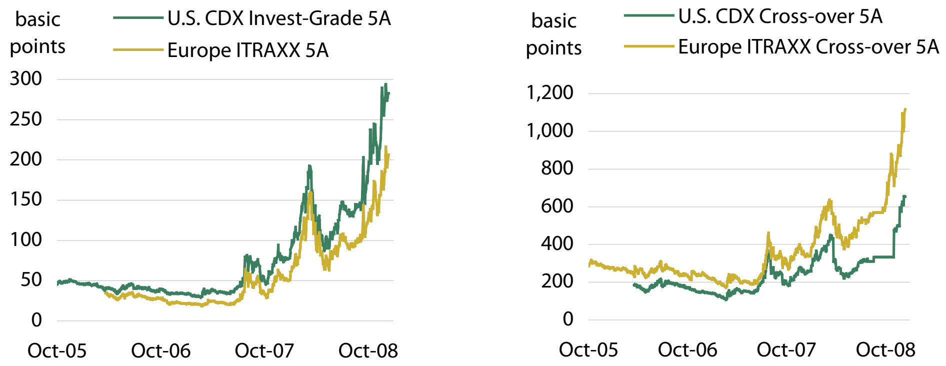
Basis points	Dec 05	Dec 06	Dec 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08[2]
Euro area								
3 year	43	37	76	76	153	109	139	288
5 year	53	53	108	108	196	143	183	320
10 year	77	84	127	127	199	175	191	306
U.S.								
3 year	37	54	135	135	214	191	227	297
5 year	63	68	183	183	240	234	265	288
10 year	108	96	219	219	251	228	283	314

Source: Reuters.

1 Monthly average of daily data.

2 Average data from 1 to 15 December.

Credit risk indices[1] FIGURE 3



1 Data to 15 December.

Source: Thomson Datastream.

2.4 International stock markets

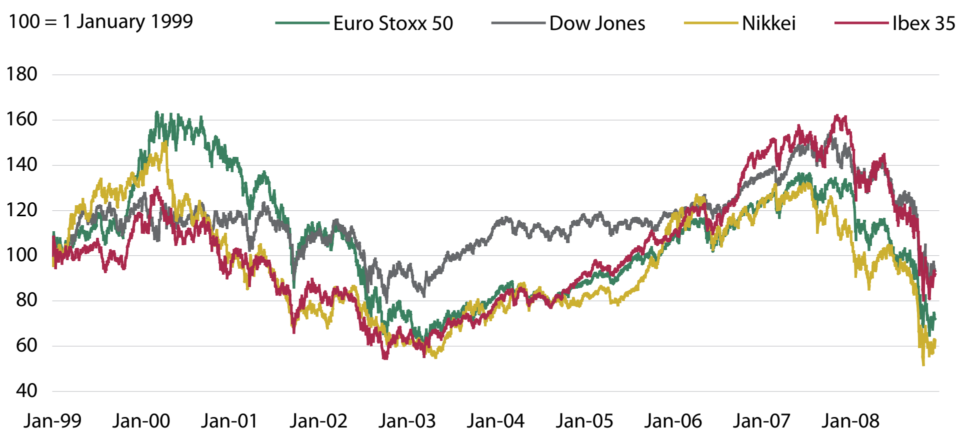
The string of events which last September unleashed what some are calling the biggest financial crisis since the 1929 crash had an immediate impact on international equity markets, which over the next four months suffered a pronounced price slide accompanied by a spiral in volatility. Although the revise-down in corporate earnings forecasts is amply discounted at current prices, the uncertainty and perception of risk afflicting market participants is absolutely the wrong recipe for a more stable climate. Government interventions in certain struggling institutions and a series of financial system action and rescue plans have so far been not enough to restore agents' confidence in these times of severe economic slowdown.

As we can see from table 6, the stock market indices of the world's most developed countries posted heavy losses in the third quarter, but worse was to come with falls of 20% of more (and continuing as we write) in almost all major bourses. Full-year losses have in most cases run to upwards of 40%. And a majority of indices are back to 2003 levels after the largest cumulative decline in their history.

In the United States, fourth-quarter losses ranged from the 21.1% of the Dow Jones (35.4% in 2008) to the 27.9% of the Nasdaq (43.1% in 2008). In Japan, the Nikkei dropped over 23% in the same period taking year-long losses to over 43%.

In Europe, euro area markets performed broadly in line while the United Kingdom fared a little better. The main euro-area share indices shed between 20% and 24% in the closing quarter with full-year losses ranging from the 40.6% of the Ibex-35 to the 49.0% of the Mib 30. In the UK, the price correction was somewhat milder (12.7% in the quarter and 33.8% in the year), helped perhaps by the prompt approval of what is possibly the most comprehensive rescue plan launched to date.

Main stock market indices[1] FIGURE 4



Source: Thomson Datastream.

1 Data to 15 December.

Performance of main stock indices[1] TABLE 6

	2004	2005	2006	2007	Q1 08[2]	Q2 08[2]	Q3 08[2]	Q4 08 (to 15 December) % Q[3]	% /Dec	% y/y[3]
World										
MSCI World	12.8	7.6	18.0	7.1	-9.5	-2.5	-15.7	-24.6	-43.9	-43.7
Euro area										
Euro Stoxx 50	6.9	21.3	15.1	6.8	-17.5	-7.6	-9.4	-20.8	-45.3	-45.1
Euronext 100	8.0	23.2	18.8	3.4	-16.2	-6.1	-11.8	-22.1	-45.9	-45.8
Dax 30	7.3	27.1	22.0	22.3	-19.0	-1.8	-9.2	-20.2	-42.3	-41.4
Cac 40	7.4	23.4	17.5	1.3	-16.2	-5.8	-9.1	-21.0	-43.3	-43.2
Mib 30	16.9	13.3	17.5	-6.5	-17.3	-5.1	-14.7	-23.8	-49.0	-49.4
Ibex 35	17.4	18.2	31.8	7.3	-12.6	-9.2	-8.8	-17.9	-40.6	-42.1
United Kingdom										
FT 100	7.5	16.7	10.7	3.8	-11.7	-1.3	-12.9	-12.7	-33.8	-33.1
United States										
Dow Jones	3.1	-0.6	16.3	6.4	-7.6	-7.4	-4.4	-21.1	-35.4	-35.8
S&P 500	9.0	3.0	13.6	3.5	-9.9	-3.2	-8.9	-25.5	-40.8	-40.8
Nasdaq-Cpte	8.6	1.4	9.5	9.8	-14.1	0.6	-8.8	-27.9	-43.1	-42.8
Japan										
Nikkei 225	7.6	40.2	6.9	-11.1	-18.2	7.6	-16.5	-23.0	-43.4	-44.2
Topix	10.2	43.5	1.9	-12.2	-17.8	8.8	-17.6	-22.1	-42.6	-43.6

Source: Datastream.

1 In local currency.

2 Change vs. previous quarter.

3 Year-on-year change to the reference date.

This price tumble was accompanied, as stated, by a surge in volatility across all main indices (see figure 5), from average levels bordering on 25% in the third quarter to

65% in the fourth, or even higher in the Japanese market (average fourth-quarter volatility upwards of 76%). Although still at highs, readings for this variable have come down appreciably from their end-October peak.

Historical volatility of main stock indices[1] TABLE 7

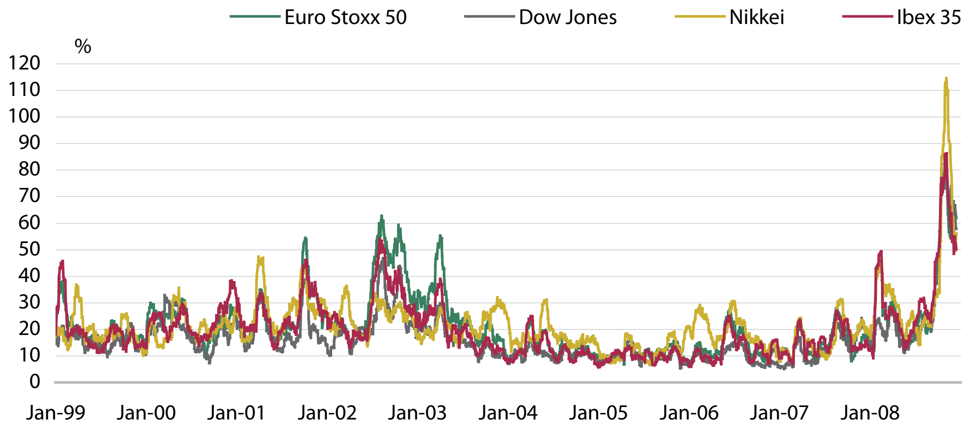
%	1999-2003	2004-2007	2005	2006	2007	Q1 08	Q2 08	Q3 08	Q4 08[2]
Euro Stoxx 50	25.08	13.17	10.73	13.63	14.94	28.39	17.83	25.41	65.92
Dow Jones	18.83	10.75	9.95	9.41	13.11	20.50	17.38	24.59	67.74
Nikkei	22.95	16.29	12.14	19.08	16.65	33.75	24.47	23.32	76.20
Ibex 35	23.09	12.44	9.86	12.45	15.32	29.56	19.68	29.92	65.04

Source: Thomson Datastream.

1 Average daily data.

2 The latest available data corresponds to 15 December.

Historical volatility of main stock indices[1] FIGURE 5



Source: Thomson Datastream.

1 Data to 15 December.

Emerging country markets performed even worse than their developed country counterparts, albeit with notable differences persisting between and within geographical areas (see table 8).

Overall, prices fell most sharply in Eastern European economies. In Russia, for example, the Moscow exchange had to close its doors for several days after the share price collapse of a number of listed companies. The country's leading stock index fell by over 47% in the third quarter and over 43% in the fourth, giving a full-year decline of 70%. And losses were similarly severe in the Bulgarian and Romanian markets, whose indices shed around 80% and 70% of their value respectively.

Asian markets too posted large price falls in both the third and fourth quarter of 2008, lifting cumulative losses to around 50% in almost all cases. The Chinese market came out worst with an annual decline of 62.7%. In contrast to most world indices, however, the run-down was steeper in the first than in the second half.

Finally, Latin American markets, whose prices had held up better than those of remaining developed or emerging economies over the first half of 2008, was finally sucked into the maelstrom by the world financial crisis and certain difficulties of its own. Second-half losses were heaviest in Argentina, Peru and Brazil, whose main stock indices shed 48.2%, 59.5% and 40.0% respectively in the course of the year.

Performance of other international stock indices[1]

TABLE 8

	Index	2007	Q1 08[3]	Q2 08[3]	Q3 08[3]	2008 – Dec[2] % Q	2008 – Dec[2] %/ Dec 07	2008 – Dec[2] % annual
Latin America								
Argentina	Merval	2.9	-2.2	0.2	-24.2	-30.2	-48.2	-49.0
Brazil	Bovespa	43.7	-4.6	6.6	-23.8	-22.6	-40.0	-38.6
Chile	IGPA	13.8	-4.7	9.1	-11.5	-14.0	-20.8	-19.8
Mexico	IPC	11.7	4.7	-4.9	-15.3	-15.4	-28.7	-29.8
Peru	IGRA	36.0	-0.8	-6.3	-31.0	-37.0	-59.5	-60.3
Venezuela	IBC	-27.4	-7.5	6.3	1.9	-9.5	-9.4	-7.2
Asia								
China	Shanghai Comp	96.7	-34.0	-21.2	-16.2	-14.4	-62.7	-60.8
India	BSE	59.7	-26.2	-14.6	-4.8	-25.1	-55.0	-54.3
South Korea	Korea Cmp Ex	32.3	-10.2	-1.7	-13.5	-20.0	-39.0	-38.9
Philippines	Manila Comp	21.4	-17.6	-17.6	4.5	-25.5	-47.2	-45.9
Hong Kong	Hang Seng	39.3	-17.8	-3.3	-18.5	-16.5	-45.9	-45.4
Indonesia	Jakarta Comp	52.1	-10.9	-4.0	-22.0	-25.8	-50.5	-50.4
Malaysia	Kuala Lumpur Comp	31.8	-13.7	-4.9	-14.1	-16.9	-41.4	-39.7
Singapore	SES All-S'Pore	18.7	-13.2	-2.0	-20.0	-24.8	-48.8	-48.5
Thailand	Bangkok SET	26.2	-4.8	-5.9	-22.4	-26.7	-49.1	-47.7
Taiwan	Taiwan Weighted Pr.	8.7	0.8	-12.2	-24.0	-19.3	-45.8	-43.2
Eastern Europe								
Russia	Russian RTS Index	19.2	-10.3	12.1	-47.4	-43.1	-69.9	-69.6
Poland	Warsaw G. Index	10.4	-13.7	-14.3	-9.2	-25.8	-50.2	-51.2
Romania	Romania BET	22.1	-29.6	-6.0	-34.5	-33.1	-71.0	-69.8
Bulgaria	Sofix	44.4	-29.0	-8.1	-31.3	-54.6	-79.7	-79.0
Hungary	BUX	5.6	-17.2	-6.1	-7.4	-37.5	-55.1	-55.7
Croatia	CROBEX	63.2	-26.6	-6.7	-16.6	-44.0	-68.0	-66.0

Source: Thomson Datastream.

1 In local currency.

2 Data to 15 December.

3 Quarterly change vs. the last day of the previous quarter.

The additional yield earned from dividend payments was sizeably higher in the second half, above all in Europe. The dividend yield of main stock indices ranged from the 5.7% of the Dax 30 and the 8.5% of the Mib 30 to the notably inferior 3.5% and 3.0% of the S&P 500 and Topix respectively.

Dividend yield of main stock indices

TABLE 9

%	2005	2006	2007	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08[1]
S&P 500	1.94	1.91	2.20	2.11	2.20	2.42	2.48	2.67	3.51
Topix	0.95	1.11	1.46	1.37	1.46	1.79	1.73	2.03	2.96
Euro Stoxx 50	3.28	3.52	3.73	3.79	3.73	4.68	5.05	5.56	7.72
Euronext 100	3.23	3.32	3.81	3.73	3.81	4.75	4.86	5.50	7.89
FTSE 100	3.59	3.77	3.88	3.94	3.88	4.58	4.85	5.26	6.72
Dax 30	2.17	2.29	2.52	2.50	2.52	3.64	3.73	4.09	5.65
Cac 40	3.43	3.79	4.34	4.41	4.34	5.22	5.42	5.93	8.00
Mib 30	3.53	3.67	3.81	3.66	3.81	4.76	5.58	6.21	8.54
Ibex 35	3.08	3.02	3.08	3.16	3.08	3.75	4.25	4.76	6.25

Source: Thomson Datastream.

1 Data to 15 December.

Price-earnings ratios (P/E) descended to new lows in tune with the overall performance of world stock indices. Japanese ratios proved the most resistant, and continued heading the table after a fall of just over 3 points. Elsewhere, ratios traced a parallel progression to close more than 4 points down on their start-out levels. North American P/Es (see table 10) remained substantially above the levels of Europe (between 7x and 8x). Finally, Spain's Ibex 35 index experienced the largest run-down in the full-year period though its closing ratios were still the highest in Europe by a small margin.

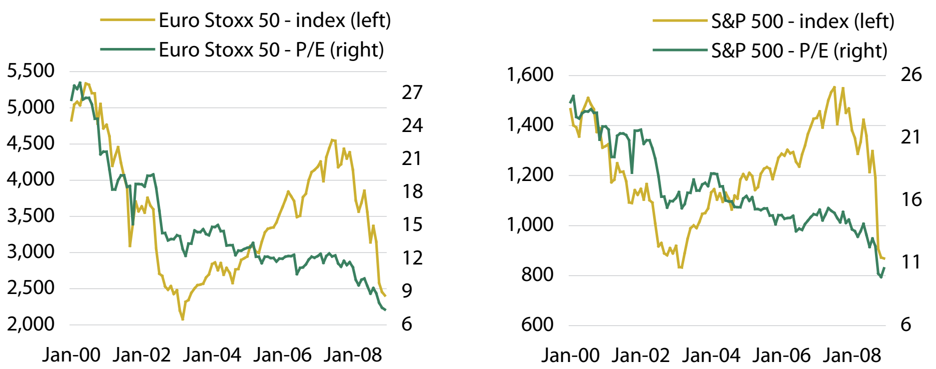
P/E of main stock indices TABLE 10

	2005	2006	2007	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08[1]
S&P 500	14.85	15.07	14.67	14.69	14.67	13.49	13.25	12.06	10.57
Topix	19.52	17.80	15.06	15.59	15.06	12.92	15.24	13.58	11.77
Euro Stoxx 50	12.03	12.15	11.56	11.55	11.56	9.68	9.15	8.64	7.39
Euronext 100	12.46	12.93	12.30	12.64	12.30	10.47	10.00	9.15	7.90
FTSE 100	12.45	12.41	12.07	11.95	12.07	10.62	9.93	8.59	7.83
Dax 30	12.62	12.78	12.33	12.35	12.33	10.22	10.06	9.44	8.18
Cac 40	12.14	12.68	11.80	12.08	11.80	10.06	9.49	8.68	7.74
Mib 30	13.38	13.07	11.50	12.09	11.50	9.52	9.15	8.24	7.33
Ibex 35	12.88	14.29	13.00	12.67	13.00	11.55	10.35	9.57	8.21

Source: Thomson Datastream.

1 Data to 15 December.

Stock indices and P/E: Euro Stoxx 50 vs. S&P 500 FIGURE 6



Source: Thomson Datastream. Data to 15 December.

A gap opened up as the year progressed between American and European bourses. While the former managed to grow its turnover in year-on-year terms, the latter registered a large decline, betraying the effects, presumably, of the bear run. In any case, as price falls have been fairly similar on both sides of the Atlantic, we can infer a significant difference in real-term activity (trading volumes) in favour of U.S. markets.

Turnover on main international stock markets

TABLE 11

Billion euros

Exchange	2005	2006	2007	Q3 07	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08[3]
U.S.[1]	20,042	27,044	32,758	8,776	8,803	8,735	7,925	9,267	4,059
New York	11,410	17,222	21,177	5,807	5,545	5,893	5,208	6,502	4,283
Tokyo	3,603	4,617	4,713	1,192	1,081	1,042	951	890	693
London	4,583	5,991	7,545	2,142	1,240	1,255	1,323	1,054	597
Euronext	2,345	3,006	4,102	1,113	966	918	777	732	464
Deutsche Börse	1,546	2,165	3,144	827	725	813	616	640	453
Borsa Italiana	1,051	1,258	1,681	395	389	311	322	246	120
BME[2]	854	1,154	1,667	372	435	383	258	287	192

Source: World Federation of Exchanges and CNMV.

1 The sum of New York Stock Exchange (NYSE), Nasdaq and American Stock Exchange.

2 Bolsas y Mercados Españoles. Not including Latibex.

3 Data for October and November except the U.S., where data is for October only.

3 Fixed-income markets in Spain

Interest rates on domestic commercial paper headed sharply lower after a relatively settled third quarter, along with changing expectations about the future direction of ECB monetary policy. The decline was most intense in the 12-month term, down 1.8 percentage points vs. its September average, leaving December's average rates at around 3.7% across all maturities (see table 12).

Short-term interest rates[1]

TABLE 12

%	Dec 05	Dec 06	Dec 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Commercial paper[2]								
3 month	2.58	3.78	4.97	4.97	4.74	5.16	5.24	3.66
6 month	2.74	3.91	4.91	4.91	4.74	5.31	5.45	3.74
12 month	2.93	4.00	4.85	4.85	4.73	5.59	5.63	3.85

Source: AIAF.

1 Average daily data. December data correspond to the average between 1/12 and 15/12.

2 Trading on private fixed-income market AIAF.

Medium and long-term yields[1]

TABLE 13

%	Dec 05	Dec 06	Dec 07	Dec 07	Mar 08	Jun 08	Sep 08	Dec 08
Private fixed income[2]								
3 year	3.15	4.04	4.59	4.59	4.21	5.79	5.39	3.89
5 year	3.48	4.14	4.65	4.65	4.41	5.97	5.48	4.23
10 year	3.89	4.26	4.94	4.94	4.82	5.94	5.65	4.74

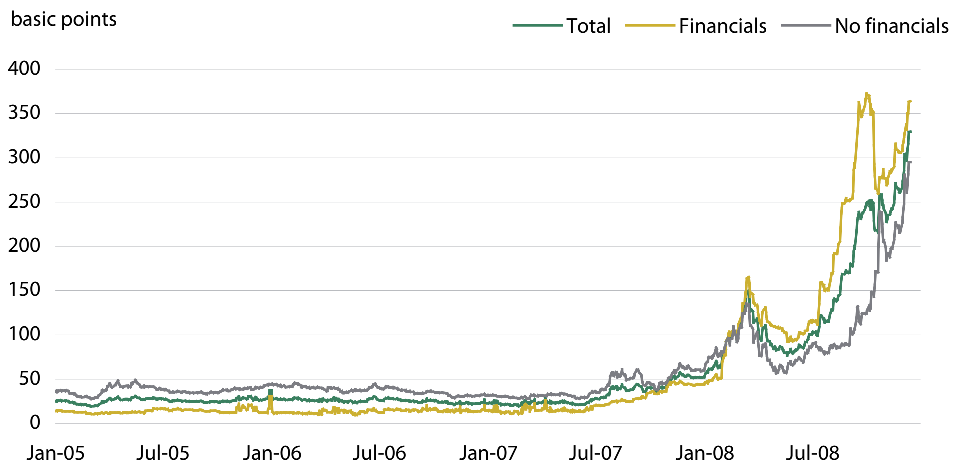
Source: AIAF.

1 Average daily data. December data correspond to the average between 1/12 and 15/12.

2 Bonds and debentures in outright trades on the AIAF market.

Long-term corporate bond rates traced a downward course in the third and fourth quarters due to changed expectations for ECB monetary policy and the tamer inflation outlook. Declines were sharpest (more than 1.7 percentage points) in the three-and five-year terms as far as December averages of 3.9% and 4.2% respectively. This larger run-down in shorter dated instruments caused a steepening of the curve, with the spread between 10- and 3-year notes widening from 15 basis points in June to 85 bp in December. Meantime, credit risk premiums reached new highs in the year's closing quarter, with financial sector spreads pulling ahead of the rest (see figure 7).

Aggregate risk premium[1] based on the five-year CDS of Spanish issuers FIGURE 7

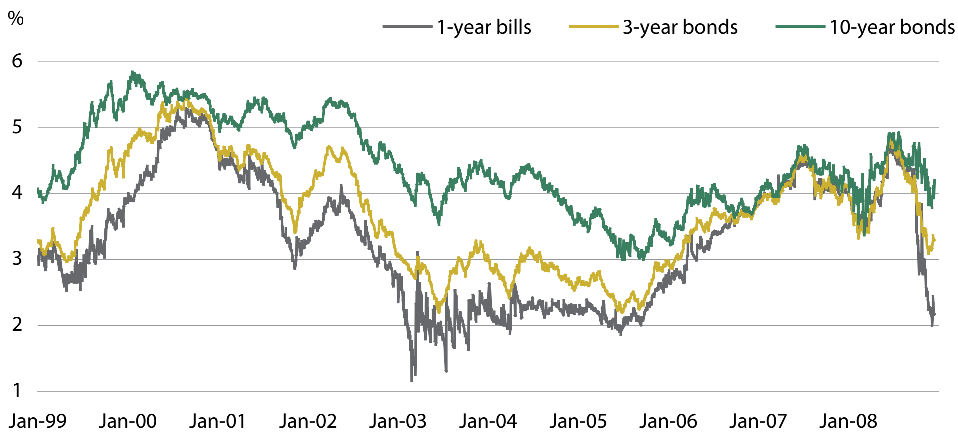


Source: Thomson Datastream and authors. Data to 15 December.

1 Simple average.

Long-term government yields performed similarly to those of private fixed-income instruments, registering a downward movement in the third and fourth quarters that was most intense in shorter maturities (i.e., accompanied by a steepening of the yield curve). Note, though, that sovereign yields in Spain fell less than the euro area benchmark, signalling an increased perception of country risk and a shift —shared with other European economies— into the market that has historically served as refuge. A similar reading emerges from the five-year CDS on the Spanish bond, which was trading at over 100 basis points in mid December (against the 30-50 bp interval prevailing till September).

Spanish government yields [1] FIGURE 8

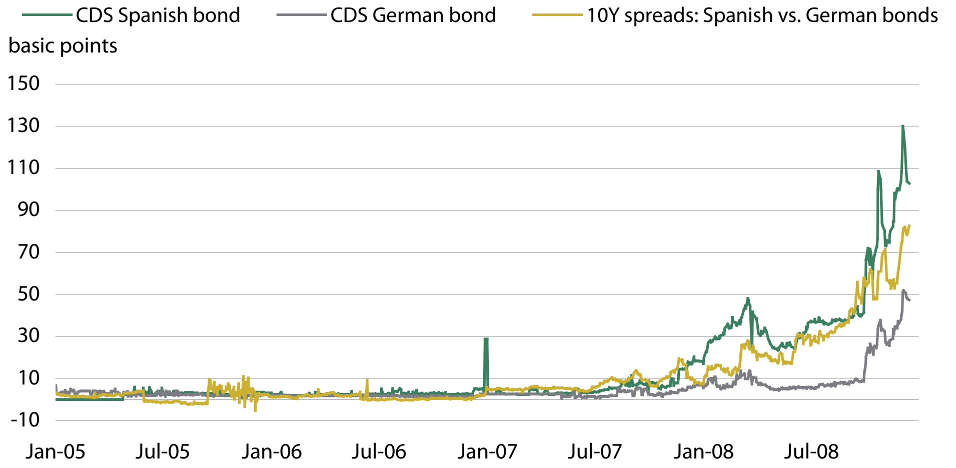


Source: Thomson Datastream.

1 Data to 15 December.

Risk premium of Spanish government bonds[1]

FIGURE 9



Source: Thomson Datastream.

1 Data to 15 December.

The dearth of fixed-income issues registered with the CNMV confirms the slow state of primary markets for this kind of instrument. Total 2008 issuance (pending data for December) was just 427 billion euros, compared to the 648 billion of 2007. The largest year-on-year decreases corresponded to non convertible bonds and debentures, after a timid second-quarter recovery, and covered bonds, particularly territorial issues. That said, fourth-quarter figures reveal an issuance upswing in asset-backed securities, whose volumes rose to 40 billion euros, almost half the amount issued in the closing quarter. It also bears mention that top-rated bonds (AAA and AA) raised their issuance share from 90.7% to 94.5% at the expense of sub BBB paper (see table 15).

The tougher financing conditions issuers face due to the financial crisis and domestic macroeconomic difficulties have caused a gradual shift in their borrowing mix. Increasingly, plain bond and debenture issues have made way for short-term commercial paper, whose issuance share has climbed from 64% to 67% in the last two years, and for asset-backed securities, up from 17% to 27%. It will be interesting to track the progress of primary bond markets in the coming months, to see whether government measures and the fall in interbank rates usher in improved financing conditions and, therefore, an upswing in issuance volumes.

Gross fixed-income issues[1] registered with the CNMV

TABLE 14

				2007	2008			
	2005	2006	2007	Q4	Q1	Q2	Q3	Q4[2]
NOMINAL AMOUNT (million euros)	414,254	523,131	648,757	154,568	117,527	134,468	90,554	84,619
Mortgage bonds	35,560	44,250	24,696	2,525	1,250	10,120	1,685	945
Territorial bonds	1,775	5,150	5,060	110	1,020	0	0	800
Non convertible bonds and debentures	41,907	46,688	27,416	257	604	3,744	4,215	1,239
Convertible/exchangeable bonds and debentures	163	68	0	0	0	0	0	0
Asset-backed securities	69,044	91,608	141,627	52,819	28,657	34,386	11,736	39,617
Domestic tranche	28,746	30,886	94,049	51,309	28,657	32,993	10,607	39,617
International tranche	40,298	60,722	47,578	1,510	0	1,393	1,129	0
Commercial paper[3]	264,360	334,457	442,433	98,857	85,900	86,118	72,868	42,018
Securitised	2,768	1,993	465	85	133	48	94	43
Other	261,592	332,464	441,969	98,772	85,767	86,070	72,774	41,975
Other fixed-income issues	89	0	7,300	0	0	0	0	0
Preference shares	1,356	911	225	0	96	100	50	0
Pro memoria:								
Subordinate debt issues	11,079	27,361	47,158	16,197	2,313	1,945	1,575	3,852
Covered issues	94,368	92,213	121,608	32,702	6,534	7,573	2,115	4,215

Source: CNMV.

1 Including those admitted to trading without an issue prospectus.

2 Last data: 30 November 2008.

3 Figures for commercial paper correspond to amounts placed.

Issues of asset-backed securities[1] registered with the CNMV Distribution by credit rating

TABLE 15

% total unless otherwise indicated	2007			2008			
	Q2	Q3I	Q4	Q1	Q2	Q3	Q4[2]
Million euros	31,518	17,898	52,819	28,657	34,386	11,736	39,617
Percentage	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Investment grade							
AAA	94.6	92.9	93.7	93.7	94.2	90.1	92.3
AA	0.6	0.7	0.9	1.3	0.3	0.6	2.2
A	2.5	2.9	1.9	1.6	2.8	5.0	2.3
BBB	1.4	1.9	2.0	1.5	1.6	2.4	2.4
Speculative grade							
<BBB	0.9	1.5	1.5	1.9	1.0	1.9	0.8

Source: CNMV.

1 Including mortgage bonds and non mortgage asset-backed securities.

2 Data to 30 November.

4 Spanish equity markets

4.1 Prices

Spanish stock markets performed on a par with other European bourses over the third and fourth quarter. At home, wavering confidence about the sustainability of the financial system was compounded by a growth stall which made large inroads into corporate earnings and sent prices tumbling across almost all main indices and sectors.

The Ibex 35 posted a fourth-quarter fall of around 18%, in line with other European indices, to add to its third-quarter losses of 9%. The result was a full-year decline of 40.6%, the largest in its history[5], taking it back to the levels of the closing quarter of 2004. Other domestic indices recorded losses on a similar or even larger scale. Specifically, medium and small cap indices shed over 45% and 54% respectively in the full-year period (49% and 57% in year-on-year terms). And the FTSE Latibex indices, which had held up reasonably well to mid year, had a dismal second half which took their cumulative losses (see table 16) to 49% in the case of the FTSE Latibex All-Share and 42% in that of the FTSE Latibex Top.

This sharp correction was accompanied by a dramatic upturn in price fluctuation, i.e., volatility, which recorded decade-long highs during the closing months (see figure 9). Implied at-the-money (ATM) volatility on the nearest expiry date of Ibex 35 options averaged 63.3% in the fourth quarter compared to 31.2%, 23.0% and 31.3% in the preceding three and an average of 23% since January 1999. Of course share prices tend to fluctuate more at times of increased risk aversion and agent distrust. Note, however, that implied volatility has eased to near 50% from its mid-October peak of over 100%.

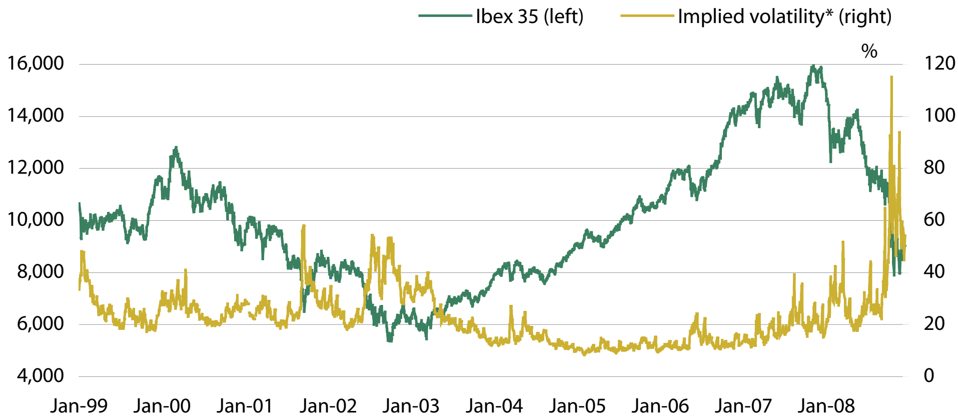
Performance of Spanish stock indices (%) TABLE 16

								Q4 08 (to 15 Dec)		
	2004	2005	2006	2007	Q1 08[1]	Q2 08[1]	Q3 08[1]	% Q	%/Dec	% y/y
Ibex-35	17.4	18.2	31.8	7.3	-12.6	-9.2	-8.8	-17.9	-40.6	-42.1
Madrid	18.7	20.6	34.5	5.6	-12.4	-9.8	-9.5	-18.2	-41.5	-43.1
Ibex Medium Cap	25.1	37.1	42.1	-10.4	-9.8	-15.0	-14.5	-16.8	-45.4	-48.9
Ibex Small Cap	22.4	42.5	54.4	-5.4	-13.6	-11.6	-23.1	-21.7	-54.0	-57.4
FTSE Latibex All-Share	31.0	83.9	23.8	57.8	-10.5	14.5	-27.7	-31.4	-49.2	-48.6
FTSE Latibex Top	28.1	77.9	18.2	33.7	-6.2	15.8	-25.3	-28.3	-41.8	-42.0

Source: Thomson Datastream.

1 Change vs. previous quarter.

Performance of Ibex 35 and implied volatility FIGURE 10



Source: Thomson Datastream and MEFF.

* Implied at-the-money (ATM) volatility on nearest expiry. Data to 15 December.

Not a single sector[6] closed the period or the year in positive terrain. The worst hit were the banks, whose fourth-quarter fall of almost 29% (see table 17) nudged year-

5 Since the year-on-year decline of 39.8% registered in September 2001.

6 Of the Madrid General Index (IGBM) which we take as our reference in this report.

to-date losses above 50%. Spain's top two banking groups posted losses in line with the sector and together accounted for more than half of the fourth-quarter decline in the Madrid General Index (IGBM).

Among the other rear enders were real estate and construction companies, with year-to-date price slides of 64% and 49% respectively. Oil and energy, meantime, outperformed the index by a small margin to close with a cumulative fall of 37.5%.

The best performer, as in previous years, was technology and telecommunications, which has served as an investor haven. Prices in this sector slipped 4.5% in the fourth quarter for a full-year outcome of -28%. Consumer goods too consistently outperformed the market to end 24% down on its start-out levels.

Performance of the Madrid Stock Exchange by sector and leading shares[1] TABLE 17

annual % unless otherwise indicated

						2008-Dec[3]		
	weighting[2]	2007	Q1 08	Q2 08	Q3 08	% Q	%/Dec 07	% annual
Financial and real estate services	**40.55**	**-5.5**	**-13.8**	**-13.0**	**-8.2**	**-27.8**	**-50.2**	**-51.1**
Real estate and others	0.55	-40.6	-12.2	-26.1	-28.7	-21.3	-63.6	-66.9
Banks	37.33	-3.6	-13.8	-12.3	-7.5	-28.8	-50.2	-50.9
BBVA	12.08	-8.1	-16.8	-12.8	-5.8	-26.5	-49.8	-51.0
Santander	19.33	4.6	-14.7	-7.5	-10.0	-33.2	-52.6	-52.2
Oil and energy	**21.79**	**13.0**	**-8.0**	**-5.5**	**-14.3**	**-16.2**	**-37.5**	**-39.1**
Iberdrola	9.00	25.6	-5.6	-13.3	-16.1	-19.5	-44.7	-45.9
Repsol YPF	4.86	-6.9	-10.3	14.5	-16.5	-28.7	-38.8	-40.7
Basic materials, industry and construction	**9.64**	**-3.2**	**-11.3**	**-7.4**	**-22.8**	**-21.4**	**-50.2**	**-53.2**
Construction	4.71	-10.1	-13.9	-11.7	-21.9	-13.7	-48.8	-52.3
Technology and telecommunications	**19.98**	**34.3**	**-17.7**	**-7.5**	**-1.0**	**-4.5**	**-28.0**	**-29.5**
Telefónica	19.21	37.8	-18.1	-7.3	-0.5	-4.5	-27.8	-29.0
Consumer goods	**4.69**	**6.1**	**-4.9**	**-5.9**	**-8.1**	**-7.4**	**-23.9**	**-27.7**
Consumer services	**3.34**	**-8.0**	**-8.9**	**-23.6**	**-7.5**	**-11.6**	**-43.1**	**-45.5**

Source: Thomson Datastream and Bolsa de Madrid.

1 Shares capitalising at more than 4% of the IGBM.

2 Relative weight (%) in the IGBM as of July 2008.

3 Data to 15 December. Quarterly change (% Q) corresponds to the period between 30 September and 15 December 2008.

Shares with greatest impact on IGBM change[1] TABLE 18

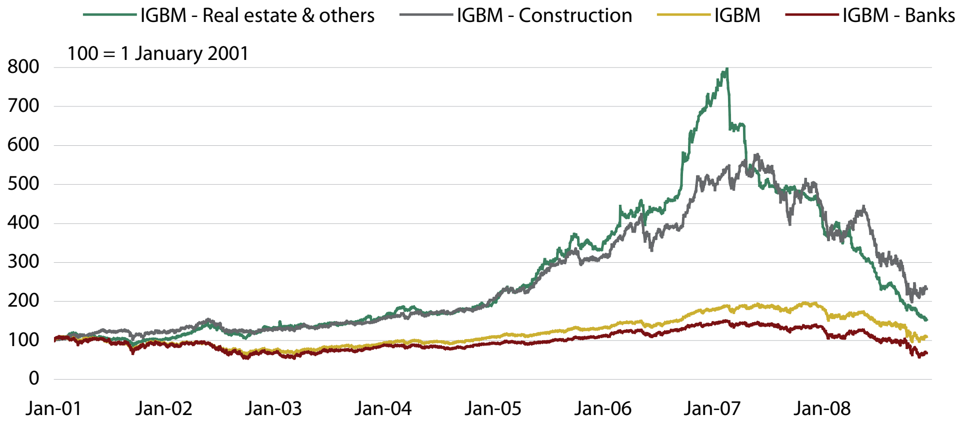
		2008- Dec[2]	
Share	**Sector**	**% Q**	**%/Dec 07**
Positive impact			
-	-		
Negative impact			
SANTANDER	Financial and real estate services	-6.42	-10.16
BBVA	Financial and real estate services	-3.20	-6.01
IBERDROLA	Oil and energy	-1.75	-4.03
REPSOL YPF	Oil and energy	-1.39	-1.89
TELEFÓNICA	Technology and telecommunications	-0.86	-5.34
BANCO POPULAR ESPAÑOL	Financial and real estate services	-0.74	-1.26
GAMESA	Basic materials, industry and construction	-0.64	-0.83
GAS NATURAL SDG	Oil and energy	-0.45	-0.91
ACCIONA	Basic materials, industry and construction	-0.27	-0.78
GRUPO FERROVIAL	Basic materials, industry and construction	-0.25	-0.41
ARCELORMITTAL	Basic materials, industry and construction	-0.24	-0.32
GRIFOLS	Consumer goods	-0.23	-0.15
TÉCNICAS REUNIDAS	Basic materials, industry and construction	-0.18	-0.27
CRITERIA CAIXACORP	Financial and real estate services	-0.18	-0.47
SACYR VALLEHERMOSO	Basic materials, industry and construction	-0.16	-0.32

Source: Thomson Datastream and Bolsa de Madrid.

1 The shares listed are those having most impact (equal to or more than 0.15 points) on the quarterly change in the IGBM.

2 Data to 15 December.

Performance of Real estate and others, Construction and Banks[1] FIGURE 11



Source: Bolsa de Madrid.

1 Data to 15 December.

Table 19 offers a snapshot of the quarterly performance of IGBM shares. We can see that market turbulence lifted the percentage of issuers in losses to 87% in the fourth quarter.

Performance range of IGBM shares TABLE 19

% total IGBM companies	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08[1]
≥ 25%	0.0	0.0	0.8	0.8	2.3
10% to 25%	7.9	3.0	6.0	5.3	1.5
0% to 10%	19.7	20.0	15.0	7.6	9.2
≤ 0%	72.4	77.0	78.2	86.4	87.0
Pro-memoria: total no. of companies					
	127	135	133	132	131

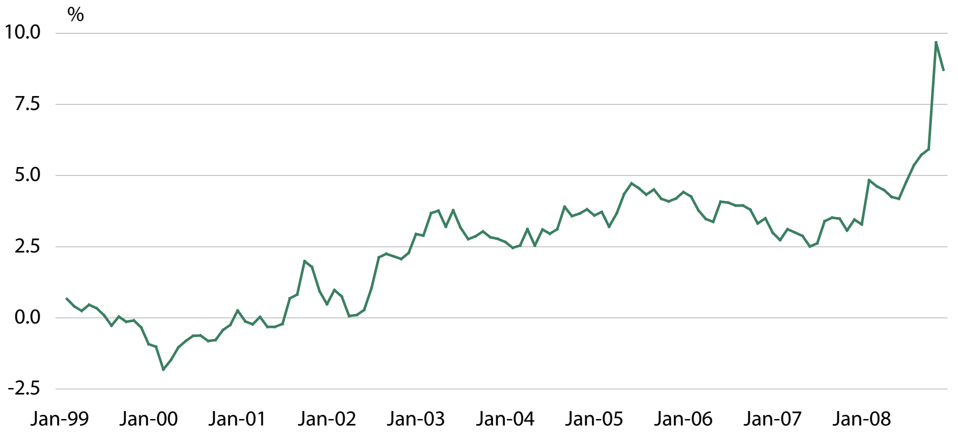
Source: Thomson Datastream.

1 Data to 15 December.

The price-earnings ratio of the Ibex 35 dropped from an average 9.6x in September to 8.2x at 15 December (see table 10) mirroring the steep run-down in equity prices. That said, the Spanish market conserves the highest P/E out of main European contenders.

The earnings yield gap (indicating the risk premium on equity investment versus long-term government bonds) widened considerably in the year's last quarter under the combined effect of falling prices and the downtrend in government yields. The latest estimate of 8.5% puts it well ahead of the average recorded since 1999 (2.4%).

Earnings yield gap[1] of the Ibex 35 FIGURE 12



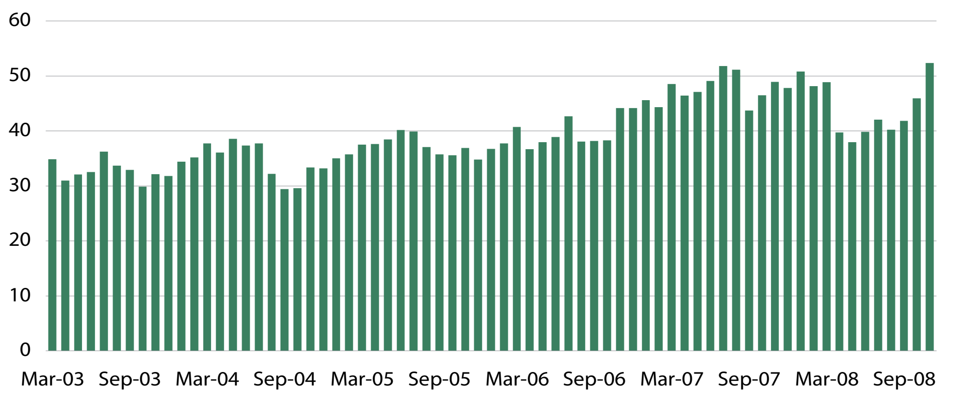
Source: Thomson Datastream and authors.

1 Difference between stock market yield, taken as earnings/price, and ten-year bond yields. Monthly data to November.

4.2 Activity: trading and liquidity

Turnover on the Spanish stock market stabilised in the second half after the notable declines of the first and second quarters, and even picked up slightly in the closing months in average daily terms: 4.48 billion euros in the fourth quarter against 4.36 billion in the third (see table 20). Given the run-down in prices over this last period, we can assume that trading volumes have substantially recovered; a conclusion borne out by the latest readings for turnover velocity, the ratio between turnover and capitalisation (in the electronic market).

Turnover velocity[1] of the Spanish stock market[2] FIGURE 13



Source: CNMV.

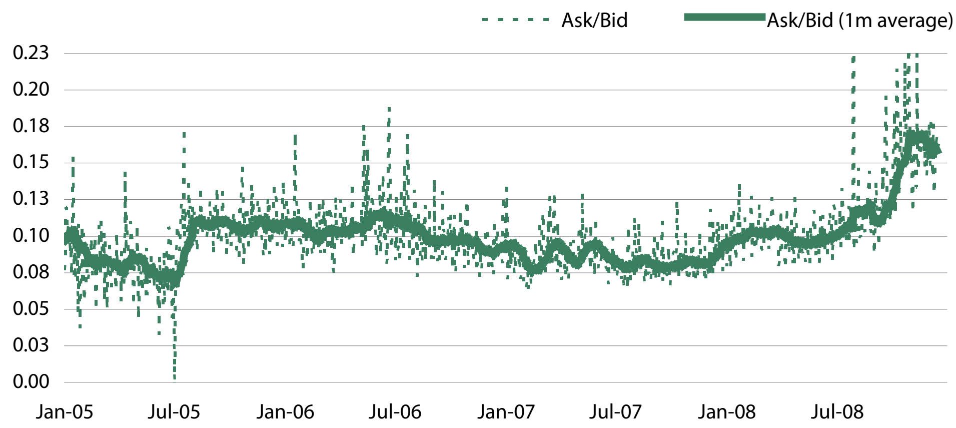
1 Ratio of cumulative trading volume in the electronic market in the last quarter and average monthly capitalisation in the same period.

2 Data to November.

The liquidity conditions of the Spanish market also felt the pressure, with bid/ask spreads worsening as the year progressed (see figure 14) to a fourth-quarter peak testing 0.18% (against 2007 averages of around 0.08%). Again, however, we can detect some improvement in the closing days of the fourth quarter.

Liquidity indicator (bid/ask spread, %) of the Ibex-35[1]

FIGURE 14



Source: Thomson Datastream and authors.

1 Data to 15 December.

Turnover on the Spanish stock market

TABLE 20

Million euros	2005	2006	2007	Q4 07	Q1 08	Q2 08	Q3 08	Q4 08 [1]
All exchanges	**854,145**	**1,154,294**	**1,667,219**	**434,823**	**383,254**	**258,023**	**287,680**	**192,467**
Electronic market	847,664	1,146,390	1,658,019	432,081	380,935	256,454	286,063	190,818
Open outcry	5,899	5,318	1,154	274	44	23	65	14
of which SICAV [2]	4,864	3,980	362	15	6	2	7	7
MAB [3]	-	1,814	6,985	2,240	1,966	1,376	1,406	1,558
Second market	26	49	193	12	3	18	10	0
Latibex	557	723	868	216	306	153	136	77
Pro-memoria: non resident turnover (% all exchanges)								
	57.1	58.2	61.6	62.3	na	na	na	na

Source: CNMV and Directorate-General of Trade and Investments.

1 Cumulative data to 30 November.

2 Open-ended investment companies.

3 Alternative investment market. Data since the start of trading on 29 May 2006.

na: data not available at the closing date for this report.

II Reports and analyses

Economic and financial trends in listed companies in the first half of 2008

Belén de Anta and Carolina Moral (*)

* Belén de Anta and Carolina Moral are part of the CNMV's Financial and Accounting Reports Office.

1 Introduction

The purpose of this article is to analyze the main magnitudes of the public information[1] that issuers have reported to the CNMV on the first half of 2008.

This information refers to results, financial position, cash flows, number of employees and dividends distributed. The companies analyzed, totalling 188, are in the following sectors: energy (14 companies); trade and services (41 companies); construction and real estate (28 companies); industry (51 companies); banks (12 companies); savings banks (36 companies); other financial institutions (3 companies); and insurance (3 companies).

Our analysis is subject to the following considerations:

- The data analyzed are obtained from periodic consolidated or individual[2] financial reports[3] submitted to the CNMV by issuers of shares and debt instruments[4] listed on a regulated Spanish market, where Spain is the originating Member State.
- 37.7% of the summary accounts posted in the first half of 2008 include an auditors' opinion or limited review[5], which percentage rises to 64.7% if we consider only IBEX 35 companies.
- The aggregate figures exclude listed groups' dependent issuers. But these are included in data by branch of activity where such issuers are active in a sector other than that of their controlling company.
- Data from periods outside the scope of this article were taken from a representative sample of companies listed at any one time.

Section 2 of this article analyzes developments since 2005 in net turnover; sections 3 and 4 look at trends in results and return on equity and on investment, respectively; section 5 refers to debt in non-financial companies; and sections 6, 7 and 8 describe the variation, over the same period in the previous year, in cash flows, workforce and dividends distributed. Finally section 9 summarizes our main conclusions.

1 Pursuant to article 35 of Law 24/1988 of 28 July on the Stock Market, where Spain is the originating Member State, issuers whose shares or debt securities are tradable on an official secondary market or another resident market in the European Union are to disclose and post a financial report on the first six months of the year.

2 Except for firms that submit no comparative information, in accordance with the fourth transitory provision of Royal Decree 1415/07 of 16 November adopting the Spanish Standard Chart of Accounts (PGC).

3 Submitted on the models established in Circular 1/2008.

4 Except for firms that have issued preferential shares and instrumental companies set up to issue debt securities and the Official Credit Institute (ICO).

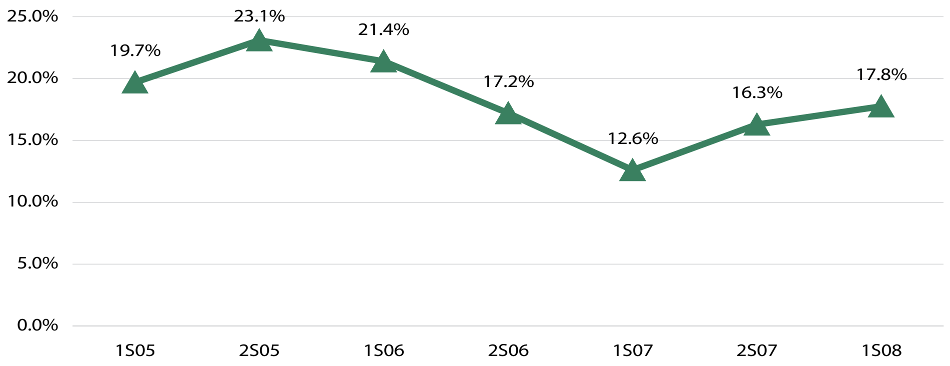
5 Pursuant to article 14 of Royal Decree 1362/2007.

2 Net turnover

Figure 1 shows the year-on-year rate of change in net turnover[6] for the period from the first half of 2005 to the first half of 2008.

As we see, in the first half of 2008 the rate was 17.8%, mainly due to positive trends in the energy sector. Without companies in that sector the rate would have dropped to 13.5%. This trend continued in the third quarter of 2008, with a rate of some 13.6%.

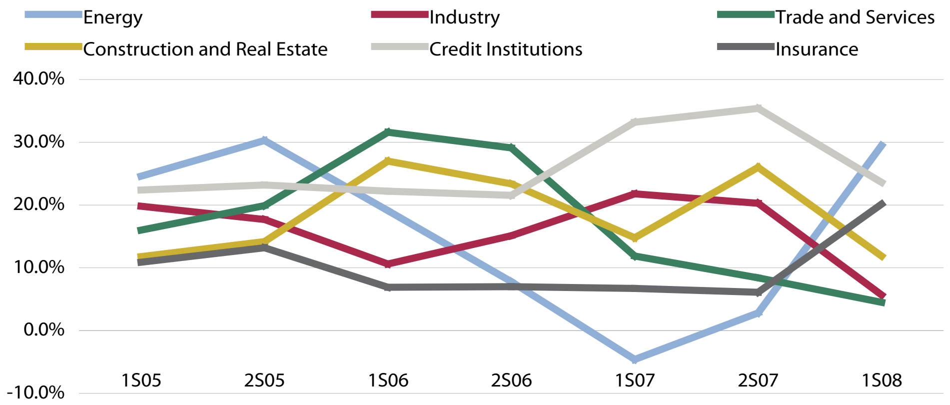
Rate of change in net turnover FIGURE 1



Source: Authors' data.

Figure 2 shows the trends in turnover for the various sectors.

Rate of change in net turnover by sector FIGURE 2



Source: Authors' data.

6 As turnover for credit institutions we have taken the amount of interest receivable and similar income, and for insurance companies the amount of life and non-life premiums attributable to the year net of reinsurance.

As may be seen, the trend was uneven across the various sectors:

- Energy. Net turnover increased by 29.5%. This growth was affected by:
  - The consolidation of major companies which were not fully consolidated in the first half of 2007 as they were acquired towards the end of that period.
  - Supply costs are a key factor in sales. In this case the trend in average oil prices is especially significant, from 63.2 dollars for a barrel of Brent in the first half of 2007 to 138.86 a barrel at 30 June 2008. But this effect was offset by the gradual depreciation of the dollar, from $/€1.34 in the first half of 2007 to $/€1.56 at the end of the first half of 2008.
- Industry. In the first half of 2008 the growth rate was 5.7%, well below that recorded in previous periods, for in 2007 rates of more than 20% were reached. This figure highlights the slowdown taking place in industrial activity.
- Trade and services. In this sector net turnover grew in the first half of 2008 by some 4.5%, maintaining the trend begun in the first half of 2007.
- Construction and real estate. The 11.9% growth in turnover was chiefly due to holdings in the energy sector being consolidated for the first time. Leaving out this impact, we find a significant reduction in the level of activity, with a rate of change of 4.3%.
- Credit institutions. The income from interest and similar revenue recorded by credit institutions in the first half of 2008 rose by 23.4% relative to the same period of the previous year. This rise was much less than that of previous periods due to the combined effect of the rising trend in interest rates[7] and the more moderate rise in turnover as a result of the financial crisis and economic slowdown. This change of trend, already appreciable in savings banks in the second half of 2007 when the Spanish real estate sector began to show signs of cooling, reached banks in the first half of 2008.
- Insurers. An increase in turnover of some 20% over the same period of the previous year, in both the "life" and "non-life" branches.

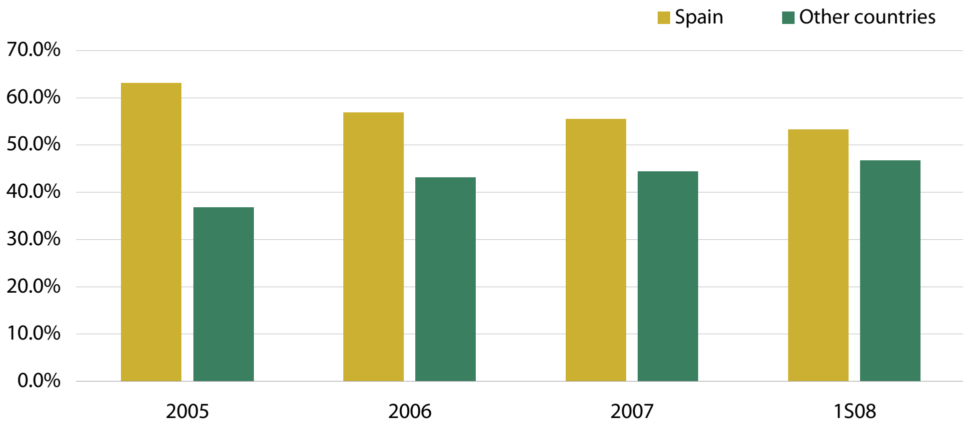
Figure 3 shows the regional distribution of turnover in non-financial companies from 2005 to the first half of 2008.

As we see, in 2006 there was a significant increase in the relative importance of sales generated abroad, due to the acquisition of foreign companies and, to a lesser extent, the establishment and development of companies or businesses (motorway concessions, etc.) in foreign markets. In subsequent periods the percentage of sales generated abroad remained stable, with a slight upward trend.

7 In June 2007 the one-year Euribor rate was 4.51%, and in June 2008 it had risen to 5.36% (source: Bank of Spain).

Net turnover by region

FIGURE 3



Source: Authors' data.

Table 1 gives a regional breakdown of net turnover of companies in the various non-financial sectors.

Net turnover by region and sector

TABLE 1

		2005	2006	2007	1st 1/2 2008
Energy	**Spain**	**67.3%**	**62.2%**	**60.5%**	**56.6%**
	Other countries	32.7%	37.8%	39.5%	43.4%
Industry	**Spain**	**43.8%**	**40.2%**	**39.4%**	**41.7%**
	Other countries	56.2%	59.8%	60.6%	58.3%
Trade and services	**Spain**	**59.7%**	**49.8%**	**49.4%**	**46.6%**
	Other countries	40.3%	50.2%	50.6%	53.4%
Construction and real estate	**Spain**	**76.9%**	**71.1%**	**68.1%**	**64.3%**
	Other countries	23.1%	28.9%	31.9%	35.7%

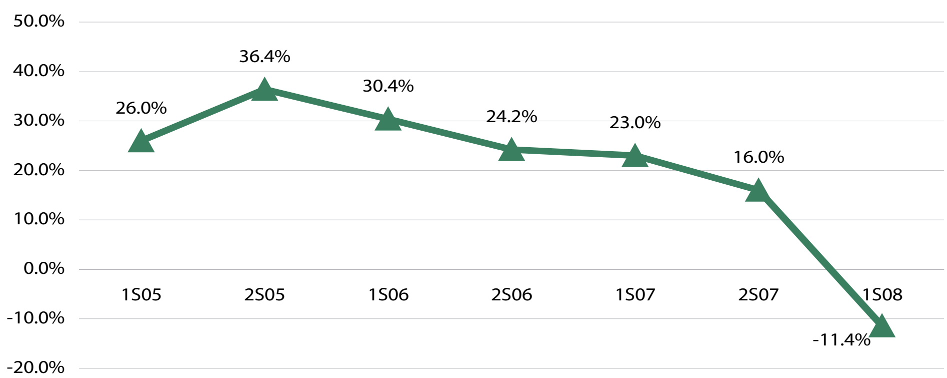
Source: Authors' data.

3 Results

Figure 4 shows the year-on-year rate of change in pre-tax results from continuous activities since the first half of 2005. As from the first half of 2006 we see a progressive reduction in the rate, sharply accentuated in the first half of 2008, with a drop of 11.4%.

Rate of change in pre-tax results

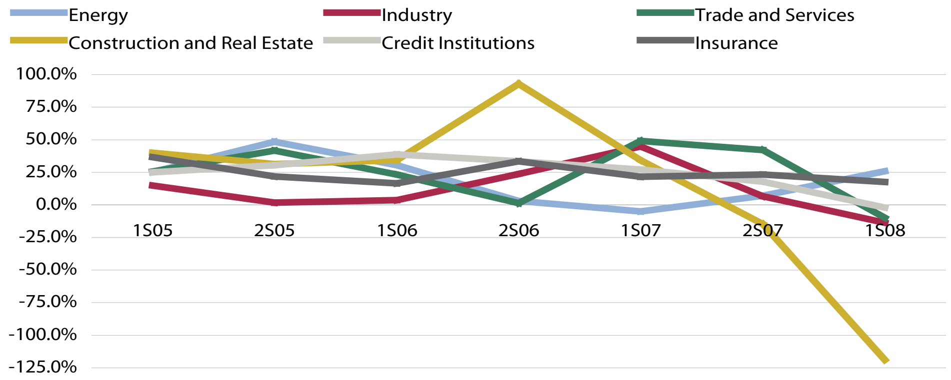
FIGURE 4



Source: Authors' data.

Figure 5 shows the trend in this magnitude in the various sectors. Three of the six sectors show falls in results, especially sharp in the case of construction and real estate, with a negative rate of 118.9% and losses of 817 million, as opposed to profits of 5.96 billion in the first half of 2007. Only the energy sector showed improved results, with a rise of 25.9% due to non-recurring capital gains. Insurance companies' results held up relative to the same period of the previous year, while those of credit institutions fell off slightly.

Rate of change in pre-tax results by sector FIGURE 5



Source: Authors' data.

Table 2 shows the main profit and loss margins corresponding to the first half of 2008 and their variation relative to the same period of the previous year.

EBITDA, EBIT and year's results TABLE 2

million euros	EBITDA		EBIT		YEAR'S RESULT	
	Amount	% Change	Amount	% Change	Amount	% Change
Energy	16,148	14.57%	11,648	18.49%	13,086	99.45%
Industry	3,713	-3.53%	2,597	-9.48%	1,788	-4.89%
Trade and services	15,435	-0.86%	9,570	0.03%	5,770	-8.05%
Construction and real estate	4,337	-44.45%	2,193	-63.68%	-817	-113.62%
Credit institutions					15,020	0.4%
Insurance companies					729	21.5%

Source: Authors' data.

By sector, the most notable events were as follows:

- Energy. Operating results rose by 18.5%. This rate was less than that of the rise in turnover (29.5%), which is explained by the rise in supply costs linked to the price of oil.

  The sector's net financial burden rose by 14.3%, though its pre-tax results went up by 25.9% as a result of profit from the disposal of financial instruments (758 million euros, as opposed to 191 million euros in the first half of 2007).

  Its result for the year rose by 99.5%, mainly due to income from interrupted operations. Without this impact the rise would have been 31.2%.

- Industry. The slowdown in the Spanish economy over the first half of 2008 affected companies in this sector in particular. Despite a rise in turnover, operating results fell 9.5% due to the rise in commodity supply costs and energy prices, as well as amortization expenses.

  The sector's result was down for the year, but less than its operating results thanks to a lower tax burden and better results from interrupted operations.

- Construction and real estate. This is the sector most affected by the economic slowdown. Aggregate EBITDA and EBIT fell by 44.4% and 63.7% respectively, and the year yielded a negative result of 817 million euros. But this trend was uneven across the various construction and real estate firms.

  Real estate firms' EBITDA, EBIT and results for the first half of 2008 showed negative figures of 1.80, 1.82 and 2.74 billion euros respectively. This situation reflects:

  - a fall in sales;
  - a downward trend in sale prices;
  - updates to market value of real estate assets acquired through business combinations; and
  - a reduction in the value of stocks and real estate investments.

  As a result, construction companies also recorded a 49.4% drop in their results for the year because of their exposure to the real estate market (due to the consolidation of companies in the sector), their rising losses due to the deterioration and disposal of fixed assets (426 million euros) and capital losses on their financial instruments (221 million euros, as opposed to 125 million euros of capital gains in the first half of 2007).

- Credit institutions. The rising cost of finance, due to greater difficulties in acquiring resources and the slowdown in credit, prompted by the economic situation, directly affected interest margins, which grew by 13.6% in the first half of 2008, well below the 22% reached in the second half of 2007.

  In the first half of 2008 all financial institutions had to fund large reserves to cover the rise in the default rate, a circumstance that significantly marred their operating results. Losses due to deterioration in the assets of banks and savings banks rose by 61% and 63.8% respectively in the first half of 2008 over the same period of 2007, absorbing 15% and 21% of their respective gross margins.

- Insurance companies posted a 21.5% rise in after-tax results relative to the first half of 2007, in line with the growth in their net turnover, due to:

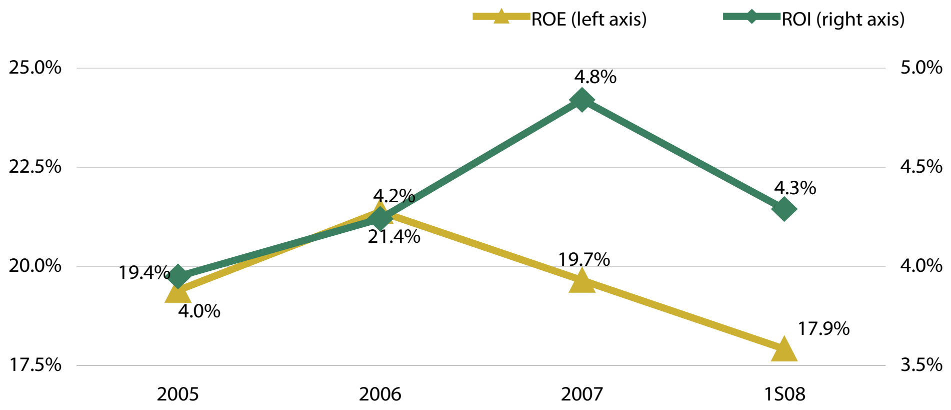
  - the issuing of endowment policies and, significantly, the accounting consolidation of companies specialized in the life branch; and
  - containment of operating costs, offsetting the higher claim rate in the non-life branch.

With the information available in the third quarter of 2008, as posted by the main insurers in the sample, we see that in aggregate terms the trend of the first half of the year has been slightly attenuated, with a drop in operating results of 3% relative to the same period of the previous year.

4 Return on equity and on investment

Figure 6 shows the trend[8] in return on equity (ROE) and return on investment (ROI) since 2005. As we see, the decrease in aggregate results has caused a fall in both indicators, with ROE dropping to levels below those of 2005 and ROI to levels similar to those of 2006.

ROE and ROI FIGURE 6



Source: Authors' data.

Tables 3 and 4 show the trend in ROE and ROI for the various sectors. For the first time since 2005, the ROE and ROI of trade and service companies in the first half of 2008 went down, by twelve and four points respectively.

Companies in the industrial, construction and real estate sectors continued the trend begun in 2007 with poorer performance in both ratios, especially in construction and real estate, where ROE took on negative values due to losses sustained in the first half of 2008 and ROE was lower than the cost of debt.

The drop in the ROE of financial institutions was due to the inclusion in the sample of credit institutions that issue debt securities, which were not obliged to disclose periodic information in 2007 and previous years. Leaving out these firms, ROE rose by 19.2%, in line with previous periods.

The energy sector, however, saw an increase in both ROE and ROI due to non-recurring profits representing 37% of its results in the first half of 2008.

8 In this analysis no account is taken of insurers, whose results for the year accounted for 2.3% of the total results of the sample.

ROE

TABLE 3

	2005	2006	2007	1st 1/2 2008
Energy	20.6%	18.6%	15.9%	27.9%
Industry	16.0%	20.6%	17.7%	16.0%
Trade and services	25.4%	27.6%	32.4%	20.5%
Construction and real estate	19.4%	29.8%	18.3%	-3.6%
Credit institutions	17.2%	19.1%	19.1%	16.7%
TOTAL	**19.4%**	**21.4%**	**19.7%**	**17.9%**

Source: Authors' data.

ROI

TABLE 4

	2005	2006	2007	1st 1/2 2008
Energy	10.2%	9.6%	9.1%	14.7%
Industry	9.0%	11.6%	11.5%	10.4%
Trade and services	10.5%	10.8%	12.1%	8.4%
Construction and real estate	8.3%	10.1%	7.8%	2.9%
Credit institutions	2.8%	3.0%	3.8%	3.8%
TOTAL	**4.0%**	**4.2%**	**4.8%**	**4.3%**

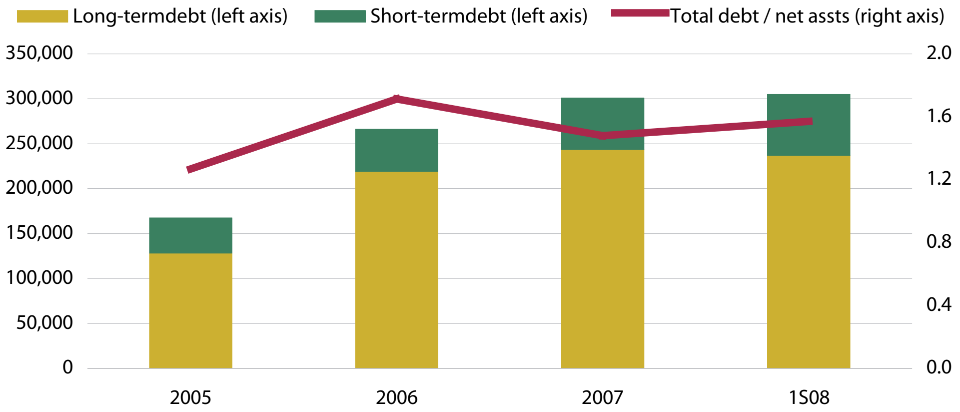
Source: Authors' data.

5 Borrowing

Figure 7 shows the trend in gross financial borrowing[9] (in millions of euros) by the companies forming the sample.[10]

Debt structure and leverage ratio

FIGURE 7



Source: Authors' data.

After several years of significant growth in borrowing (2003-2006), the rise in the first half of 2008 was just 1.4%. Contributing factors were fewer company acquisitions and the credit restrictions imposed by financial institutions.

9 Gross borrowing = Credit institution debt + issues of bonds and tradable securities.

10 Excluding credit institutions and insurers.

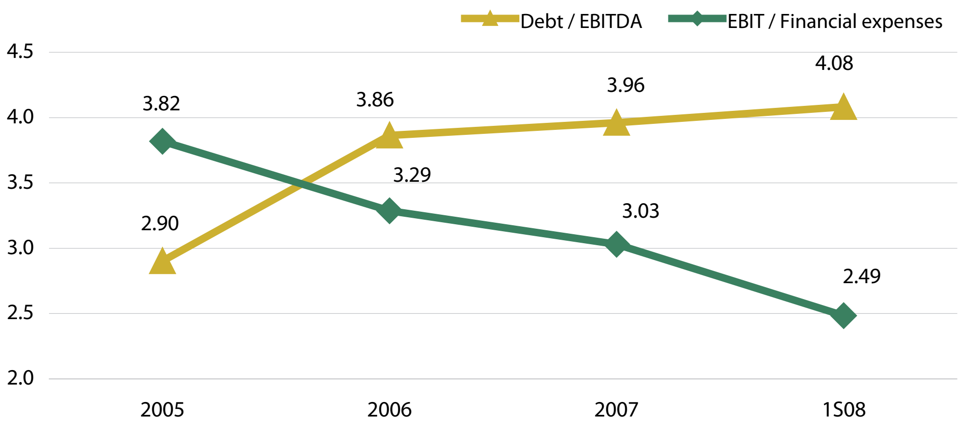
The percentage of short-term debt rose by more than three points over that at the end of the previous year, for reasons such as the violation of certain loan covenants due to the drop in company results. According to the current IFRS, when a company violates a debt covenant without getting a waiver from the lenders before the end of the accounting period, it must reclassify the debt concerned as short-term, regardless of its contractual maturity.

In the first half of 2008 many companies (and especially construction and real estate firms) renegotiated, or were in the process of renegotiating, the maturity structure and conditions of their financial debt, resulting in longer periods and higher costs for finance.

The leverage ratio, linking debt to assets, worsened in the first half of 2008, reaching a rate of 1.57, as against 1.48 at the end of 2007. However, 2006 levels were not returned to.

Figure 8 shows the trend in debt coverage ratio and financial interest, through EBITDA and EBIT. As a result of the poorer operating margins achieved in the first half of 2008, both ratios worsened considerably. This highlights the difficulty experienced by non-financial companies in servicing their debt with resources generated in ordinary business.

Coverage ratios FIGURE 8



Source: Authors' data.

Table 5 shows the trend in the level of borrowing and the main ratios by sector. We may highlight construction and real estate firms, whose debt/EBITDA ratio was 16.25, as opposed to 10.83 in 2007. Their EBIT/interest ratio dropped to 0.52 from 1.17 in 2007.

Trend in borrowing by sector TABLE 5

		2005	2006	2007	1s 2008
Energy	**Debt**	**58,586**	**59,191**	**69,172**	**74,798**
	Debt / Assets	0.93	0.89	0.78	0.77
	Debt / EBITDA	2.41	2.17	2.48	2.32
	EBIT / Financial expenses	4.02	4.65	4.10	4.58
Industry	**Debt**	**12,760**	**15,684**	**13,312**	**14,913**
	Debt / Assets	0.75	0.78	0.61	0.67
	Debt / EBITDA	2.07	2.07	1.82	2.01
	EBIT / Financial expenses	6.50	5.71	5.93	5.26
Trade and services	**Debt**	**55,710**	**91,522**	**96,941**	**106,190**
	Debt / Assets	1.70	2.52	1.70	1.93
	Debt / EBITDA	2.68	3.58	3.01	3.44
	EBIT / Financial expenses	3.37	2.44	3.23	2.81
Construction and real estate	**Debt**	**48,324**	**111,000**	**138,933**	**140,940**
	Debt / Assets	2.16	3.10	3.08	3.20
	Debt / EBITDA	6.52	11.52	10.83	16.25
	EBIT / Financial expenses	2.79	2.04	1.17	0.52
Adjustment		**-7,942**	**-11,199**	**-17,391**	**-31,711**
TOTAL	**Debt**	**167,438**	**266,198**	**300,967**	**305,130**
	Debt / Assets	1.27	1.71	1.48	1.57
	Debt / EBITDA	2.90	3.86	3.96	4.08
	EBIT / Financial expenses	3.82	3.29	3.03	2.49

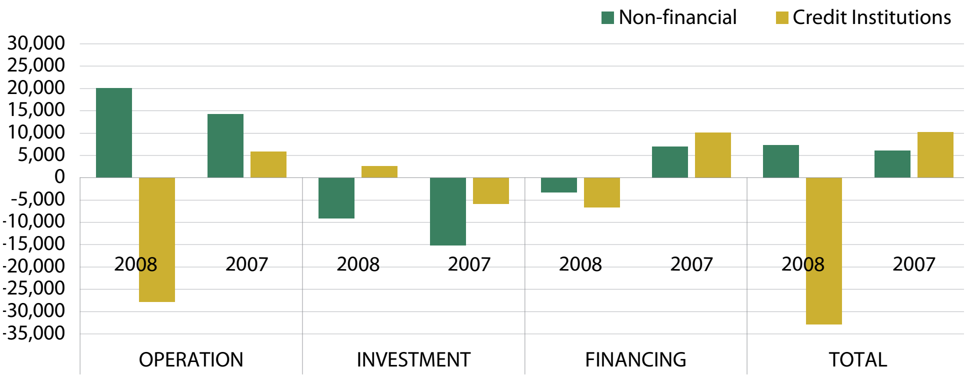
Source: Authors' data.

6 Cash flows

Figure 9 shows the aggregate trend in cash flows generated in first halves of 2007 and 2008 by the companies in our sample, except for insurers. Non-financial companies are distinguished from credit institutions given the different nature of their activities.

Cash flows generated FIGURE 9

(million euros)



Source: Authors' data.

As we see, the trend has been uneven:

- Non-financial companies. The cash flows generated in operations and disinvestment in the period (21.31 billion as against 12.27 billion euros in the first half of 2007) were able to offset outlays in financing activities (3.28 billion euros) and investments (30.85 billion euros), which remained stable relative to the previous period.

By sector we should note that only energy and trade and services saw an increase in their cash and equivalent flows. The former as a result of disinvestment in the period (11.70 billion euros) and the latter due to a reduction in dividends paid (3.92 billion euros less than in the first half of 2007).

- Credit institutions. The resources obtained were not enough to prevent the use by all credit institutions of part of the liquidity generated in previous periods – in the first half of 2008 the net flow from operating activities was negative, as compared to the positive flow in the first half of 2007 – to a large extent reflecting the liquidity strains on the financial markets.

  On the other hand, the tougher conditions for obtaining finance on the wholesale markets was reflected in an outflow of funds from financing activities, as opposed to the positive net financing activity recorded in the same period of the previous year.

7 Number of employees

Table 6 shows the average workforce, in aggregate and for the six sectors, in the first halves of 2008 and 2007. In aggregate terms the average workforce grew by some 7.4% relative to the same period of the previous year. In all sectors except industry this growth was prompted chiefly by the consolidation of dependent companies acquired in the second half of 2007 and the first half of 2008.

Average workforce by sector TABLE 6

	1st 1/2 2008	1st 1/2 2007	Variation
Energy	145,615	134,154	8.5%
Industry	234,196	212,039	10.4%
Trade and services	524,583	488,960	7.3%
Construction and real estate	431,334	407,123	6.0%
Credit institutions	436,076	411,405	6.0%
Insurance companies	37,819	31,771	19.0%
Adjustments	-29,711	-28,242	
TOTAL	1,780,025	1,657,336	7.4%

Source: Authors' data.

The ratio of net turnover to average workforce in non-financial companies showed aggregate growth of some 7.3%, similar to growth in the number of employees. But it is worth noting that this ratio fell in industry and trade and services. In the energy sector, though, it rose significantly, by 19.3%.

Average unit cost per employee in credit institutions remained at about 26,000 euros, while the ratio of interest receivable and similar income to average workforce improved to 17%.

8 Dividends

Dividends distributed in the first half of 2008 amounted to 11.52 billion euros. Table 7 shows the dividends distributed in the first halves of 2008 and 2007 by sector.

Dividends distributed by sector TABLE 7

	1st 1/2 2008	1st 1/2 2007	Variation
Energy	2,234	1,779	25.6%
Industry	547	747	-26.8%
Trade and services	3,305	6,135	-46.1%
Construction and real estate	894	827	8.1%
Credit institutions	4,790	3,779	26.8%
Insurance companies	235	154	52.6%
Adjustments	-482	-3,814	-
TOTAL	11,523	9,624	19.7%

Source: Authors' data.

As we see, in aggregate terms there was a rise of 19.7%, which was due mainly to dividends distributed by credit institutions and energy companies. But there was a notable fall in the dividends distributed by the trade and services sector, mainly due to the dependent companies of listed consolidated groups.

9 Conclusions

The economic slowdown and the turbulence on the financial markets, both internationally and domestically, are affecting the main financial magnitudes of companies with listed stock.

The crisis in the Spanish property market caused a significant drop in the volume of sales and the margins obtained by construction and real estate firms, which had high levels of borrowing due to corporate operations carried out in previous periods. This situation also led to a fall in the turnover of financial institutions, whose growth in previous periods had been closely linked to the housing and construction sectors.

The economic slowdown, along with the rise in defaults and bankruptcies, significantly affected the growth rate in the business and income statements of credit institutions. In addition, the liquidity crisis on the financial markets led to the use by financial institutions of liquidity resources generated in previous periods.

The industrial sector, and trade and services, were not immune to the general trend of lower results due to rising supply costs, more expensive energy and increased financial costs. Companies in the energy sector, however, exhibited an upward trend based on non-recurring positive results due to the disposal of financial instruments and interrupted activities.

Appendix

To facilitate interpretation, the following definitions were used in calculating ROE and ROI:

- ROE is calculated on the basis of results after tax[11], including those obtained from interrupted operations; results are adjusted by interest net of tax effect[12] for the purposes of calculating ROI.

  For financial issuers, the net interest used in ROI is interest and similar charges forming the intermediary's margin.

- Balance sheet magnitudes (net worth and investments) are calculated from the half-total of balances at the start and end of each period.

  Investments, for non-financial companies, are equivalent to total assets minus current liabilities that have no explicit interest, and to total assets for financial institutions.

11 For consolidated groups, results are before distribution to minority shareholders.

12 The tax rate used is the one actually applied by the company to work out book expenditure for corporate tax.

Short selling

Rodrigo Buenaventura (*)

*	Rodrigo Buenaventura is part of the CNMV's Secondary Markets Office.

1 Introduction

In spring of the year 1609 there was a sharp fall in the share price of the Dutch East India Company (Verenigde Oostindische Compagnie, or VOC), which may be regarded as the first corporation whose shares were traded on an organized market. Some shareholders blamed the fall on a group of investors led by the shipowner Isaac Le Maire (a major shareholder in the company and former board member). It seems proven that Le Maire[1] and his partners sold VOC shares for future delivery (in one year) that he did not hold at the time of sale. Then, by spreading false rumours or disclosing (true) unfavourable information on the company's accounts or the poor results of the consignments of spices arriving in ships chartered by VOC, they got the share price to fall and paid a cheap price for the shares that they had promised to deliver in closed forward sales. What is surprising about this true story is not only that the first case of short selling coincides with the first great listed company but also that the authorities, prompted by shareholders' protests, introduced a ban on the sale of shares not held by the seller, and reduced to one month the maximum admissible delivery period and established guarantees on delivery by the seller.

Between 19 and 22 September 2008, nearly 400 years later, the securities supervisors in the main financial markets recalled or introduced restrictive measures (see table 1) on short sales of bank shares. This movement came in the context of sharp falls in the share prices of financial institutions (beginning for underlying reasons other than short selling), some of which were starting to clearly show a spiral characterized by the sequence: share price depreciation—spreading of rumours about solvency—lack of confidence—stigmatization on the capital market—barring of access to financing—bankruptcy. Cases were detected on some markets of deliberate spreading of rumours about the possible insolvency of a particular company by "investors" who had previous taken short positions on their shares. Clearly this latter practice, as well as illegal, was extremely dangerous for the stability of the financial system, already going through a very difficult time.

As we see, the existence and regulation of short sales and the debate on the subject cannot be seen as new, for they have been part of stock markets since they first existed.

This article discusses how short selling is to be defined (section 2), its positive and negative effects on the stock market (section 3) and the most usual regulatory options (section 4), with particular reference to the Spanish case and the period following the adoption of measures in September 2008 (section 5).

1 Isaac Le Maire, an enterprising shipowner, always claimed that the fall in the share price was the product of the company's poor financial situation, of which the shareholders were not informed by the managers. As well as being the first known case of short selling it seems this affair was also one of the first cases of the reporting of irregularities in financial information and in the transparency of share-issuing companies.

Measures introduced in the most notable countries on short selling in September 2008* TABLE 1

US	Temporary measure: establishment of a requirement to buy back on D+4 in the event of fails in delivery, in any stock. If the mature sale is not closed, no further short sales (even with a prior loan) may be made (or accepted by members of the DTCC) until the positions have been settled.
	Ban on short sales (including loan-covered ones) in 799 financial stocks.
	It was made unlawful for short sellers to deceive brokers as to whether they hold enough stocks before the sale.
	Permanent measure: requirement to disclose short positions on more than 0.25% of share capital (and more than $1m)
UK	Temporary ban on short selling in any instrument (including derivatives) in financial stocks, up to January 2009. Market makers excepted. Breach of the ban is regarded as misleading behaviour.
	Requirement to disclose net short positions (with any instrument, including derivatives) in such stocks in excess of 0.25% of share capital. Failure to disclose is treated as misleading behaviour.
Germany	Ban on naked short selling in 11 financial stocks. Exemption for market makers.
France	Requirement to have 100% coverage in the form of shares (in financial institutions and insurers) in the stock to be sold (in France there were already minimum obligatory margins). Market makers and counterparties excepted. It is up to brokers, if they are depositaries, to check the existence of securities or to get their clients to declare that they actually hold them.
	Requirement to disclose net positions of more than 0.25% in the capital of financial institutions and insurers.
Italy	Initial reminder relating to financial stocks. Extended on 10/10 to all stocks, with a ban on even loan-covered short sales.
Spain	Reminder of the ban on naked short sales (including intraday ones), with exceptions for market makers.
	Temporary requirement to disclose net positions of more than 0.25% of the capital of financial issuers.

* A list of measures may be seen in the CESR Committee document with the URL: http://www.cesr-eu.org/popup2.php?id=5238

2 Concepts and definitions

Given the lack of commonly accepted definitions of short selling we must devote a short section to the basic concepts and how they are most widely construed.

Generally speaking, the term "short selling" is applied to the disposal of stocks not previously held by the seller. The clearest example is where a participant arranges a sale of securities in which it has no holding, either from past purchases or from loans of securities received before the sale. This practice is called *naked short selling*, as there is no cover for the securities being sold. A second type is *covered short selling*, which occurs where the securities have been procured previously, typically through a loan.

The sale is *short* in that it gives rise to a short position (favourable exposure to falls in the price of the stock being sold), as opposed to a *long* sale, namely one that offsets or reduces a long position (but never creates a short position).

As we will see, the concept of short selling is still not wholly clear and varies significantly depending on whether the perspective is that of the trade or of its settlement and delivery. Below we will use the terms "shares", "stocks" and "securities" interchangeably to refer to shares listed on regulated markets.

2.1 The delivery perspective

From the delivery perspective, short sales are just trades which in one way or another put at risk the delivery of the stocks sold. In this sense a short sale is defined according to whether the seller is able to get the shares required for delivery before the appointed delivery time. In stock markets, which normally settle trades three days after they are made, if shares are procured for delivery in a sale (arranged on D) on D+1, D+2 or even D+3, the sale may be settled without incident, respecting the terms of delivery agreed with the buyer. Thus if the seller manages to get the securities on loan on the day after the sale (and settles the loan on the same day), it can supply them to the buyer (or to the CCP, if applicable) on D+3. From the strict perspective of settlement, a sale would be "short" only if the seller did not hold the securities at the settlement time.

Several countries have mechanisms for seeking to ensure that the securities sold are delivered, though none address the short-selling problem as explicitly and directly as Spain, as described in more detail in point 4.2. In some cases (e.g. France), prior availability or guarantees are required, which the seller's broker must check and deposit to cover the sale. In others, penalties are established in proportion to sales that mature but do not go through.

In any event, the settlement perspective addresses only one aspect (probably not the most important one) of short selling.

2.2 The trading perspective

From the trading perspective, short sales are defined as trades in which the seller sells more shares than it holds at the time of sale. This concept is quite independent of the delivery time, of whether trades can be cancelled or are final, or of any corrective measures in the post-trade process.

From the trading perspective, a sale may strictly be said to be short if the seller sells securities that it "does not hold" at that time, without going into whether it gets them immediately afterwards or whether it has the means to get them before the settlement.

How "time" is defined is important here[2]. For in some countries a sale and a subsequent purchase of the same amount and security, but within the same day, are regarded as two mutually netted trades, the time of which is not considered. But in others a sale with no prior availability of securities is short even if a purchase of the same amount and security is made the next minute. So there is no international consensus as to whether to regard sales covered by intraday purchases as short.

2 Time, in this context, has no single, objective definition (if it has one even in physics). The convention in the financial markets is that one day is normally the minimum unit of time for the purposes of calculating an interest rate (except in countries with hyperinflation, where fractional time units are needed), and also in some cases the minimum unit in defining the concept of "before" and "after" the time of sale, for the purposes of defining short sales.

The concepts of "before" and "after" may therefore refer below, depending on each country's regulations, to a number of days before or after a sale (with time as a "discrete variable", with a minimum and indivisible unit of one day) or to any moment before or after a sale (with time being "continuous").

2.3 Covered sales and naked sales

As mentioned above, there are two basic types of short selling depending on whether the seller holds no securities before arranging the sale or whether it has previously taken securities on loan. If it does not have them on loan, the short selling is *naked*. If it has arranged a loan before the sale, the short selling is *covered*.

As may be seen, taking the securities on loan does not impede the transaction: the seller normally uses the securities so obtained to settle the sale (on D+3, for example). On a later date (10 days, one month, three months) it has to return the loaned securities, buying them back on the market (no later than T-3, where T is the date set for the return of the loaned securities). If the price has gone down since the sale was arranged, it buys the securities back at prices lower than those charged in the short sale and makes a profit. If the price has gone up, it makes a loss.

Though the difference between the two types of transaction (loan-covered or naked) is clear, there are many differences and nuances between countries. This is because there are few jurisdictions in which there is a legal definition of short selling, so the concept is subject to market conventions or the practice of each supervisor. Let's look at two examples:

- most countries regard sales of stocks with purchase or conversion options not yet exercised as naked short sales;
- some countries consider that short sales are covered if the seller has previously exercised a conversion right or purchase option that means it will receive the securities, while other countries do not even see this procedure as a short sale.

2.4 Short positions

The term *short position* normally refers to the existence of a series of trades (in cash or derivatives) entailing that the holder is favourably exposed to any negative change in an asset's price. That is, a short position on an asset is any combination of trades meaning that, where the price of the asset falls, the holder of a short position will make a profit (i.e. the position will gain value). A short position may be taken in various ways such as via a covered short sale, a sale of a future, a purchase of a put option or an equity swap trade. So not all short positions are taken via short sales, but all short sales establish or extend a short position.

3 Advantages and risks of short selling

As we said above, short selling has been attacked and defended since the beginnings of stock markets. Though this article's purpose is not to examine empirical evidence on the subject, we will now review the pros and cons normally associated with the practice.

3.1 Benefits

Since it first appeared, even short selling's critics have recognized that the practice has certain benefits for a mature market:

- Provision of liquidity

  Perhaps the most often mentioned benefit of short selling is its positive effect on market liquidity. Like any speculative strategy[3] (in the most positive sense of the term), naked selling (and subsequent buyback) improves the market's liquidity by channelling orders (first sale orders, then purchase ones) which would otherwise not exist.

  The existence of investors specialized in making a profit on bearish markets or from overvalued stocks clearly enhances liquidity and depth on both sides of the order book.

  They also play a major indirect role in the work of market makers (whether or not such figures are recognized on a market). Thus firms that quote bid and ask prices on their own behalf often make short sales in the course of a session when their sale positions are previously (or more strongly) "attacked" than their purchase ones. For market makers, short selling is an inextricable part of their activity.

- Market efficiency

  As well as providing liquidity, short selling is also a useful means of assuring market efficiency, in that prices instantly, or at least quickly, reflect all the information available. When a company shows weakness in its fundamentals that entails that its market price is not justified, the (downward) price adjustments may be slower without possibility of short selling than with that possibility. By adopting short-selling strategies in the stock of overvalued companies, markets adjust to their fundamentals more quickly and accurately.

- Mitigation of bullish bubbles

  Periods of euphoria and bullish bubbles are high-risk events, as seen in the last 18 months, which may (when they burst) jeopardize the stability of the financial system and the global economy. Short selling plays a positive role here by limiting the overvaluing of securities and mitigating episodes of irrational exuberance.

3 Speculation is needed in order for a market to develop, and if it does not predominate, it gives the market liquidity at times when this is most necessary: the speculator buys when "no one" wants to do so and removes excess paper from the market, and sells when "everyone" wants to buy and there is a lack of paper, which otherwise would not get onto the market. It is another matter when speculation is by means of corners, squeezes or other abusive or manipulative practices based on an abuse of market power.

- Hedging of long positions/interrelation with derivatives

  In the management of portfolios whose derivatives sometimes have little liquidity, short selling can neutralize the risks of long positions in derivatives (not in cash positions, as that would not be a short sale). Similarly it can enhance the liquidity of derivatives markets, where a long position must often be hedged on the cash market with a short cash sale.

- Arbitrage

  Short selling allows strategies that result in greater market efficiency and the correction of price distortions between competing trading venues or in pairs trading. This practice does not involve a short position in the market as a whole but a correction of relative prices between two securities, generally in the same sector. Also in the Europe, since the MiFID directive, a single security will be quoted in several trading venues, so buying in one and selling (on occasion with short sales) in the other represents a mechanism to make prices converge. All these practices result in greater market efficiency and so in lower transaction and capital costs.

3.2 Risks

Although one of the main virtues of short selling is precisely that of bringing prices down to levels consistent with each company's theoretical value, overshooting phenomena may occur. This will be of no great significance if we look at markets in a dynamic long-term perspective, but it may be an extraordinary disruptive element when the fall in prices generates undue risk signals that trigger "sympathy" sales or even panic in other investors.

Such reactions may subsequently be corrected but they have two peculiarities that are worth analyzing:

- Generation of mini-trends

  The psychology of market participants and a failure to observe certain safeguards may turn what was initially a "gentle" adjustment into a sharp bearish trend. On this problem, the advocates of short selling normally argue that all short sales are followed at some point by a buying movement for the same amount to close the positions, and so that it is a zero-sum game: if we wait long enough we find a net result equal to zero in any short-selling strategy. But for some authors this approach is fallacious in that the speed and sharpness of a fall triggered by a series of orders may, in so far as it involves other (long) participants in the selling movement, be greater than the later recovery caused by purchases to close the short sales. That is, the effect of short selling on prices is not always equal to zero and may rather be negative (or exceptionally positive, when there is a short squeeze and short sellers have to accept rising or even exorbitant prices in order to be able to close their positions).

- The relationship between stock market quotations and the perception of an issuer's financial soundness (especially for banks).

  The financial sector is underpinned more than any other by the perception of its solvency by investors and the general public. It has often been seen (most recently in September 2008) that a sharp fall in shares issued by financial institutions may seriously affect the perception of their solvency, which at times of high uncertainty may entail a barring of access to wholesale credit or even the withdrawal of deposits by customers, potentially making the institution bankrupt. In so far as short sales occur at a speed liable to accelerate falls in price above a certain rate, the effect may be devastating for such an institution.

The two risks mentioned so far cannot be attributed solely to the existence of short selling. We should note that as yet there is no firm evidence to support the assertion that short selling caused the bearish spirals in bank share prices in 2008. It cannot even be said that short selling was one of the primary triggers of the stock market falls, of more than 40-50% on all markets, in 2008.

- Misuse associated with market abuse

  One unlawful way of making a profit from spreading false rumours or using insider information is to take short positions before spreading the rumour or publishing the adverse information. In this case short sales are a means of taking advantage of the unlawful conduct. But really the role of short selling in such manipulative behaviour is no different from that which may be played by a position sold in futures or a bought put.

In the case of naked short selling there are several additional risks:

- Inflation of balances:

  While in loan-covered short sales the total sale (and purchase) balance cannot exceed the amount of tradable capital (provided that a sale cannot be covered with securities loaned previously), this is not so with naked sales. In this case, each naked short sale increases the balance of "open" positions by the same amount and the securities are directly inflated (albeit temporarily, while short positions are closed with purchases becoming due a few hours or days later). So naked short selling directly increases the balance of existing securities – the sum of securities registered plus those bought from short sellers – by a ratio of 1:1[4].

- Jeopardizing the delivery of securities:

  If a trader making a short sale has no ability or intention to get hold of securities before the time when the transaction is to be settled, it is putting at risk the timely and appropriate delivery of the securities traded, which entails extra risk and less efficiency and market confidence in the finality of transactions. This normally requires, in turn, more active and costly management of the central clearing mechanism, resulting in higher transaction costs for all participants.

It is worth considering another aspect of naked short selling that does not strictly represent a risk. In a covered sale, the seller previously takes a securities loan, provides collateral (in the form of cash or securities) to the lender and pays interest for the duration of the loan, i.e. it commits its own resources or assets and bears the loan's cost. In a naked short sale the seller provides none of its own resources

4 Some authors (Miller, 1977) liken the short-selling mechanism to the process of creating money supply through the banking multiplier. In the process of creating bank money, a deposit becomes a loan at a factor of (1–% of reserve) which is in turn deposited in another bank that continues the same process. In the case of naked sales, the multiplier factor is 1, in a similar way to how the money supply would be reproduced with no (legal or self-imposed) reserve requirement.

(though it does run a risk – of making a loss if the strategy proves mistaken) and may even take on a degree of leverage which, unlike in a loan-covered sale, may be infinite (zero own resources for each short position taken). In especially volatile markets, this difference between the two types of short selling represents a clear risk and a sharp contrast with other ways of taking short positions (via futures, CFDs, equity swaps, etc.) which do have guarantee, remuneration, collateral or daily mark-to-market mechanisms.

4 Regulatory options

Securities market regulators have historically taken various approaches in dealing with the risks involved in short selling, or some types of it. As in many other aspects of financial regulation, there has been no lack of pendulum swings, with periods with no curbs (generally of euphoria) alternating with others (generally after serious asset deflation events) in which tough restrictions are imposed on the practice.

Thus, after the first ban in 1610, successive bans or restrictions are chronicled, like those of 1812 and 1937 in the US. The rules and degree of regulation appropriate to the practice have also been periodically analyzed and reviewed. For example in the US, the country with most tradition of regulating developed securities markets, reports were published (in several cases with congressional involvement and public consultation) on the pros and cons of regulating short selling in 1937, 1963, 1976, 1986, 1991 and 1997. It is fair to say that the review and discussion of to what extent, if any, short selling should be regulated is one of the most debated issues in the regulatory histories all national stock markets.

The options considered to date in the various countries are basically as follows:

1 Transparency

The requirement for some type of disclosure of details of short sales is normally one alternative. The variants range from monthly disclosure of volumes of aggregate short positions to daily disclosure of securities loans or short positions in each security. The aim is that participants should get an idea of the level of *shorting* on the market at a certain frequency. In most cases it is secondary market operators that draw up and disclose the statistics.

Disclosure of figures on securities loans, in so far as such transactions are a requirement for covered sales, may give useful information to the market. But two important caveats should be made:

a) Not all loans are for covering short sales. Other operations, such as dividend stripping or resolving settlement incidents may require loans to be taken out, so statistics on outstanding loan balances should not be taken as a true and consistent indicator of the volume of short sales.

b) In some countries, and especially Spain, there are serious problems of true and fair representation in loan registration. The reason for this is the lack of correspondence between actual loan cancellations and cancellations reported to Iberclear for registration purposes. It is well established that many fewer cancellations than those actually made are reported, so the outstanding balance of loans (or the difference between loans taken out and loans cancelled, which determines the net flow and therefore the variation in loan stock) is probably overestimated, with there being many fewer outstanding loan transactions than are registered. Without going into the detailed reasons for this (which lie in the institutional complexity of relending chains and the practices of foreign brokers, especially in London, where most lending activity is based), we should note that public data from the special loans register should not be taken as an accurate indicator of the level of short selling in a security.

2 Flagging of short sales

This measure is not actually in itself a regulatory solution but rather a means of applying other measures: a solution adopted in several countries to facilitate the application of mechanisms for transparency or to restrict short selling. It consists of putting a flag on each short-sale trade that a broker processes for execution. Though the flags are not visible in the order book, the market and the supervisor can detect them and take them into account when applying transparency measures (end-of-day or end-of-week publication) or uptick rules. With this measure, short-sale orders bear a hallmark allowing them to be traced from start to end and given special treatment.

3 Ban on naked short selling

In some venues (Hong Kong, Australia, Spain, France, the US) there are or have been bans or restrictions on naked short selling. The options range from a requirement for a specific declaration by the broker's client that no short sale is being made, to a requirement for a deposit of securities to sufficiently cover the sale transaction. In most countries the restrictions do not apply to market makers.

4 Disclosure of net short positions

One possible measure is a requirement to disclose net short positions in excess of a certain percentage of tradable stock in a particular company. Among the measures adopted in September 2008, some countries made it compulsory to disclose any net short position in excess of 0.25% of tradable stock in a particular issuer (typically bank issuers, for the reasons mentioned above).

5 Tick rules

A tick rule limits the possibility of making a short sale according to the market price and the sale order. In its commonest form (the uptick rule), no short sale order can be made at a price equal to or lower than the last traded price, or in some cases, lower than the best sale price. The purpose of such rules is to prevent short sales being made at falling prices and setting a trend, so their price is limited according to that given in other orders at any one time. Indeed up to 2007, the US had had an uptick rule in force for several decades.

No single pattern is to be found in the way in which the main regulators have adopted these measures. Though preferred options may be detected in some areas (tick rules in North America and Asia, restrictions on naked sales in Europe), there is no consistent approach across the main trading venues.

5 The situation in Spain

5.1 Legal provisions

The legal restriction on naked short selling in Spain stems from the Trading Exchanges Regulation, enacted in Royal Decree 1506/1967. The applicable parts of that Regulation (some parts were repealed by the Stock Market Law, LMV) are ill-suited, given their origin and age, to the nature of a modern and demutualized market and urgently need full reformulation, as required by the recently amended LMV article 31.bis, which gives the governing body of each official market the responsibility of adopting provisions and submitting them for review by the CNMV. As the old regulation is in force, though, it still has to be applied.

Article 64 of Decree 1506/1967 provides that: "In the cash market, sellers may trade only in securities of which they are already the owners." Thus it provides a clear ban on naked short selling.

LMV's provisions do not change this, and indeed reinforce it:

- on one hand, art. 36 recognizes short selling in the provision that: "Without prejudice to other types of loan, securities traded on an official secondary market may be loaned for the purpose of subsequent sale, to be the subject of a loan or to serve as collateral in a financial transaction";
- on the other hand, art. 39 states that: "Anyone holding the position of member of an official secondary market shall be obliged to execute, on his clients' behalf, the orders that he receives from them for the trading of securities on the corresponding market. However, his compliance with this obligation, in the case of cash trades, may be subject to the receipt of proof of ownership of the securities from the ordering client (...)".

That is, without going into any thorough legal analysis, it may be said that the current regulation recognizes loan-covered short sales and forbids naked short selling.

5.2 The settlement perspective

At settlement level there are also mechanisms to limit and discourage naked short-sale transactions. These mechanisms are designed to guarantee the finality of transactions right from the trade, preventing delivery failures that might unnecessarily jeopardize the settlement system. Accordingly they do not address the trading perspective, though they have indirect effects, as we will see, that have played a big role in limiting short selling in Spain.

The Spanish settlement system has, probably more than any other, developed rules that penalize short sales (defined from the settlement perspective) in all cases in which the seller does not hold securities before the settlement time or obtains them in purchases after the settlement date.

This penalty is twofold: it consists of a fixed amount of 0.1% per day of delay (on the theoretical settlement) and the difference between the price agreed in the sale and the price at which the system (Iberclear) buys back the securities on the market on D+4. That is, the system confiscates the profit from a short sale in a bearish phase by penalizing the participant for an amount equivalent to all the profit that it would have made.

There is no penalty if the seller gets the securities by a purchase on the day of the sale or by a loan on the same or next day, up to the settlement day, D+3.

From the settlement perspective, this penalty system makes sense in a country where stock market transactions become final at the very time of sale: in so far as loans after day D represent a mechanism for being able to settle trades in the event of possible failures in the receipt of the securities, their use is not penalized. Suppose a seller sells 100 shares on D, believing that on D+1 he will receive a transfer of 50 and that a sale of another 50 will go through. But the sale does not go through due to an unforeseen event, so at the end of D+1 he sees that he has no securities available to settle the sale on D+3. In this situation he takes a securities loan for 50 shares on D+2, effective on the same day, with the aim of adding them to the purchase already settled (correctly on D+1) and thereby being able to deliver the 100 shares as arranged, on D+3. From the settlement perspective there is no delivery failure here because the outcome of the transactions is not put at risk.

In view of the above it may be understood that the level of naked short selling in Spain was lower than in other countries that had no such restrictions at settlement level[5].

5.3 Resolution of the CNMV's Executive Committee of 22 September 2008

The exceptional circumstances undergone by stock markets in the second and third weeks of September 2008 led several stock market supervisors to take concerted action to establish or recall restrictions on short sales. Naturally no supervisor regards short selling as the trigger or cause of a slump on this scale, or even as the main element in the price collapse in some sectors. But all agree in pointing to short sales (or at least naked ones) as a catalyst of the process in particular companies[6]. One of the few measures that could be taken to curb it or slow it, with a view to the possibility – not at all remote, as seen since – of a chain of bankruptcies or public interventions in major international banks, was to mitigate at least temporarily the element of bearish speculation in banks. The convergence of prices with the underlying value of such institutions could be seen as a matter of time. But regulators considered that they could intervene so that the process would not take place disorderly and with panic.

This is the context of the CNMV Executive Committee's resolution of 22 September 2008. First it undertook to publish net short positions of more than 0.25% of the stock of firms in the financial sector, a measure similar to that taken by other su-

5 Restrictions that are indeed much criticized by international associations of financial intermediaries at times of calm, but which have proven very useful at times of volatility or in bankruptcy situations in major participants or clients in the system.

6 It is very interesting to see how the literature that questions the effectiveness of the measures taken (Marsh and Niemer, 2008) analyzes average effects in the market before and after the measures. But in September 2008 some supervisors took measures not to contain the average prices of bank securities (which is impossible) but to make it harder for a particular bank being pointed at as liable to have problems to be taken advantage of and brought down by short sales. That (marginal, not average) effect of the measures, which as the aforesaid authors say is key to evaluating them, cannot easily be detected or included in quantitative analyses.

pervisors such as the British FSA, designed to extend the transparency obligations that already applied to long positions (significant holdings) to the short side of the market. The logic of this measure is to make bears disclose their positions when significant, which entails, as well as the greater risk in offloading them if the market bases its position on these data, the identification of the main potential beneficiaries of further price falls, a significant detail in an analysis of any malicious spreading of false rumours so as to increase gains from short positions. This does not of course mean that bearish investors habitually engage in market manipulation (and nor can this be said of bulls). Bearish positions are as useful on an orderly market as bullish ones, so it may be asserted that both should be subject to transparency requirements.

The reminder of the ban on naked short selling for all securities was accompanied by an assessment of its practical scope.

On one hand it was noted that intraday naked sales come under the ban provided by the 1967 regulation. Perhaps this is what had most impact on a market which, used to a lack of penalties at settlement level on intraday naked sales, might have assumed implicitly that it was permissible to make naked sales at the start of the session and to buy back after closing the position before the end of the session. The Resolution recalls that this procedure, though acceptable for settlement purposes, cannot be regarded as in line with current trading rules. Intraday naked short selling has exactly the same effects and risks as those mentioned above in point 2.2. and is therefore able to generate bearish mini-trends in a security that are not always counteracted by later buybacks.

To say that intraday naked selling transactions have no effect on prices is like saying that intraweek or intrayear transactions (selling naked in January and buying back in December) have no effect on prices. Leaving aside the settlement problem, the period (in a discrete time approach) used to define the naked selling concept is irrelevant: intraday transactions have the same effects as any others in so far as the time at which the market is interrupted (night, weekends, public holidays) is not relevant to how prices are determined in the following periods. In a round-the-clock market such as the currency market, this point is self-evident.

Likewise, intraday naked selling also causes inflation in balances which, though it goes unnoticed in normal situations in which positions may be closed before the session closes, may cause serious problems when trading in a security is interrupted for any reason without prior notice (mid-session suspension of trading that lasts several sessions, such as in an unforeseen bankruptcy scenario, etc.). In such cases the oversold volume (the amount of naked sales) in excess of the balance of securities in circulation in the system may not be settled, generating inefficiencies in settlement and conflictive situations from the corporate perspective.

Given all this, and as the 1967 regulation says nothing about exempting intraday trades from the ban, the Resolution of 22 September extended the same rule to any naked sale (whether or not it is closed with purchases a few seconds, minutes or hours later).

The other novel element in the Resolution is its special treatment of market makers, which may be likened to an exemption. Given the lack of a legal definition of this concept in the Spanish equity market, the Resolution and the subsequently published FAQ answers clarify the concept as regards the operations of market makers.

This is especially important in allowing institutions that enter corresponding orders on both sides of the book, making the market, not to get into a situation of regulatory risk. This type of activity is essential to ensuring depth in the order book and in almost all countries with restrictions (permanent or temporary) on short selling there are exemptions for market makers.

5.4 Effectiveness and impact of measures taken

The short time since the introduction (or reminder) of measures on short selling by several countries makes it difficult to evaluate the measures' effectiveness and impact. Also the exceptional trends in stock markets since September (with volatility that has few historical precedents) make it tricky to distinguish the effects of the ongoing crisis from those that may have stemmed from these measures.

In any event, the early data analyzed would seem to point to a lack of significant changes in the relative behaviour of securities subjected to the new requirement, introduced in Spain, to disclose short positions as distinct from other securities. As to market liquidity, looking at volumes traded and turnaround rates, no reduction in the liquidity of the official secondary market is to be observed following the Resolution's publication.

Some widening in average bid-ask spreads is observable for continuous market values as a whole on the days following the Resolution (which were in any event a time of great volatility, which normally shows a positive correlation with the size of such spreads). The widening of spreads, which might point to a drop in liquidity or, in other words, a rise in the cost of getting into or out of a stock, seems to have had a temporary effect, for in early December average cent-denominated spread figures were back to levels comparable with annual averages before the Resolution of 22 September (though not as regards the spread percentage on share prices, given the sharp tumble taken by prices).

As regards intraday transactions, a reduction in volume is observable (of some 5 percentage points on the total traded) in the period following the Resolution. As regards settlement efficiency, less use of after-sale loans is apparent in transaction records, as is a level of system efficiency slightly higher than the averages prior to the Resolution.

6 Conclusions

The debate on short selling has reappeared with the recent crisis in a market – the share market – which has since its very origins seen an argument between advocates and detractors of short sales. In this context the measures taken by securities supervisors in September 2008 constitute an attempt to curb the bearish spirals which in those days threatened to jeopardize the system's stability, though they will probably be temporary measures and be progressively lifted in the coming months, as the situation in the markets returns to more normal parameters.

However, despite the measures' temporary nature, the supervisory architecture and current close cooperation within the international stock market organizations (CESR and IOSCO) may cause a convergence, albeit slight, in views on the issue, whether or not it takes the form of similar regulation in the various countries. The establishment of a special working group on short selling in IOSCO, in which the CNMV is taking part, is a pointer in this direction.

In Spain, the need for a renewed and updated system of stock market trading rules (Stock Exchange Regulations) has also become evident with regard to short selling. Until this is provided, supervisors should continue to monitor transactions so as to ensure that brokers' actions are lawful. In any event, the trade-off of observable risks and benefits means that we should recognize the contribution of covered short selling to market efficiency, and note the risks of naked selling.

7 Bibliography

Blount, E.W (2006). "The impact of short sales and securities lending on capital market portfolios-1990 through 2006". Center for the Study of Financial Markets Evolution (www.csfme.org).

IOSCO (International Organization of Securities Commissions) Technical Committee (2003). *Report on transparency of short selling* (www.iosco.org).

Marsh, I. and Niemer N. (2008). "The impact of short sales restriction". International Securities Lending Association (ISLA; www.isla.co.uk).

Miller, E (1977). "Risk, Uncertainty and Divergence of Opinion". The Journal of Finance, volume 32, Issue 4, 1151-1168.

Staley, K (1997). *The art of short selling*. John Wiley and sons, Ed.

US Congress. "Short-Selling Activity in the Stock Market: Market Effects and the Need for Regulation (Part 1)" (House Report), H.R. Rep. No. 102-414 (1991).

US Securities and Exchange Commission. "Short Sales: SEC Concept Release", 1999. (www.sec.gov.us).

Van Dillen, J.G., Poitras and Majithia (2006). "Isaac Le Maire and the early trading in Dutch East India Company shares". Pioneers of financial economics, v.1: Contributions prior to Irving Fisher. Ed. by Geoffrey Poitras. Edward Elgar Publishing.

Van Dillen, J. (1935). "Isaac le Maire et le commerce des actions de la Compagnie de Indes Orientales". Revue d'Histoire Moderne: 5–21, 121–37.

The financial crisis and fair value: the debate on its impact and evaluation of the measures adopted

Eduardo Manso and Víctor Rodríguez (*)

* Eduardo Manso is a member of the Financial and Accounting Reports Department of the CNMV and Víctor Rodríguez of its President's Office.

1 Introduction

The financial crisis has been growing with increased intensity since the summer of 2007, although it was in the second half of 2008 that its contagion effect was most clearly seen in Europe. A sharp reduction in liquidity in the system worsened the position of those entities which were already in a weakened position in terms of solvency.

In addition, financial entities in countries such as France, the United Kingdom, Germany, Belgium, Holland and Italy, have had to resort to state aid to ensure they could continue operations. The situation has obliged nations and international bodies to adopt urgent coordinated measures.

The fifteen members of the Eurogroup who met on 14 October 2008 agreed a number of measures. Among them were that each Member State of the European Union, depending on individual circumstances, should increase the amount covered by the deposit guarantee fund to a minimum of 50,000 euros, and inject sufficient finance to ease the lack of liquidity and the financial difficulties experienced by financial institutions.

A few days earlier, a meeting in the ECOFIN Council of 7 October had agreed additional measures dealing with the scope of financial information that financial institutions listed on a regulated market should publish on a regular basis.

This article analyses the debate on the application of the accounting concept of fair value in the current financial crisis and reflects on some of the measures proposed to ease its supposed procyclical effects.

Some of these measures have resulted in modifications or interpretations of the financial information that entities with securities admitted to trading are obliged to submit to the competent authorities in accordance with the International Financial Reporting Standards (IFRS) adopted by the European Union. Section 2 describes the concept of fair value and discusses the controversy that it has attracted during the current crisis. Section 3 outlines the initiatives adopted in recent months by the various international bodies. Section 4 analyses in more detail the measures taken by the IASB, the body that draws up the international accounting standards, to deal with the problems related to financial instruments traded on inactive markets and how to measure their fair value. Section 5 deals with the initiatives taken by the European securities supervisors within the CESR framework. Finally, section 6 includes some reflections on the lessons to be learned from these developments and the impact they may have on the process of the international convergence of financial reporting standards.

2 Fair value and the current crisis

Fair value is a core concept in international accounting standards. It contrasts with the concept of historic cost which has traditionally been used in accounting standards in continental European countries. Put most simply, fair value could be equated to market value, meaning the value at which assets and liabilities on the balance sheet could be exchanged at the accounting reference date of financial statements. Historic cost reflects the amount paid or received for the acquisition of the asset or incurrence of the liability. As a result of this conceptual turnaround the financial information provided by entities now gives a truer picture of their economic and financial reality.

The formal definition of fair value proposed by the IASB is now found in IAS 39 *Financial Instruments: Recognition and Measurement*: "Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties, in an arms-length transaction." But this is not the only possible definition of fair value. This is why the IASB is working on the process of improving its definition so that it can be used to unify the methodology for determining fair value in all the international standards, as well as achieving convergence in this respect with the standards in force in the United States (US GAAP). In the GAAP, fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date. Unlike the previous definition, which does not stipulate whether we are dealing with an entry or exit price, the US standards specify that it is an exit or selling price of the asset or liability. It is in the area of financial instruments that the IFRS apply the concept of fair value most extensively. IAS 39 deals with its recognition and valuation, and IFRS 7 with the analysis of information that should be provided with respect to these instruments.

The financial crisis has made clear that when there is a downturn in markets and the prices of financial assets are falling, entities which had previously entered significant profits as a result of increased prices now have to reflect the lower values in their equity and profit and loss accounts. Voices have been raised claiming that the concept of fair value is to blame for intensifying the downward[1] trend of the markets. Entities have tried to get rid of instruments whose deteriorating value was a drain on their yearly profits and their solvency situation. However, this procyclical behaviour appears to be more directly linked to the fact that entities lack the "cushion" of capital to allow them to assume losses in times of crisis without the need to issue new capital instruments.

In addition, the aim of restoring confidence has to include an increase in transparency regarding the real financial strength of entities. This involves increasing the application of good valuation practices and avoiding reforms of accounting standards that weaken the way in which accounting statements reflect the impact of market turbulence on the economic reality they should represent.

1 A number of bodies have declared themselves against fair value in the current situation on the grounds that market participants are behaving illogically and over-reacting. They claim that market prices are no longer "fair" and that new fundamental values have to be used that exclude exaggerated premiums on an unfounded aversion to risk. This situation is worse in illiquid markets, where there are few transactions and the use of valuation techniques could reflect fair value better.

Despite the above, it should be admitted that the financial crisis has also made clear that the valuation standards[2] contained in the IFRS need to be fine-tuned to respond as well as possible to extreme situations such as the current one, in which market references are lost through inactivity or because an increased number of forced transactions. The following sections cover the proposals and actions undertaken to this end.

3 Initiatives adopted

3.1 Financial Stability Forum

In October 2007 the Financial Stability Forum (FSF) was mandated by the economy ministers and governors of the central banks of G7 countries to analyse the causes and weaknesses that had led to the financial turmoil, and to propose recommendations designed to enhance the resilience of markets and institutions. This mandate was to produce results in April 2008 coinciding with the meeting of G7 ministers and governors.

In its report, the FSF stated that the IASB should reinforce its standards to strengthen disclosure requirements for valuations, including the methodologies and the uncertainties related to these valuations. It also asked the IASB to improve its guidance on valuing financial instruments when the markets in which they are traded are no longer active. To this end, the FSF called on IASB to set up an expert advisory panel in 2008[3].

The FSF report also recommended that financial institutions should establish rigorous valuation processes and make robust disclosures.

In June 2008 the FSF published a document monitoring the implementation of its recommendations. It pointed to the fact that the IASB was speeding up its work on the accounting standards and disclosure of information of off-balance-sheet vehicles and that it had planned to issue for public consultation a proposal for a standard on the consolidation of special purpose vehicles (SPV) and other similar entities, as well as the corresponding disclosures[4]. It also pointed out that the IASB had followed its recommendations in already announcing the creation of the expert advisory panel mentioned above. Finally, in October 2008 the FSF issued a follow-up report on the implementation of its recommendations.

In addition, the FSF stated that the IASB, in collaboration with the expert advisory panel, had issued a draft paper on valuation and disclosure practices when markets are no longer active.

The FSF also informed on the steps taken in September by the SEC together with the staff of FASB, the US accounting regulations body, and in October by the FASB staff itself (which issued a FASB Staff Position with additional guidance).

2 As well as disclosure requirements.

3 This is the group mentioned above.

4 By the end of 2008.

In short, the FSF recognised the significant efforts made by the accounting regulators and urged them to speed up the work to improve their guidance on valuating instruments in inactive markets and achieving convergence in standards.

3.2 Senior Supervisors Group

This group is formed by France, Germany, Switzerland, the United Kingdom and the United States. In March 2008[5] it issued a report called "Observations on Risk Management Practices during the Recent Market Turbulence". This work summed up the results obtained from a review of the practices of eleven major financial institutions. It also reflected the conclusions of a roundtable discussion between participating supervisory agencies and industry representatives held in February 2008.

The report included some aspects relating to financial information and the practices used to determine fair value. It explained how some firms had failed to price properly the risk of exposure to certain off-balance-sheet vehicles. This has led to significant reductions in the value of these entities' assets. The firms that have managed to avoid these problems have been those whose managers have exercised critical judgment and firm discipline regarding how they valued holdings of complex or potentially illiquid securities, both before and after the onset of the market turmoil. These firms had dynamic risk measurement systems that were capable of changing underlying assumptions quickly to reflect new circumstances. They also chose to develop their own methodologies for properly valuing exposure in structured products, given the doubts as to the valuations carried out by credit rating agencies. Another feature characterising this group of entities is their consistency in applying valuations, including both their own positions and those of their counterparties.

Thus those few entities that used valuation models for their exposure to super-senior tranches of securitisation of subprime mortgages before the third quarter of 2007 were able to take the appropriate decisions, such as selling positions (when still possible) or contracting hedges, and thus avoid significant losses in their portfolios.

The entities that suffered large losses were those that trusted primary market prices as inputs in their valuation models, when there were practically no transactions in the secondary market. It was not unusual for these entities to also trust the valuations of credit rating agencies.

In April 2008 the Senior Supervisors Group published another document containing a review of the practices of disclosure of information on exposure to certain instruments that the market considered to be high risk at the time or that involved a higher risk to that initially forecast. This time, the scope of the work was extended to twenty global financial institutions. The report was designed to serve as an example to other entities. The fundamental conclusion of the report was that information disclosure practices could be improved without the need to reform existing standards, which allowed entities significant discretion as to the form in which they reported information.

5 In response to a request by the FSF.

3.3 International Monetary Fund

In its Global Financial Stability Report of October 2008, the International Monetary Fund (IMF) included a chapter on fair value accounting and procyclicality.

Its conclusion is that although weaknesses in fair value accounting methodology may introduce volatility and procyclicality, and thus some improvements are needed, it continues to be the most appropriate accounting framework for financial institutions and the measure that best reflects an institution's financial condition. Nevertheless, the application of fair value makes more transparent the effects of economic volatility on balance sheets more transparent. This means that under certain risk management frameworks, the balance sheets could exacerbate the cyclical movements in asset and liability values. Thus profits are exaggerated in boom periods and create the wrong incentives. Conversely, more uncertainty surrounding valuation in downturns may translate into overly tight credit conditions and negatively affect growth at a time when credit expansion is most needed. The report points out that much of the controversy surrounding fair value accounting stems from the investment decision and risk management rules using these valuations rather than the accounting framework itself.

The IMF also made some proposals aimed at solving the problems highlighted by the financial crisis. It pointed out that the estimates for provisions and capital adequacy should be capable of overcoming problems derived from volatility, and that greater transparency could be achieved not necessarily by more disclosures, but better disclosures[6].

It indicated that the extension of the concept of provisions to incorporate additional ways of retaining income in the upturn phase of the cycle could give some protection to balance sheets against procyclical effects. In the opinion of the IMF, coordination between accounting regulators and prudential supervisors would be needed to make these changes.

Fair value estimates should be supplemented with an appropriate analysis of the assumptions underlying the valuations and sensitivity analyses so that investors can form their own opinion in this respect.

More refined disclosures could meet the needs of a varied group of users, including investors, supervisors, depositors, etc.

Further, the volatility associated with a fair value balance sheet may mean that the balance sheet is no longer the primary medium for evaluating bank capital. Market participants and supervisors may increasingly turn their attention to cash flow statements, equity or income statements and risk measures to obtain enhanced information. These financial statements must evolve to respond to users' needs.

The IMF also emphasised that simulations appear to suggest that the application of fair value to both sides of the balance sheet would introduce a countercyclical component that may cushion some of the financial shocks that can result in large swings in bank equity. However, it is also necessary to take into account the risk of this practice of producing gains when the valuation of liabilities worsens. This is of particular concern when a deterioration in the bank's own creditworthiness, and the

6 This has also been pointed out by the Senior Supervisors Group. The IMF comments that the proposals of the FSF also point in the same direction.

subsequent decline in the value of its own debt, results in gains and a false sense of improvement in bank's equity position.

Finally, the IMF considers it important to enrich the fair value accounting framework so that market participants and supervisors are better informed and can thus promote market discipline and financial stability. The current fragmented solution between the accounting, prudential and risk management approaches to valuation is insufficient and must be reconciled. This will require adjustments in all three aspects, while ensuring that none of them should subordinate its objectives to any of the others (specifically, accounting standards should not be distorted by prudential objectives because this could endanger the fair presentation that financial statements should offer investors).

4 Measures adopted by the IASB as a response to the crisis

The IASB adopted a set of measures addressing certain aspects that had shown themselves to be relevant in current market conditions and that require an urgent solution[7].

4.1 Off-balance-sheet vehicles and asset derecognition

As mentioned above, one of the main aspects highlighted in the reports prepared by the various international bodies is the need to improve accounting and disclosure of special purpose vehicles. These include vehicles used by entities to transfer financial assets from the balance sheet through securitisation. This process transfers the credit risk related to certain assets to third parties.

However, in most cases this transfer, whether via a classic finance securitisation or synthetic securitisation incorporating credit derivatives, has involved retaining a large part of the risks and profits associated with the transferred assets: for example, through the concession of credit improvements by way of guarantees, reserve funds or the underwriting of the most subordinate bond tranche. In many cases, there has also been a continuous relationship or involvement with the transferred assets through debt service withholding or the administration of the vehicle's assets.

In addition to the above, the need to avoid reputational risk has led many entities in the recent crisis to assume the losses on previously securitised assets which had been removed from the balance sheet of the transferring entity.

This has led the FASB and IASB to analyse the weaknesses of the current rules and propose more solid criteria. However, it should not be forgotten than on occasions derecognition was the result of a rather strained application of the standards. It should be pointed out that this has not occurred in Spain, where both the CNMV and the Bank of Spain have overseen the proper application of international standards.

7 In April 2008 it published the report *Enhancing Market and Institutional Resilience* in response to a request from the FSF.

In any event, the IASB, which was already addressing the subject, decided to speed up its work. First, the IASB was planning to integrate the two criteria currently required for the consolidation of a subsidiary or special purpose entity onto a controlling entity's balance sheet into a single standard under the same concept of "control". The two criteria are control as power in IAS 27 and control as the retention of the majority of risks and benefits in SIC 12. The new definition being considered by the IASB covers both concepts of control more explicitly than now, as the power to manage the financial and operational policies of the controlled entity in order to obtain a benefit. In those cases where the entities operated on autopilot and control as management power had been exercised in constituting the vehicle, the subsequent emphasis would be concentrated on the idea of obtaining and appropriating a benefit. This project, which aims to achieve convergence with the US GAAP, is nevertheless headed up by the IASB, while the FASB is waiting for more concrete results. The *Exposure Draft* paper is expected to be published before the end of 2008 or at the beginning of 2009.

The IASB is also working to determine the criteria for derecognition of financial assets. It is worth remembering that IAS 39 indicates that when evaluating the derecognition of a financial asset from the balance sheet of a particular vehicle, an entity must first consolidate all entities and vehicles under its control, and subsequently apply the derecognition criteria under IAS 39 on this consolidated balance sheet.

The current treatment is certainly complex, particularly in those cases in which all the risks and benefits have neither been transferred nor retained. In addition, the continued relationship of the transferring entity with the transferred assets has to be analysed. This situation gives rise to complex accounting treatments which may even lead to the duplication of some assets and liabilities. A draft of this work is expected during the first quarter of 2009.

4.2 Fair value measurement and disclosures

The IASB has been working on the concept of fair value since mid-2006. Its aim is to establish consistent guidance and criteria for measuring the fair value of any asset or liability when required by an IFRS. It has published[8] a *Discussion Paper* including a standard issued by the FASB, which unifies the criteria for determining the fair value in US GAAP called SFAS 157 with some reflections from the IASB staff. This is a very important project, particularly so in the current circumstances in which, as commented above, there is talk of the possible procyclicity of fair value and its impact on regulatory capital.

Further, there has also been criticism of the use of fair value to the extent that it is not sustained by a robust theoretical framework specifying its nature and objectives, and which can determine whether it is appropriate or not for a certain class of asset or liability.

Thus in the definition SFAS 157 there is talk of the price that would be obtained in an orderly transaction between market participants. This presents the problem of what occurs when there is no market. It is also not clear whether this is an entry or exit price, and if it is an exit price, what the reasoning is for applying it to assets

8 First quarter of 2006.

which are not going to be disposed of, but rather consumed internally or maintained until their maturity.

Certain objectives have to be explored and properly explained in this respect. They include the following: how to allow an appropriate evaluation of asset management by the entity's own directors; how to measure the profitability of assets and equity in appropriate and comparable terms; and how to decide properly between various alternative projects. Such an analysis can help establish whether the fair value is the proper measurement criterion for all financial instruments and also for some classes of non-financial assets, such as property investment or biological assets.

The lack of liquidity also highlights the need to define the appropriate counting unit; in other words, whether the financial statements should always refer to fair value of individual elements or if sometimes they should refer to a set or block of assets, for example when they are managed or to be disposed of jointly.

Nevertheless, in the short term there is a need for guidelines in relation to financial instruments traded on markets that have become inactive, with a liquidity that has been seriously impaired. This is why, as has already been commented, the IASB set up an expert panel in May. The panel has already published educational guidance on determining the fair value of illiquid assets, as well as examples of practices used for disclosure. The guidance raises questions regarding the subjectivity and uncertainty associated with the determination of fair value, the models and main inputs used, and the sensitivity of fair value to certain unobservable market inputs and variations in them.

Some important events took place between the date of presentation for public consultation of the report containing the guidance and its final publication[9]. The crisis took a notable turn for the worse. Some financial institutions announced viability problems, and this led to market liquidity levels falling even more. The IASB itself approved the modification of IAS 39 to allow reclassification of trading portfolio assets.

The panel report includes a description of the practices used by various entities to determine the fair value of illiquid assets, and of the associated disclosures. They are guidelines that will form part of the educational volume on financial instruments published annually by the IASCF. Thus they are not legal or obligatory in character, nor are there any assumptions made as to other possible ways of determining fair value or providing disclosures that could also conform to international standards.

The amendments to the report should not be understood as contradicting its initial drafting. Rather, they show that the application of the general IFRS criteria in current conditions will force the entities to use internal valuation models, sometimes based on inputs that are unobservable in the market. At the same time, when many entities are passing through serious financial difficulties, it is probable that some of the market transactions may in fact be forced transactions. For this reason, in line with the FASB *Staff Position* mentioned above, the report states that not all the market transactions should automatically be considered appropriate to determine fair value, although the opposite extreme cannot be affirmed either.

9 The panel first published a draft open to consultation on 16 September 2008, with a submission period for comments until 3 October. A total of 37 comments were received and the definitive report was finally published on 31 October.

The report determines that transactions in an inactive market are inputs to be used in any valuation model, although they do not of themselves determine fair value. In fact, both approaches are not necessarily contradictory as in illiquid markets prices of real transactions may need significant adjustments, either because they are not recent prices, are forced transactions, or refer to markets where transactions are infrequent. In this context, the use of models based on internal estimates of flows is considered acceptable, but at the same time current risks have to be taken into account, including illiquidity and credit quality.

Other special cases may also occur, and are worth reflecting on. One can imagine a market where there are hardly any real transactions, but in which a real transaction took place on 31 December, just a few minutes before market closing. The transaction had the following characteristics: (i) the amount was not very significant, both from the point of view of the entity which wants to use to transaction to value the instrument on its balance sheet, and from the perspective of either of the two contracting parties in the transaction; (ii) the transaction immediately prior to this one took place more than 15 days previously; (iii) neither of the parties to the transaction are normal market operators in this instrument, and thus are not used to valuing this type of instrument. These circumstances would throw doubt on the validity of this transaction to determine of itself the fair value. There is a chance that the parties may not have correctly adjusted the price of the previous transaction to take into account the changes in market conditions. This makes it a good idea for the entity to determine the fair value of the instrument by obtaining and using real sources of evidence to help judge the quality of the price from the actual transaction.

The difference between the fundamental value for a unit of a particular financial instrument and its fair value is that the former is a specific value of the entity and thus dependent on the entity's own expectations and estimates. On the other hand, the fair value in an active market reflects the expectations of the market itself, which are the result of reconciling the different individual expectations of each of the market participants through the interplay of supply and demand, together with the arbitrage actions which try to take advantage of market inefficiencies. When transactions are very infrequent, the chances that there are no recent or real transactions increase, and the risk rises that the price of a real transaction reflects not so much the general market expectations as the private expectations of the two specific parties participating in the transaction. This may require more evidence such as sources of alternative prices from brokers and pricing services, prices of similar instruments, indices, consensus prices, etc.

4.3 Reclassification of assets from the trading portfolio

As mentioned above, on 7 October ECOFIN asked the IASB to resolve urgently before the end of October the competitive disadvantage caused by the difference between the IFRS and the US GAAP in terms of the possibility of reclassifying financial assets outside the trading portfolio.

IAS 39 *Financial Instruments: Recognition and Measurement* strictly forbade any reclassification of a financial instrument in or outside a portfolio "at fair value through the profit or loss category", which includes the trading portfolio.

However, the equivalent US standard, the SFAS 115, did allow reclassification from the trading portfolio to other portfolios that are valued at amortised cost, although only in "rare circumstances". It should be pointed out that the standard did not limit these rare circumstances, although in practice both the FASB and the SEC interpreted that these circumstances never or hardly ever occurred. In fact, before the subprime crisis, there is no sign of any US company making use of this faculty to reclassify assets from a trading portfolio to another.

Before continuing with the discussion of the process that led IASB to approve this change in IAS 39 and analysing its content, it is worth describing succinctly the types of instrument portfolios dealt with by IAS 39, and the criteria for measuring and allocation them, either to profit and loss or directly to equity:

- Loans and other receivables. Measured by their amortised cost. Cannot include instruments that are traded on an active market.

- Held-to-maturity investments. Also measured by their amortised cost. They can include instruments that are traded on an active market. The entity must have the intention and the financial capacity to maintain them until maturity. There is a penalisation if a significant part of this portfolio is sold. In this case, the rest is "contaminated" and should be reclassified in the available-for-sale portfolio.

- Portfolio at fair value through profit or loss. This portfolio, as its name indicates, is measured by its fair value, reflected in the profit and loss account. It includes 3 sub-portfolios:

  a) Derivatives that are not hedging instruments.

  b) Financial instruments initially designated as belonging to this portfolio.

  c) Trading portfolio. This is made up of instruments forming part of a set of assets that are often negotiated to obtain gains through short-term price variations.

- Financial assets available for sale. These are assets also measured at fair value, but fair value changes are registered directly against equity and not in the profit and loss, until the moment of sale or if it is determined that the asset is impaired.

On 13 October the IASB decided to approve an amendment in a standard without prior public consultation. It amended paragraph 50 of IAS 39, and added additional requirements for disclosures regarding reclassifications, modifying IFRS 7 *Financial Instruments: Disclosures*. This prompt and effective reaction was backed by the action of the European Commission itself. The following morning, the EFRAG issued its favourable technical report confirming the standard, and on Wednesday the 15th, two days later, the Accounting Regulatory Committee (ARC) also voted in favour. On the same day the European Commission adopted it through the publication of Commission Regulation No. 1004/2008 of 15 October. Broadly speaking, the main modifications are as follow.

Of the three sub-portfolios described at fair value through profit and loss, the assets in the trading portfolio can now be reclassified to held-to-maturity investments, as of 1 July 2008, in "rare circumstances". In the press release announcing the change in the rules, the IASB explained that the current situation met the criterion of "rare circumstances". Thus these assets may begin to be measured by their amortised cost from 1 July. The amortised cost will be its fair value on the date of reclassification. This allows some financial institutions not to have to register losses suffered in the third quarter of 2008 that are associated with the changes in fair value of these assets. The case that has had the most media attention in this respect is probably Deutsche Bank. This German institution presented a positive result in the third quarter of 414 million euros after reclassifying 24.9 billion euros to its portfolio of loans and other receivables from its trading portfolio (12.8 billion) and available-for-sale portfolio (12 billion). The assets began to be measured at amortised cost, so that portfolio losses of 845 million euros and a direct negative adjustment in equity for capital losses of 649 million euros did not have to be imputed in the profit and loss account.

The amendment also allows reclassification of assets either from the trading portfolio or the portfolio of available-for-sale financial assets to the loans and other receivables portfolio, as long as these assets complied with the definition of loans and other receivables and the entity has the intention of holding them at least for the foreseeable future.

Finally, IFRS 7 was amended to require entities that make use of this possibility to provide appropriate information about what the effect on the profit and loss or equity would have been if the reclassification had not taken place.

At the same time it is worth highlighting that some aspects of the reform have given rise to problems of interpretation.

In particular, the new paragraph 103G of IAS 39 indicates that the amendment will be applied from 1 July 2008, but that any reclassification of a financial asset made in periods after 1 November 2008 shall take effect only from the date on which the reclassification is made. This could literally be understood to mean that those entities which publish quarterly financial reports (with the accounting year coinciding with the calendar year) can still retroactively apply the reclassification at the start of the fourth quarter of 2008 (which begins 1 October), although the asset may have been reclassified at a later date (for example, 20 December). Given such doubts, the IASB in its *Update* for October states that if an entity decides to reclassify an asset after 1 November, it may apply the change retroactively from 1 July, but if the reclassification is after 1 November, it will take effect from the date of reclassification. Subsequently, given the uncertainty created, the IASB issued a new standard clarifying the matter.

Another question giving rise to doubts is when the determination has to have been made, in accordance with the new paragraph 50D, as to whether an asset classified as available for sale meets with the definition of loans and receivables. Some people understand this determination to refer to the date on which the asset was initially classified as available for sale; others that the determination only has to be made on the date of reclassification. This is important, as one of the requirements is that the asset should not be traded on an active market, and given the general reduction in liquidity, it is rather more likely that this condition should be met on the date of reclassification (for example, 1 July 2008) than when the asset was initially classified. It appears that the doubt has been generated because of the wording, due in part to the speed in approving the standard, and also the fact that various versions of the standard were being debated, and this may have led to a certain internal in-coherence between the different paragraphs in the final version. In fact the second interpretation, that of the date of reclassification, which has been adopted by various audit firms, may be the most acceptable.

5 The CESR

The main functions of the Committee of European Securities Regulators (CESR) are to improve coordination among securities supervisors in the EU, advise the European Commission and work to ensure a consistent implementation of the Community legislation in all EU Member States. Given that securities supervisors are institutions that normally are responsible for the supervision of the application of international accounting standards in their respective jurisdictions, the CESR participates actively in the development and implementation of the IFRS through constant dialogue with all the relevant parties involved in the process.

It is thus not surprising that the CESR has adopted a very active role throughout this period, sometimes at the request of the European Commission, and at others on its own initiative. At some of these times, the CESR has acted jointly with the CEBS and CEIOPS, the two other EU supervisory committees that make up the Lamfalussy level three (3L3 Committees).

Thus at the request of ECOFIN, CESR undertook to prepare guidelines containing best practice in relation to the determination of fair value of illiquid instruments and associated disclosure[10]. As is the case with the IASB expert panel document, it should be read in conjunction with a joint clarification by the SEC and FASB, and with the work carried out by the IASB on the final report by the panel itself[11].

The most recent documents of the FASB and the SEC, as well as those of the IASB expert advisory panel, include more evidence as to the worsening market conditions, with a drastic fall in liquidity and a more complicated financial situation for some entities, making it less unlikely that transactions may occur that can be classified as forced.

As a result[12], the three level 3 committees (3L3) of the European Union published a joint communication in which they backed the latest IASB initiatives, including the urgent amendment of IAS 39 to allow reclassifications between portfolios of financial instruments, converging with the US GAAP and avoiding possible competitive disadvantages[13].

10 This report was put up for public consultation from 10 July 2008 to 12 September, and was published after consultation with financial issuers at a European level and their auditors. It was taken into account by ECOFIN in its September meeting.

11 CESR published its final report on 3 October 2008. The CESR document was also used by the panel as an input in its work.

12 21 October.

13 The ECOFIN meeting of 7 October had called this initiative urgent and necessary. It also urged the IASB to resolve it before the end of the month. The joint document applauded the speed of the European Commission in adopting the amendment in only two days, after having published the amendment of IAS 39 on 13 October. This swift response also avoided any unilateral action in the EU and the approval of a new carve-out of IAS 39, which would have reduced the degree of convergence with the IFRS as approved by the IASB.

As has been pointed out above, this amendment allowed financial entities to reclassify financial assets as of 1 July 2008, from trading and available-for-sale asset portfolios (under certain conditions) to loan or held-to-maturity asset portfolios, which are both measured at amortised cost. This enabled some EU financial institutions in the third quarter of 2008 to avoid recognising part of the losses derived from falling prices of fixed-income assets that they held in their trading portfolio during this period, or the equity impairment of those that were classified as available for sale.

In their communication the 3L3 committees urged issuers and auditors to take into account these new IASB staff indications (on the compatibility of the SEC and FASB clarification with the IFRS) immediately, as they facilitated and made more flexible the determination fair value in a worsening financial crisis.

Finally, they declared they were prepared to collaborate and continue working with the European Commission and the IASB on any other aspect of IAS 39 and IFRS 7 which may be considered relevant. In this respect, the CESR has started to analyse some of the subjects raised, such as the difficulty relating to embedded credit derivatives in certain synthetic securitisations and the question of whether they should be separated or not from the main contract; and the need to determine whether it is proper to extend reclassification to instruments initially designated at fair value through profit and loss. A final point to mention is the possibility of reviewing the current treatment of the impairment of available-for-sale financial assets in relation to the reversal of impairment of capital instruments via equity; as well as with respect to the obligation that exists today of reclassifying the total capital losses, previously entered in equity, in the profit and loss account, if a fixed-income asset is considered impaired. The effect of impairment on future cash flows cannot be split, so the result is an increase in the discount rate with respect to the effective initial rate of the instrument.

6 Conclusions

The current global financial situation has put an unprecedented strain on the whole conceptual framework related to financial instruments and the determination of their fair value. But it has also led to positive results. It has served to highlight some deficiencies and the need for additional guidance allowing issuers to apply the IFRS consistently in extreme market conditions which have led to the almost total lack of active market references for many of the financial instruments in the balance sheets of financial entities.

Another positive factor has been to show that accounting regulators need robust procedures that are sufficiently flexible and swift to respond to urgent demands in situations of special emergency such as those that exist at present.

There have been calls for the temporary suspension or even permanent abolition of fair value and its replacement with historic cost or measures as artificial as using average half-yearly prices.

At root, many of these demands would only reduce the level of transparency and conceal the real financial situation of entities. They could actually be counterproductive, as they would increase the lack of trust in companies and the market in general, thus constricting the liquidity in the system even more. In fact, the destabilisation that leads to falling asset prices should be tackled by prudential regulation rather than accounting standards.

However, it has to be admitted that it would be a good idea for international accounting regulators to establish a robust conceptual framework for the measurement of assets and liabilities. They should state what the overall objectives and the advantages and disadvantages of each valuation criterion are, and the reason for determining which criterion is most appropriate for each category of assets and liabilities.

With regard to fair value, there are still many points pending a clear theoretical foundation: for example, whether the entry or exit price should be used, what the appropriate unit of measurement is (the problem of blocks), or the difference between fair and fundamental value. Given that fair value aims to reflect transactions between market participants, when it does not exist in practice additional criteria and guidance are needed. In this sense, more work should be done on aspects related to inactive markets. For example, robust principles should be laid down regarding when a price obtained in a current transaction in an inactive market can be subjected to significant adjustments.

At the same time, due process should be respected as far as possible when preparing and amending standards. Specifically, there should always be a minimum consultation period to allow reactions from the interested parties. There should not be any hasty amendments that have not evaluated the impact on the rest of the standards with a minimum of care. This is compatible with the need to modulate the length of the consultation periods according to the degree of urgency of the planned reform in question.

In any event, everything possible should be done to ensure that any change in the current standards is compatible with the aim of achieving a single set of principles for financial information applicable to the companies listed on all the international markets. This implies that European standards should not distance themselves by corresponding carve-outs of international principles. There should be a speedier convergence between all the national standards, including the American ones, and those issued by the IASB. The structure of government and legitimacy of the IASB should be enhanced by the establishment of a committee to monitor its work (this is already planned), with the participation of relevant securities supervisors.

7 Bibliography

CESR (2008): "CESR Statement: Fair value measurement and related disclosures of financial instruments in illiquid markets". CESR Website. Paris. Ref. CESR/08-713b.

CESR (2008): "CESR welcomes IASB's guidance on measuring and disclosing the fair value of financial instruments in non-active markets". CESR Website. Paris. Ref. CESR/08-888.

CESR, CEBS y CEIOPS (2008): "Joint Statement from CESR, CEBS and CEIOPS regarding the latest developments in accounting". CESR Website. Paris. Ref. CESR/08-839.

EU Commission (2008): "Accounting Standards: Commission welcomes IASB guidance on the application of fair value measurements when markets become inactive". Brussels. IP/08/1636.

EU Commission (2008): "Further issues related to IAS 39". Brussels. MARKT.F3/AD D (2008) 47947.

EU Commission (2008): "Commission Regulation (EC) Nº 1004/2008 of 15 October 2008". Brussels.

Financial Stability Forum (2008): "Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience". Financial Stability Forum Website. Basel.

Financial Stability Forum (2008): "Update on the Implementation of the FSF's Recommendations". Financial Stability Forum Website. Basel.

Financial Stability Forum (2008): "Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience. Follow-up on Implementation". Financial Stability Forum Website. Basel.

FMI (2008): "Global Financial Stability Report. Financial Stress and Deleveraging. Macrofinancial Implications and Policy, Oct 08". FMI Website. Washington DC.

IASB (2008): "Expert Advisory Panel: Meeting Summaries". IASB Website. London.

IASB (2008): "Amendment to IAS 39 & IFRS 7: Reclassification of Financial Assets". London.

IASB (2008): "Exposure Draft Improving Disclosures about Financial Instruments". IASB Website. London.

IASB (2008): "IASB response to the credit crisis". IASB Website. London.

IASB (2008): "IASB announces next steps in response to credit crisis". IASB Website. London.

IASB (2008): "IASB staff position on SEC-FASB clarification on fair value accounting". IASB Website. London.

IASB (2008): "IASB provides update on applying fair value in inactive markets". IASB Website. London.

IASB (2008): "IASB Expert Advisory Panel: Measuring and disclosing the fair value of financial instruments in markets that are no longer active". IASB Website. London.

IOSCO (2008): "Report on the Subprime Crisis". IOSCO Website. Madrid.

IOSCO (2008): "The role of credit rating agencies in structured finance markets". IOSCO Website. Madrid.

IOSCO (2008): "IOSCO Technical Committee Statement on Accounting Standards Development and Enforcement". IOSCO Website. Madrid.

SEC and FASB (2008): "SEC Office of the Chief Accountant and FASB Staff Clarifications on Fair value Accounting". SEC Website. Washington.

Senior Supervisors Group (2008): "Observations on Risk Management Practices during the Recent Market Turbulence". Financial Stability Forum Website. Basel.

Senior Supervisors Group (2008): "Leading-Practice Disclosures for Selected Exposures". Financial Stability Forum Website. Basel.

Private fixed-income markets in Europe

Elías López Blanco (*)

* Elías López Blanco is a member of the Studies, Statistics and Publications Department of the CNMV.

1 Introduction

Private fixed-income issuance has grown sharply around the world in recent years, mainly as a result of low interest rates. Financial institutions have played a particularly decisive role in boosting the fixed-income markets because of their growing need for finance. Non-financial companies have also notably increased their issuance, although to a lesser extent. The increase in issuance has been accompanied by the presence of increasingly complex instruments, among them various types of asset-backed bonds.

The financial crisis that started in August 2007 has given rise to the need to review various aspects of the process of classification, valuation and distribution of the most complex instruments. At the same time, the lack of liquidity in some wholesale secondary markets that are essential in generating reference prices for valuing investment portfolios and credit institutions' own finance has concentrated greater attention by the financial community and the regulators on how private fixed-income markets operate. The interest in these markets is also growing as a result of an old debate on transparency requirements for trading required by secondary fixed-income markets. This debate has taken on new force after the approval of the Markets in Financial Instruments Directive (MiFID).

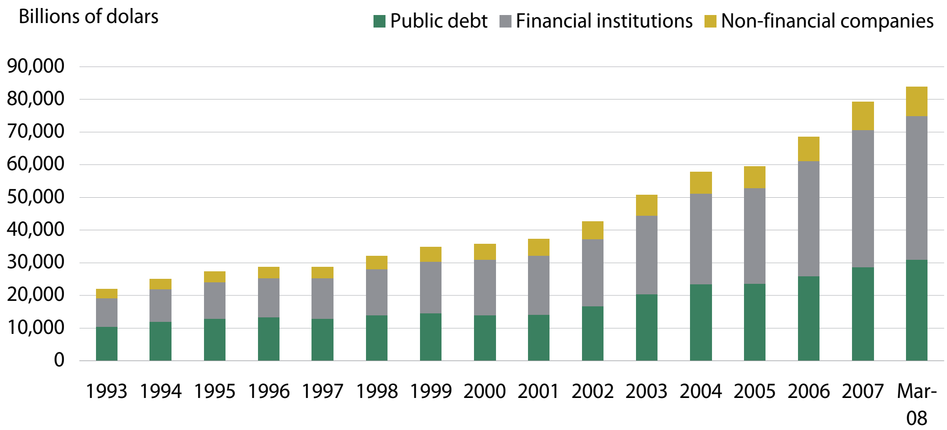
This article aims to offer an overall (although of necessity simplified) view of the European private debt markets. It is an attempt to contribute to a greater knowledge of how these markets are regulated and how they operate. In particular, it aims to offer a description of the most frequent systems of placement in primary markets, as well as the market types and trading systems in secondary markets. The article is divided into the following parts: Section 2 gives historical data relating to issuance in Europe and compares it with other geographical areas; section 3 is dedicated to regulation and placement procedures in primary markets; section 4 deals with regulation and different types of trading infrastructures offered in secondary markets; and finally, section 5 gives the conclusions.

2 Background information

Fixed-income issuance saw strong growth worldwide starting in 2002. While the outstanding global balances grew at an average annual rate of close to 7% between 1992 and 2001, this average increased to 13.5% between 2002 and 2007. The increase was boosted by a period of low interest rates starting in the brief recessionary in the US economy in 2001 and has been maintained since then. As can be seen in Chart 1, the issuing activity of financial institutions represented the main driving force of global growth in outstanding balances, while the issues of public administrations grew at a considerably lower rate. Issues by non-financial companies also increased, though at a much slower rate.

In accordance with data from the Bank for International Settlements, and including both issues for international markets and those exclusively for domestic markets, the outstanding total balance of fixed-income issues in March 2008 was around 84,000 billion dollars. The issues by financial institutions represented 52% of the total, and non-financial institutions about 11%.

Global outstanding balance of fixed income FIGURE 1



Source: Bank for International Settlements.

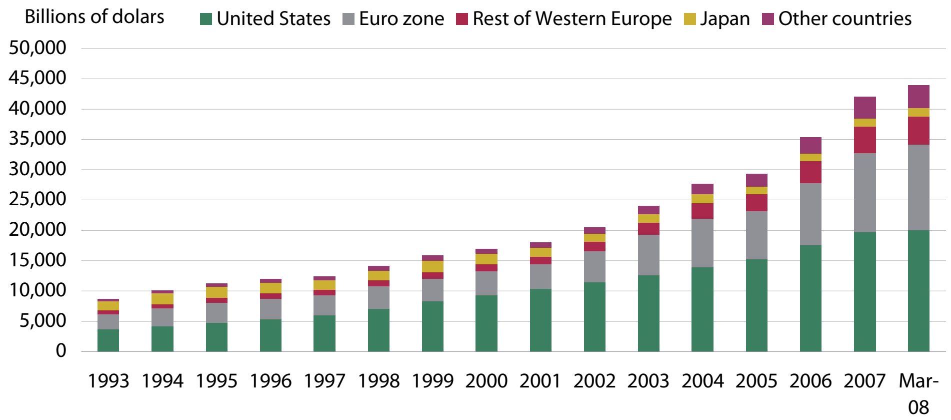
The sector of financial institutions includes credit institutions, mortgage agencies (in America), securitisation vehicles, insurance companies and other financial entities. Issuance is fundamentally concentrated in the first three types of institution. A substantial part of the increase in activity by credit institutions can be explained by the increase in demand for finance for consumer activities and the acquisition of assets in the property market. Business leverage resulting from the major expansion of mergers and acquisitions has also been a significant factor in increased issuance.

As can be seen in Chart 2, European and North American financial institutions represent the bulk of the outstanding balance in this sector. In March 2008, the outstanding balance of North American issues was 46% of the total, compared with 42% for European financial institutions, including both the euro zone and other Western European countries. The euro zone itself represented 32% of the total.

Issuance by European financial institutions has grown in recent years by more than American issuance. Between 2002 and 2007, European issuance increased at an average annual rate of 22%, both in terms of the euro zone and Western Europe as a whole, while American issuance increased by 11%.

Global outstanding balance of fixed income issues by financial institutions

FIGURE 2



Source: Bank for International Settlements.

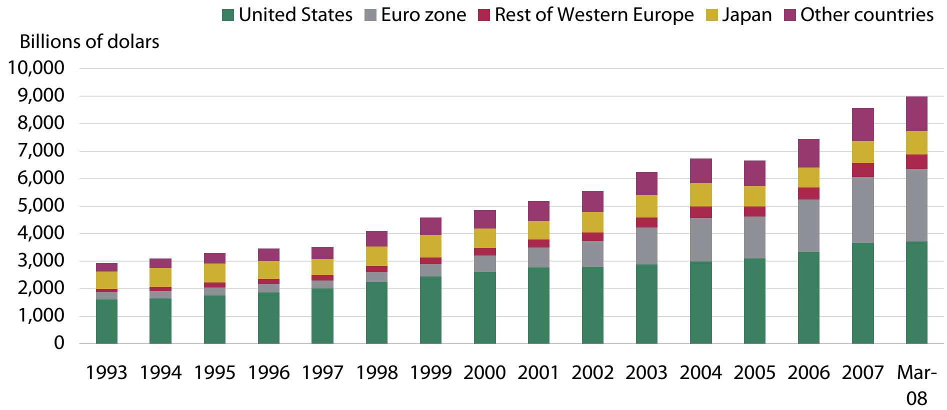
Corporate debt issues in the strict sense, in other words those by non-financial organisations, have always been considerably less significant than those by the financial sector. The bulk of corporate issues have historically been concentrated on issues with high credit ratings, although the positive performance of the market and the economy has allowed a significant growth in issues with ratings below investment grade. Chart 3 shows that European issuers also occupy a significant position in this sector. Taken as a whole, issues in the euro zone plus those of other Western European countries concentrated 35% of the total outstanding balance in 2008 (29% for the euro zone). However, the American proportion continues to be greater, at around 42% of the total.

In terms of growth of issuance, the Europeans have also posted higher growth than the Americans during the 2002-2007 period. Thus while the European issuance grew at an annual average of 20% (23% for issues in the euro zone) in this period, the rate was 5% for America.

Despite the relatively more intense growth of private fixed-income issuance in Europe, fixed-income issuance in America continues to have a far greater weight by far than the European in the private sector. Chart 4 compares the relation between the outstanding balance of private fixed income and GDP for various countries and the euro zone as a whole. As can be seen, this measure of the size of the private fixed-income market compared with the size of the economy clearly shows the greater importance of the American market over the European, although it also highlights the growth in European private fixed-income issuance. It can also be seen in the chart that there has been an extraordinary growth in Spanish issuance compared with other European countries, and even with the United States. As is well known, the growth in Spanish issuance has been basically supported by two types of instruments: commercial paper (company bonds) and asset-backed issues (securitisation and guaranteed bond issues).

Outstanding balance of fixed income issuance by non-financial companies

FIGURE 3

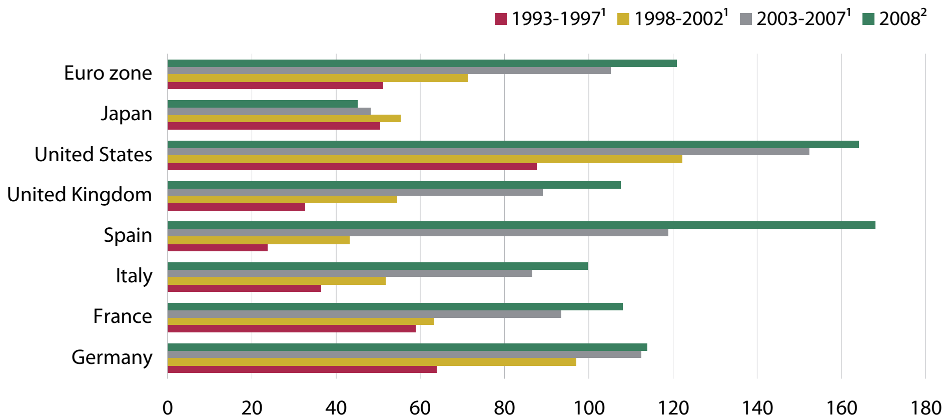


Source: Bank for International Settlements.

Outstanding balance of private fixed-income as proportion of GDP

FIGURE 4

As percentage



Source: Bank for International Settlements, Datastream and own calculations.

1 Average.

2 Outsanding balance in March 2008.

3 Primary markets

3.1 Regulation

The issue of securities in primary markets in the European Union is regulated by the Prospectus Directive (Directive 2003/71/EC of the European Parliament and Council). The most important requirement for issuers is the publication of a prospectus with the characteristics of the securities to be issued and relevant data on the issuing entity, including its audited financial statements and a report on its prospects. At the same time, if the securities are guaranteed by a third party, the prospectus should include the same information about the guarantor as required from the issuer. The prospectus should be registered with the competent authority of a Member State, which must examine it to check that its content and format meet the requirements established in the level 2 regulation implemented by the Directive. Key points to consider in this examination are the precision of the information, its completeness and its comprehensibility. If there is disagreement in any of these and/or other aspects, the supervisor may request the issuer to make corrections, or include clarifications or additional information. The supervisor may also refuse to register the prospectus if he considers that it does not meet the requirements of the regulation. In any event, the registration does not represent a guarantee by the supervisor of the content of the prospectus. This is exclusively the responsibility of the issuer and the auditors (the latter for part that corresponds to them).

There are important exemptions with regard to the application of the Directive as a whole, or more specifically the obligation to publish a prospectus. Thus the Directive is not applicable to fixed-income issues in the following cases:

- Issues by public administrations and institutions, in the case of:
  - European Union Member States or a Member State's local or regional authorities.
  - Public international bodies of which one or more Member States are members.
  - The European Central Bank or the central banks of the Member States.
  - Securities unconditionally and irrevocably guaranteed by a Member State or by one of a Member State's local or regional authorities.
- Issues by associations with legal status or non-profit-making bodies, recognised by a Member State, with a view to their obtaining the means to achieve their non-profit-making objectives.
- Issues of credit institutions, in the following cases:
  - Non-equity securities issued in a continuous or repeated manner by credit institutions, provided that these securities (i) are not subordinated, convertible or exchangeable, (ii) do not give a right to subscribe or acquire other types of securities and are not linked to a derivative instrument; (iii) materialise reception of repayable deposits; and (iv) are covered by a deposit guarantee scheme under Community legislation.
  - Non-equity securities issued in a continuous or repeated manner by credit institutions where the total consideration of the offer is less than 50 million euros, calculated over a period of 12 months, provided they comply with conditions (i) and (ii) of the point above.
  - *Bostadsobligationer* issued by credit institutions in Sweden to grant mortgage loans, provided that (i) the securities in the issue are of the same series; (ii) they are issued on tap during a specific issuing period; (iii) the terms and conditions of the issue are not changed during the issuing period; and (iv) the sums deriving from the issue are placed in assets which provide sufficient coverage for the liability deriving from securities.
- Securities issued in an offer where the total consideration is less than 2,500,000 euros, which limit shall be calculated over a period of 12 months.

The cases referred to below do not represent a total exemption from the obligations arising from the Directive, but only of the principal obligation, i.e. the obligation to publish a prospectus:

- Issues exclusively offered to qualified investors, meaning legal entities authorised or regulated to operate in financial markets (credit institutions, investment firms, insurance firms, collective investment schemes, pension funds, etc.) as well as entities not so authorised or regulated whose corporate purpose is solely to invest in securities.
- Issues limited in terms of:
  - The number of investors they are addressed to: 100 investors, other than qualified investors.
  - The minimum amount acquired per investor: 50,000 euros.
  - The minimum denomination per unit of the securities included in the offer: 50,000 euros.
  - The minimum total amount of the offer: 100,000 euros, calculated over a period of 12 months.

It is worth pointing out that the subsequent transfer of securities to which the exemption to present a prospectus has been applied because of the nature of the investments or the quantitative limits mentioned above does not necessarily have a new exemption guaranteed. Such a sale operation shall be considered as a separate offer and as a result must be analysed again by the supervisor to determine whether the exemption can be applied. The same exemption is applicable to the placement of securities by financial intermediaries, who shall be subject to publication of a prospectus if none of the conditions mentioned above are met. At the same time, a prospectus must be published when applying for admission to trading of securities on a regulated market when the placement in the primary market has been exempt from this obligation.

The Community regulation includes other exemptions from the obligation to publish the prospectus. Their main aim is to avoid duplications and reduce the cost of compliance with the regulation for the issuer, provided that the market already has a public document of equivalent informative value. Given the situations covered by the Prospectus Directive for applying these exemptions (securities offered in the context of mergers and acquisitions of companies, offers exclusively addressed to directors or employees, securities resulting from the conversion or exchange of other securities and admission to trading on regulated markets of securities already admitted to trading on another regulated market) their potential impact is considerably greater in equity than fixed income.

The Prospectus Directive covers certain options in presenting and registering the prospectus that are of particular interest to fixed-income issuers. The prospectus may be divided into three separate documents: a registration document, with information referring to the issuer; a note with information on the securities; and a summary note. The document with information on the issuer may be registered before the issue, as it is valid for twelve months, and if necessary it may be updated by presenting a supplementary document; whereas the informative note on securities and the summary note may be presented for publication when the securities are offered to the public. This allows issuers to adapt their issuing schedule to market conditions. The Directive also provides a flexible registration procedure for issuers who turn to the market relatively frequently. In these cases, the normal practice consists in the registration of issuing schedules to establish the maximum total consideration of the offers in the following twelve months by shelf registration. With regard to this kind of strategy, which is in fact very common among the biggest fixed-income issuers, the Prospectus Directive allows the registration of a base prospectus, valid for a year, which if necessary can be supplemented with updated information on the issuer and securities that will be offered through a supplementary document.

The prospectuses registered in any Member State of the European Union are valid in the rest of the Member States for the purpose of the corresponding public sale offer, even if the registration takes place in a Member State other than that in which the issuer has his registered office. Thus the issuers who want to place their securities in more than one European Union country only have to fulfil the registration procedure in one Member State of their choice. The prospectus, which will generally be registered in English, does not need to be translated into the languages of the Member States where the offer will be distributed, although the competent authorities of these states may require a translation of the summary note.

3.2 Placement procedures

The placement of fixed income with the biggest volume and highest credit rating tends to be through the procedure of a public sale offer of securities and usually includes the participation of financial institutions who have a threefold function: to advise the issuer; to underwrite the securities; and to sell the securities to the public. The advice function tends to include both the design of the operation and compliance with the requirements established in the regulation, particularly the preparation of the prospectus. The underwriting involves the firm purchase of the securities, thus assuming the risk of the placement. In this case, the retribution of the underwriter depends on the difference between the price paid for the purchase of the shares and the price obtained in their resale to the final investors (the underwriter's gross margin or discount). An alternative to underwriting is simple mediation, where a financial institution or an investment services firm offers its experience in the sale of securities as a best-effort arrangement in exchange for a fee. Pure mediation is fairly common in programmes for issuing short and medium-term instruments, such as commercial paper or medium-term notes (MTN). It can also be used in the placement of issues with low credit ratings or unrated issues.

Underwriting operations may involve a high risk, so it is common to form a group of financial institutions (a syndicate) to share it. The gross margin of the operation is then divided between the members of the syndicate. One of them, usually the member who obtained the contract for the operation with the issuer, acts as lead underwriter, although there may be co-directors. In terms of the sale of securities, success requires a high capacity for commercialisation. Investment banks and financial institutions that act in this segment of the financial industry tend to have a significant client base, made up of both institutional and retail investors. To increase its commercial capacity, the lead underwriter may form a selling group made up of members of the syndicate and other financial institutions. The connection of the lead underwriter to the operation does not tend to end with the sale of the securities.

These entities often also assume an important position as market makers for the security in the secondary market. The commitment to give liquidity to the security reinforces the entity's reputation and helps maintain its potential investor base for future operations.

The traditional pattern of placement described above, based on a syndicate of underwriters, may vary in a number of ways. One of these is the purchase from the issuer of a certain number of securities to be placed (a bought deal) through a firm offer from one or more entities. Typically, the offer has a very short validity period of one day or even only a few hours. This is because the idea is to offer the issuer immediacy in transactions in which, given the characteristics of the securities and markets, speed of placement is crucial for success (for example, in the Eurobond market). The high potential risk of these operations is mitigated by the fact that those making the offer tend to have a major portfolio of institutional clients with whom they may even have agreed previously to sell a substantial part of the issue. At the same time, the offering entities may use hedging strategies through interest-rate derivatives.

A variation of the traditional pattern that is more deeply entrenched than that explained above is the placement through auctions promoted by the issuer. This procedure allows for a number of variants according to the type of auction used. It is currently normal in public debt markets. Among issues in the private sector, auctions enjoyed popularity in the past, particularly with issues by utilities, whose fixed-interest issues were extremely popular among small investors. Today, the use of these systems is not very frequent among issuers in the private sector, probably as a result of the growing weight of institutional investors in the demand for private fixed-income securities.

4 The secondary market

4.1 Regulation

Unlike securities, where trading is basically concentrated in securities markets, most trading in fixed-income instruments in Europe takes place in over-the-counter (OTC) markets. An OTC market is, in essence, made up of a network of dealers, each of whom offers prices for the purchase (bids) or sale (asks) of certain securities. When these prices are offered on a firm basis and regularly, the term "market maker" tends to be used for the trading entity. The decentralised character of OTC markets means that investors who want to trade securities in them have to do so through specific dealers or market makers. The bids or asks do not come from a centralised organisation, such as a stock exchange. Thus the private fixed-income market is essentially a search market. In fact this key characteristic has from the mid-1970s created an incentive to design systems of dissemination of price information with the aim of reducing the cost of searching for the market participants. It has also created incentives to develop alternative trading infrastructures to that of the traditional bilateral relationship, through electronic trading platforms offering a number of potential counterparties, and sometimes guaranteeing anonymity to the participants. These systems are essentially wholesale, as they offer trading between dealers or between dealers and institutional investors.

The MiFID regulates the trading infrastructures in the European Union. The Directive distinguishes between regulated markets, multilateral trading facilities (MTFs), and systematic internalisers, establishing a specific regulatory treatment for each case. Both regulated markets and the MTFs offer the chance to trade through multilateral systems (multiple participants on both sides of the trade). Their functioning should be subject to non-discretionary rules. The securities admitted to trading on regulated markets should meet certain requirements established in a number of European Directives, such as the Consolidated Admission and Reporting Directive (Directive 2001/34/EC of the European Parliament and Council), the Prospectus Directive, the Transparency Directive (Directive 2004/104/EC of the European Parliament and Council) and the MiFID itself. The MTF managers should establish transparent rules on the criteria to determine which financial instruments can be traded in their system. In practice, MTFs tend to concentrate on trading securities admitted to trading on regulated markets. For their part, the systematic internalisers are investment service firms which, on an organised, systematic and frequent basis, execute client orders on own account, outside the markets and the MTFs.

One of the most debated questions in fixed-income secondary market regulation is the transparency of the trading process. This means making information on prices and depth of trading interest in bids and offers public before trading begins (pre-trade transparency), and the dissemination of information on prices and volumes actually traded (post-trade transparency). The MiFID demands pre- and post-trade transparency requirements in some detail for actions in the three types of trading systems covered (regulated markets, MTF and internalisers), but not for fixed income. The level of trading transparency in European fixed-income markets thus depends on national regulation or the rules of the individual market or trading system. In general, it can be said that currently institutional investors have access to a reasonable level of information on pre- and post-trade prices with regard to public debt and some kinds of bonds issued by the private sector with a high credit rating, thanks to the electronic trading platforms on which they can be traded directly, and to the commercial systems of price dissemination (market data vendors). On the other hand, the access restrictions to these trading systems and the cost of professional services for disseminating information limit the information available to retail investors. These generally only have access to post-trade information in some instruments, made public with a delay that reduces its usefulness considerably.

Given the decentralised nature of the fixed income markets, an improvement in the level of pre- and post-trade transparency would bring undoubted advantages for investors, particularly in the sphere of private fixed income, where market visibility is considerably lower than in public debt markets. However, improvements in transparency have always faced considerable opposition because of the central role of market makers and, in general, dealers in the provision of liquidity to these markets. In essence, it is argued that the increase in transparency increases the visibility of the financial position of these intermediaries, and thus their vulnerability to aggressive strategies by their competitors or other market participants. Supporters of this position tend to conclude that an increase in information disclosed to the market could involve an increase in the bid-ask spreads offered by market makers, and even a reduction in the number of these intermediaries.

After the approval of MiFID, the increase in transparency in fixed-income markets is the subject of debate in the European Union, and given what has occurred in recent months, its importance is increasing still more. In fact, the financial crisis which began in August 2007 has had a notable impact on some private fixed-income markets, such as markets in asset-backed securities (ABS and guaranteed bonds) and the market in company bonds, leading to a substantial fall in placements and transactions on the secondary markets. The practical freeze on operations in these markets has not only led to serious damage to its participants in terms of illiquidity and access to finance, but it has deprived the holders of the private fixed-income assets affected of reference prices which are of great use for valuing their portfolios. Given the lack of such prices, the process of valuation has become considerably more difficult and mistrust in its results has grown, with the corresponding negative impact on the demand for the affected assets. It is very probable that this negative experience will be translated in greater scrutiny on the quality of reference prices in the future. Thus an improvement in transparency in the short term could help a swifter and firmer recovery in activity in the private fixed-income markets.

4.2 Trading infrastructures

4.2.1 Securities markets

Most European securities markets, or more broadly speaking the company group to which they belong, have trading markets or platforms for trading fixed income. In some cases they are considered regulated markets in the MiFID sense. Although some stock markets make electronic trading systems available to investors, most of the fixed-income transactions registered in organised fixed-income markets are carried out through bilateral trade between the parties. They are then communicated to the market. Given that there is no centralised mechanism to form prices, it can be said that the main structuring element of these markets is the infrastructure for the clearance and settlement of reference securities established by the market manager, although MiFID recognises the right of participants to choose the provider of this service. The domestic securities traded on stock markets tend to be settled through a central national securities depository, while international values are mainly settled through Euroclear and Clearstream.

Outstanding balance of bonds traded on some European stock exchanges in December 2007 TABLE 1

Billions of euros

	Domestic private sector	Domestic public sector	Foreign issuers	Total
BME (Spain)*	775.4	8.9	0.0	784.2
Italian Stock Exchange	53.8	1,235.5	1,036.8	2,326.1
London Stock Exchange	1,084.4	588.8	985.2	2,658.4
Luxembourg Stock Exchange	0.0	0.0	5,432.9	5,432.9
OMX Nordic Stock Exchange	398.8	174.4	ND	573.2
Swiss Stock Exchange	70.3	75.5	155.8	301.5
Vienna Stock Exchange	80.1	141.3	13.5	235.0

Source: World Federation of Stock Exchanges, BME and own calculations.

* CNMV: *Annual report on securities markets for 2007.*

As can be seen from Table 1, organised fixed-income stock exchanges tend to trade in both private and public securities. What is particularly striking is the significant weight of foreign securities. In particular, these kinds of securities give the Luxembourg Stock Exchange a notable position in terms of the outstanding balance of traded bonds. This is because the Luxembourg Stock Exchange has become the main reference market for Eurobonds. The admission to trading on regulated markets for these securities is, at root, a mere formality, because such important investors in fixed income as collective investment schemes and pension funds are restricted by regulations with regard to the weight of the untraded securities in their portfolios.

Bond trading in some European stock exchanges in 2007 TABLE 2

Billions of euros

	Domestic private sector	Domestic public sector	Foreign issuers	Total
BME (Spain)*	1,134.3	83.9	0.0	1,218.2
Italian Stock Exchange	6.2	140.2	3.4	149.8
German Stock Exchange	52.8	153.4	23.3	229.5
Euronext	NA	86.9	54.7	141.6
London Stock Exchange	40.5	2,554.3	24.6	2,619.4
Luxembourg Stock Exchange	0.0	0.0	0.4	0.4
OMX Nordic Stock Exchange	838.7	1,193.8	1.7	2,034.2
Swiss Stock Exchange	23.9	21.2	59.7	104.8
Vienna Stock Exchange	0.5	0.0	0.0	0.6

Source: World Federation of Stock Exchanges, BME and own calculations.

* CNMV: Annual report on securities markets for 2007.

In any event, the trading volumes of private fixed income through traditional stock exchanges are mostly small, as can be seen in Table 2. Two noteworthy exceptions are BME and OMX. BME is the Spanish holding company of stock exchanges. It includes four national stock exchanges and AIAF, a regulated market in the MiFID sense, where trading has increased considerably over recent years. OMX is a holding company operating the stock exchanges in Sweden, Finland, Denmark, Iceland and the Baltic republics. The London Stock Exchange represents a relatively high proportion of total trading in fixed income (about a third of the traded amount in fixed income in one year); however, it should be noted that the bulk of the trading comes from securities issued by the public sector, not by the private sector (the London Stock Exchange is the regulated market of reference for the prices of securities issued by the British government). As to the Luxembourg Stock Exchange, trading in 2007 was less than 450 million euros, despite a considerable outstanding balance admitted to trading. The essentially OTC character of the private fixed-income market explains, at least in part, the reduced level of stock market trading in these kinds of instruments.

4.2.2 Electronic trading platforms

As indicated above, the mid-1990s saw the appearance of electronic trading systems for inter-dealer and dealer-institutional investor transactions. In general, these systems have been promoted by banks, which traditionally already played a very active role as market makers in various segments of fixed-income markets. Some traditional stock exchanges, such as the German Stock Exchange, the Italian Stock Exchange, or Euronext, have also become promoters of some of the most important electronic trading systems. Also noteworthy is the participation as promoters in this business of the great professional information publishers, particularly Thomson-Reuters and Bloomberg.

There are a number why these systems have prospered. Among those most commonly mentioned are the following:

- A sharply increased volatility in bonds in the first half of the 1990s. Combined with the increase in the size of orders associated with the growth in institutional investment, this represented an increase in risk for the market makers, who were obliged to assign more capital to these activities.

- The falling margins for market makers were the result of increased competition in this activity, in part thanks to the improvement in the professional price disclosure systems.

- The pressure of major institutional investors to operate in more competitive conditions, reducing the market power of the dealers. In particular, it is worth highlighting the preference for systems that guarantee the anonymity of participants.

- The swift extension of electronic trading systems in equity trading.

The electronic trading platforms may have different characteristics from the method used in normal trading. Among the possible characteristics are the following, which may come in different combinations:

- Auction systems: these are rarely used, and allow the sale of securities both in a primary market (new issues) and the secondary market through processes of auction that can guarantee the anonymity of participants if required.

- Cross-matching systems: they allow trading between dealers and institutional investors by cross matching in continuous or periodic sessions. The orders are executed automatically when the price coincides with orders on the other side.

- Anonymous inter-dealer systems: they allow transactions to be executed between dealers through a mediation service that preserves anonymity (blind brokers).

- Multidealer systems: they allow institutional investors to visualise offer and demand prices from various dealers at the same time, or the best price from among them, allowing the best transaction to be executed.

- Single-dealer systems: they allow the final investor, generally institutional, to make the transaction with a specific dealer. This system is generally limited to replacing the traditional telephone relationship between the dealer and his client by Internet access.

An increasingly common characteristic in electronic trading platforms is that as well as trading services in the strict sense, they offer pre-trade and post-trade services. The aim is to offer flexible and speedy cover of the whole cycle of services needed by the investor in the secondary market, among them the search for prices, the actual transaction, its confirmation to the clearance and settlement system, the clearance of securities with or without the central counterparty service, and finally settlement. The complete efficient coverage of the cycle of services is called straight-through processing (STP).

Table 3 details the main electronic trading infrastructures operating at European level. In most of them, the bulk of trading activity is centred on public debt, and in some of the most liquid private fixed-income securities (simple bonds issued by financial institutions, investment-grade corporate debt, guaranteed bonds and securitisation bonds backed by residential mortgages or RMBS). The interdealer trading systems are those which concentrate the greatest volume of trading, and notable among them is the MTS Group. Within this group, all the systems use a trading method based on cross-matching, except for MTS, which uses a system of firm prices. Within the electronic systems covering dealer-institutional investor trading, the cross matching systems are the most popular in the platforms promoted by stock exchanges, MOT (the Italian Stock Exchange) and the platform promoted by the Swiss Stock Exchange. The most common system, however, is the quote request system (the institutional investor may ask for price quotes from various dealers at the same time through this system). In some cases, it is combined with a system of firm prices.

Electronic fixed-income trading platforms in Europe: main characteristics TABLE 3

Platform	Type of system	Multi-dealer	Trading method	Coverage[4]
eSpeed	Interdealer	Yes	Cross-matching	G, IG, HY, A, S, O
Eurex Bonds	Interdealer	Yes	Cross-matching	G, IG, A, S, O
ICAP[1]	Interdealer	Yes	Cross-matching	G, A, S, IG, O
MTS Group	Interdealer	Yes	Firm prices	G, A, S, O
Bloomberg[2]	Dealer-client[3]	Yes	Firm prices and quote request	G, IG, HY, A, S, EM, O
Bondscape	Dealer-client[3]	Yes	Firm prices	G, IG, A, O
BondVision	Dealer-client[3]	Yes	Quote request	G, IG, A, S, O
MOT	Dealer-client[3]	Yes	Cross-matching	G, IG
Market Axess	Dealer-client[3]	Yes	Quote request	IG, A, S, O
Reuters Trading	Dealer-client[3]	Yes	Firm prices and quote request	G, IG, HY, A, S, EM, O
SWX Swiss Stock Exchange	Dealer-client[3]	Yes	Cross-matching	G, IG, HY, A, S, EM
TLX Euro	Dealer-client[3]	Yes	Cross-matching	G, IG, HY, A, S, EM
TradeWeb	Dealer-client[3]	Yes	Quote request	G, A, S

Source: Bond Market Association and European Primary Dealers Association.

1 Brockertec and ETC.

2 Bloomberg Bond Trader and ALLQ.

3 Client: institutional investors.

4 G: government, IG: investment grade corporate, HY: high yield corporate, A: agency (guaranteed bonds, RMBS), S: supranational, EM: emerging market, O: other.

5 Conclusions

European private fixed-income issuance has grown sharply in recent years, even more so than in the United States, thanks basically to low interest rates. The financial institutions have been the main leaders in the growth of these issues, although there has also been an increase in issuance by non-financial companies. Compared with other European countries, and even with the United States, the size of the private fixed-income market in Spain, measured by the outstanding balance as a percentage of GDP, has reached an extraordinarily high level, reflected in the major increase in issuance in Spain.

Issuance and, in general, public offers of securities are regulated in the European Union through the Prospectus Directive. This important legislation, which simplifies the registration procedures for transnational issues within the European Union (the European issuers' passport) includes various exemptions from the obligation to register a prospectus. One of the most important of these refers to issues exclusively addressed to qualified investors, essentially institutional investors. At the same time, the Prospectus Directive enshrines procedures for flexible registration to prevent unnecessary burdens on issuers and help adapt their issuance schedule to market conditions. In the sphere of placement procedures, the reference system is underwriting, particularly applied to issues with the highest credit ratings in the market. In any event, investment banks and other financial institutions play an essential role in placement procedures due to the importance of having an ample portfolio of potential investors to guarantee the success of the operation. The placements are mainly addressed to institutional investors.

In secondary markets, the basic European regulation is the Markets in Financial Instruments Directive. An important feature of this Directive is the fact that it demands fairly detailed requirements for pre-trade and post-trade transparency for actions in the different types of infrastructures covered (regulated markets, multilateral trading systems and internalisers), but not in the case of fixed income. Whether these requirements should be introduced in debt markets is, currently, an open question in the EU. It is if anything gaining importance in the context of the current financial crisis, given that an improvement in transparency may help a swifter and firmer recovery of activity in the private fixed-income markets most affected by the crisis. In terms of the trading systems, it is obvious that the private fixed-income market is, as is that of public debt, an essentially OTC market, where transactions are carried out bilaterally, both on the wholesale (the interdealer and dealers-institutional investors segment) and retail side. The transactions registered in regulated debt markets, linked to traditional stock markets, are mainly bilateral transactions reported to the market. Electronic trading systems promoted by banks and other financial institutions have become increasingly important since the mid-1990s. These systems are almost exclusively addressed to the wholesale sector and offer various trading alternatives (anonymous systems, cross-matching, quote request, trading at firm announced price, etc.) In general, these systems focus their activity on public debt, though they now cover a wide range of securities issued by the private sector as well.

Reviewing the Lamfalussy process: towards greater convergence in financial supervision

José Manuel Portero (*)

* José Manuel Portero is a member of International Relations Department of the CNMV.

1 Introduction

The Lamfalussy process, initiated by the European Commission in 2001 as a form of facilitating the drafting of regulations for securities markets, was extended in 2004 to the banking and insurance sectors. Currently the creation of financial standards in the European Union, their monitoring and their supervision, is based on this procedure.

Since the implementation of this process, the creation, development and monitoring of financial regulation has been divided into four levels: the first of these is the preparation of framework or general Directives through the co-decision process between the Council and European Parliament; the second level is the implementation regulations drawn up by the European Commission on the advice of the sector-based committees: CESR for securities, CEBS for banking, and CEIOPS for insurance. A third level affects convergence in the application of the legislation through standards, guidance or recommendations. This activity is reserved for the sector-based committees. A fourth and final level is reserved for the European Commission itself in monitoring and overseeing the application of Community legislation by Member States.

Although the Community institutions (the Parliament, Council and Commission) have recognised the progress made in terms of financial legislation and supervision by the implementation of this process, certain deficiencies in its operation were identified almost from the start. An example of this has been, for example, the lack of legal recognition of the committees in the framework of the Community regulation, resulting in their decisions not being binding; or the fact that decisions have had to be taken unanimously, which has also weakened their normal operation.

This is why after barely three years since the Lamfalussy process was extended throughout the financial sector in the European Union, the need has been observed to prepare a reform that reduces some of the weaknesses that have appeared and, at the same time, to reinforce other areas of action with the aim of adapting financial legislation and supervision to a changing financial environment.

This article offers a brief description of the most important actions that have led to the review of the Lamfalussy process. At the same time, it descries the main lines of reform, and the tasks carried out so far, as outlined by ECOFIN in December 2007. Finally, and by way of an afterword, it refers to the recent Larosière group which has been made responsible by the President of the European Commission for the definition of a new model of supervision which takes into account the consequences of the financial crisis.

2 The review process

Below are, in chronological order, the most important activities of the European institutions (mainly the Commission and the Council) that led to the formal inception of the Lamfalussy review process, which can be established as dating from the ECOFIN decision of 4 December 2007 establishing a road map for its implementation.

2.1 The Francq report

The ECOFIN conclusions of 7 December 2004 invited the Financial Services Committee (FSC) to carry out a strategic study on how the current financial regulatory and supervisory framework should be developed over the coming years. The FSC set up an ad-hot working group led by Terry Francq, of the French Treasury, which prepared the report that would later be endorsed by ECOFIN in May 2006. Rather than simply describing the situation at the time, the report stressed the actions that should be taken to tackle it.

The report opted for moving beyond the traditional concept of "cooperation in supervision", based on exchange of information between regulators or supervisors. It developed the concept of "supervisory convergence" based on common supervisory practices, derived from the uniform application of Community financial regulation.

The main conclusions or recommendations, as well as the proposed action lines, were as follows:

a) Challenges identified: strengthen supervision and cooperation, strengthen the cost-efficiency relation in supervision, and lastly, improve cross-border supervision.

b) The need for a political boost to establishing supervisory convergence.

c) Establishment of a common supervisory culture across the European Union. Some measures that could be taken in this respect would staff secondment and joint training projects for supervisors.

d) Establishment of a non-binding mediation mechanism to resolve disputes between banking, securities and insurance supervisors.

e) Establishment of mechanisms for delegating tasks and, where applicable, accountability.

f) Establishment of common formats for communication and information exchange with regulators.

2.2 Directive 2005/1/EC

This regulation of the European Parliament and Council established a new organisational structure for committees dealing with European financial regulation. The Directive laid down that the first complete review of the Lamfalussy process had to be undertaken by the end of 2007.

2.3 The Inter-Institutional Monitoring Group (IIMG)

Following the stipulations of the Directive, the Commission mandated the IIMG to evaluate the implementation of the Lamfalussy process and identify any possible bottlenecks in its operation. In its report, the IIMG stated that the Lamfalussy process had contributed significantly to the integration of European financial markets. However, it also pointed out that this fact had led to new challenges and tasks, in particular for the Level 3 Committees. It suggested that their role as platforms for the coordination of supervision and financial regulation should be reinforced.

For this purpose, it considered it necessary to give the Level 3 Committees an appropriate legal basis and a clear mandate from the European Union that could be accepted by the rest of the European institutions. At the same time, the IIMG report invited the Level 3 Committees to review their decision-making rules in order to increase operational effectiveness. Finally, it highlighted the need for the Committees to have sufficient financial and other resources available to carry out what was a growing number of tasks.

2.4 Communication of the European Commission

With the backing of the IIMG report and the ad-hoc reports from the CESR, CEBS and CEIOPS, on the 20 November 2007 the European Commission published a Communication on the review of the Lamfalussy process. Recognising that the process had fully met the objectives that had been set, the Commission admitted the general consensus on the need to undertake significant changes in the operation of the Level 3 Committees to reinforce cooperation and, above all, to progress towards supervisory convergence.

Although the Commission Communication presented practical proposals for the four levels of the process, it focused its recommendation on the operation of the banking, securities and insurance Level 3 Committees, highlighting the critical importance of their work in achieving supervisory convergence. It proposed that the political accountability of these committees to European institutions should be reinforced. Equally, there should be guarantees for complying with the level 3 measures (standards, guidance or recommendation), even though they are not legally binding.

In addition, it suggested a review the operational rules of the Level 3 Committees, based on European Commission decisions, to reflect better the functions and tasks they carry out. Finally, and most critically, the internal decision-making process should be improved and subject to safeguards, allowing voting by qualified majority in the decision-making process, instead of the current rule of consensus.

3 The ECOFIN conclusions and road map

As has been mentioned above, various European working groups and institutions worked on the review of the Lamfalussy process. However, it is the finance ministers of the Member States through ECOFIN who set out the tasks to be carried out, and who established a road map for their execution in the meeting held on 4 November 2007. Although the review proposed by ECOFIN covers the four operational levels of the Lamfalussy process, the recommendations are focused on the operation of the level 3 committees, in line with the reports from other institutions (IIMG and the European Commission).

The conclusions of levels 1, 2 and 4 of the Lamfalussy process for subsequent development of the level 3 recommendations are set out below.

3.1 Levels 1 and 2 (framework and implementation legislation)

a) The transposition and implementation deadlines for technical measures should be more realistic, taking account of level 2 measures.

b) The European Commission should explain the substantial deviations of its decisions with respect to the technical advice received by the Level 3 Committees, where applicable.

c) Both the European Commission and the Level 3 Committees for banking, securities and insurance should regularly consult with industry to get to know and evaluate the opinion of consumers and users of financial services.

d) Regular preparation of economic impact studies in all areas of the Lamfalussy process.

e) Reduction to a minimum of national options and discretion allowed in Directives. This effort is extendable to the European Parliament.

f) Equally, it invites Member States to keep under review the options and discretions implemented in transposing the Directives, and introduce review clauses if necessary.

g) The European Commission should carry out regular cross-sectoral consistency checks to foster coherence of terminology across all financial services law in the European Union.

3.2 Level 4 (inspection of compliance and application of Community legislation)

a) Member States are reminded that the deadlines included in the Financial Services Action Plan and supplementary measures have to be complied with.

b) Member States should adopt common formats to inform Community institutions on the transposition and implementation of financial legislation.

c) The European Commission should allocate sufficient resources to check that legislation is transposed and implemented correctly, and to implement infringement procedures where necessary.

3.3 Level 3 (convergence in the supervisory process)

As explained above, the Lamfalussy level 3 process concentrates the biggest number of recommendations and has its own specific road map. The main action lines are as follows:

a) The European Commission, in coordination with the Level 3 Committees, should study the differences in supervisory powers and of national financial supervisors. Equally, there should be a cross-sectoral studies on the equivalence and coherence of the various sanctioning regimes in Member States, as well as whether these regimes have sufficient effect.

b) The European Commission should clarify the role of the Level 3 Committees and consider different options to strengthen their working without reducing their accountability or modifying the current institutional structure.

c) The Level 3 Committees should transmit their draft work programmes to the Commission and the Council and European Parliament, so as to allow them to express their view on the key priorities and give policy advice on supervisory cooperation and convergence.

d) It is considered necessary to include in the mandates of national supervisors a task to cooperate within the EU and to work towards supervisory convergence and take into account the financial stability in Member States.

e) The Level 3 Committees should strengthen the application of their standards, guidelines and recommendations without changing their legally non-binding nature.

f) While recognising the importance of continuing making decisions by consensus to enhance the efficiency and effectiveness of their decision-making procedures, the Level 3 Committees should introduce in their charters the possibility to apply qualified majority voting. While these committees' decisions are not legally binding, supervisors who do not comply should explain their reasons publicly.

g) Given the growing workload and increasing number of obligations of the Level 3 Committees, they could benefit from the financial support under the European Commission budget for specific projects.

h) Related to the above point, those tools that contribute to developing a common supervisory culture, such as joint training programmes or secondment schemes, could receive funding from the European Commission.

There are also recommendations dealing with cross-border groups, as follows:

a) The Commission should review its financial services Directives to include provisions where possible to enable the use of the voluntary delegation of tasks. The Commission itself and the Level 3 Committees should analyse the options for the voluntary delegation of supervisory competences.

b) A set of common operational guidelines should be introduced to enhance the functioning of the colleges of supervisors. These guidelines should contain the rights and responsibilities of the members of these colleges.

c) The European Commission, with the technical assistance of the Level 3 Committees, should review the financial services Directives with a view to ensuring that procedures underpinning supervisory cooperation and the exchange of information between supervisors are satisfactory.

d) The Level 3 Committees should develop common formats for financial institutions reporting to supervisors in order to avoid duplication and unnecessary costs.

It should be pointed out that most of the tasks recommended have been carried out either by the European Commission or by the Level 3 Committees themselves in 2008. Among the most important in this respect is the amendment to the CEBS, CEIOPS and CESR charters to establish decision-making procedures by qualified majority instead of by consensus, and the significant increase in training courses for supervisors, which, in a cross-sectoral and cross-border perspective, is contributing to the development, if not implementation, of a common supervisory culture.

In addition, the European Commission has initiated the review of decisions which created the Level 3 Committees. The following section describes this question briefly.

4 The review of the decisions of the European Commission establishing the supervisory sectoral committees

One of the constant recommendations by the institutions that have worked to review the Lamfalussy process has been the need to review the functioning of the Level 3 Committees. As these committees had been created by simple decisions of the European Commission, this institution submitted to public consultation the possible modifications to the decisions by which the European Committee of Securities Regulators (CESR), the Committee of European Banking Supervisors (CEBS) and the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) had been created.

The aim of this consultation was to align, clarify and enhance the responsibilities of the three committees of supervisors and ensure their contribution to supervisory cooperation and convergence, as well as to safeguard financial stability. According to the Commission's own statement, its intention is to establish a common framework for action by the three committees in the area of supervisory cooperation and convergence. It pointed to the main activities the committees should carry out to this end. Equally, the reviewed decisions should contain the responsibilities of the committees in overseeing financial stability and the periodic reporting to supervisors.

The most important points or aspects submitted to consultation by the Commission were those relating to the mechanism of mediation, information exchange, delegation of tasks and responsibilities, the college of supervisors, the development of a culture of common supervision, cross-sector cooperation, the process of voting by qualified majority and the safeguard of financial stability.

Although at the time of drafting this article there has been no formal decision by the European Commission on this question, most of the responses received (among them one reflecting the views of the three sectoral committees in the 3L3 group) to the public consultation indicated the interest that the work and functioning of these committees cause among the participants in the financial industry.

5 The creation of a high-level group of experts on financial supervision in the EU

In addition to the above, and as one of the direct consequences of the financial crisis which began in August 2007, in October 2008 the President of the European Commission created a high-level group of experts led by Jacques de Larosière. The task of this group will consist of making recommendations to the European Commission to reinforce supervisory agreements in the European Union. The group will deal with all the financial sectors in order to establish a more efficient and integrated system of supervision in Europe. At the same time it will enhance cooperation between the European supervisors and their international counterparts. The group will complete its recommendations in February 2009, to be analysed in March by the heads of state and government.

The mandate received by the group is a clear sign of the weakness of the supervisory system in the European Union, as it continues to be compartmentalised on a nation basis, despite the substantial progress in financial integration and the growing importance of entities with a cross-border scope of action. It is also accepted that the reform of financial supervision has followed an evolutionary approach of which the Lamfalussy process, and in particular the Level 3 Committees, are the main examples. Despite certain progress in supervisory convergence, the European Union has not been able to identify and manage the causes of the current financial crisis. The basically national organisation of financial supervision limits enormously access to a true supervisory convergence.

As a result, the group of experts should consider the following aspects:

a) How to organise the supervision of European financial institutions and markets to ensure adequate solidity in the institutions, the ordered operation of the markets and thus the protection of depositors, policyholders and investors.

b) How to reinforce European cooperation in oversight of financial stability, early warning mechanisms and crisis management, including the management of cross-sector and cross-border risks.

c) How the supervisors of the competent European Union authorities should cooperate with other third-country supervisors to safeguard financial stability at a global level.

Finally, the group of experts will also examine the assignment of tasks and accountability at the national and European level.

6 Conclusion

The formal start of the review of the Lamfalussy process has taken place in parallel with the explosion of the financial crisis in August 2007 and its ferocious consequences demonstrated in particular in August 2008.

One of the lessons that may be learned from the crisis is the need to adapt financial supervision, which has a markedly national character, to global objectives in order to make it consistent and in keeping with players (financial institutions and markets) who have already been global for a long time.

As can be seen from this article, the review of the Lamfalussy process did not aim to be a tool for tackling a financial crisis. However, perhaps the final goal of the review, which is to progress in financial supervisory convergence, does have a link to some of the tools that are being used to combat the crisis.

Although many of the planned actions have already been implemented, the review of the Lamfalussy process is not complete, so it would be unwise to decide whether it will be a success or failure. In any event the review of the regulation and supervision of financial institutions and markets is not fixed, but fluid. Institutions and markets that are in a permanent state of evolution should respond to a pattern of regulation and supervision that is also in a permanent state of evolution.

The considerations of the President of the European Commission on the limitations of the review of the Lamfalussy process, reflected in the creation and mandating of a group of experts to design a new organisation of financial supervision, makes clear that we are merely the end of the beginning of the review of financial supervision in the European Union.

III Regulatory novelties

The new collective investment undertaking accounting circular

Jorge Vergara (*)

* Jorge Vergara belongs to the CNMV Supervisory Division.

1 Introduction

Collective investment undertakings (CIUs) constitute a vehicle for participation by a large number of both retail and institutional investors in capital markets.

In the case of Spain, successive legal reforms have created a legal framework on which development of these investment vehicles is built. This legislation particularly includes the Collective Investment Undertakings Act, 35/2003 of 4 November (*Ley 35/2003, de 4 de noviembre, de Instituciones de Inversión Colectiva*) and the Regulations pursuant to this Act promulgated by Royal Decree 1309/2005, of 4 November, which liberalised the investment regime of CIUs, broadening the range of assets in which these institutions can invest.

This legislation has been developed by other legislation of lower ranking, which particularly includes that aimed at establishing the accounting system governing these undertakings. This accounting system was represented by Circulars 7/1990 and 4/1994, on accounting rules for securities and real estate CIUs respectively, which constituted implementation of the 1990 Spanish General Accounting Scheme (*Plan General de Contabilidad*) in relation to CIUs. To this end both circulars adapted and specified the general accounting system for undertakings, which basically comprise a portfolio of investments, whether of securities or real estate, and which are of an open-ended nature, which is demonstrated by the possibility of regulated entry and departure of investors at a certain price, which is the liquidating value of the institution.

The new Spanish General Accounting Scheme was promulgated on 4 November 2007, pursuant to Royal Decree 1514/2007, and came into force on 1 January 2008. This new accounting scheme incorporates a decision to maintain the individual preparation of accounts of Spanish undertakings as laid down in the accounting principles of Spanish Business Accounting Law, but at the same time acknowledging the International Financial Reporting and Accounting Standards (*NIC-NIIF*) as obligatory reference.

Approval of a new accounting framework consequently makes it necessary to adapt the accounting standards of CIUs to the new regime. This adaptation is important because the new standards accord great importance to financial instruments. The approval of CNMV Circular 3/2008, of 11 September, on accounting standards, annual accounts and reserved information statements of CIUs reflects the exercise of adapting to the 2007 Spanish General Accounting Scheme. This article is devoted to an analysis of it and is structured in the following manner.

The second section of the article deals with the scope of application of the Circular and formal and procedural matters inherent in the accounting of CIUs. Section three covers the conceptual accounting framework in the form of accounting standards, valuation principles and definitions. Section four, for its part, details the specific rules for CIUs and specifies the manner of accounting for certain transactions.

Section five explains the model annual accounts and public and reserved statements which CIUs must provide, and finally section six contains the conclusions of the article.

2 Scope of application of the CIU accounting Circular and procedural questions

CNMV Circular 3/2008, of 11 September, on accounting standards, annual accounts and reserved information statements of CIUs, or the CIU accounting Circular, constitutes the development and adaptation to the collective investment sector of the accounting rules contained in the Commercial Code, the Companies Act and Spanish General Accounting Scheme. The singular nature of these institutions makes the existence advisable of various specific rules regulating their accounting regime. The Spanish General Accounting Scheme itself recognises the heterogeneous nature and complexity in recent times shown by financial markets and the entities which operate in them.

The scope of application of Circular 3/2008 refers to the collective investment undertakings regulated by Act 35/2003, of 4 November. The accounting Circular will thus apply to CIUs of a financial nature (investment funds, or IF, and variable capital investment companies "SICAV") and to real estate CIUs (real estate investment funds, or REIF, and real estate investment companies, or REIC). Even though both types of CIU, financial and real estate, will be governed in accounting terms by various common principles and standards, the different type of assets in which they invest make it necessary for the Circular to devote separate sections to each category. Furthermore, within financial CIUs the greater operating capacity and flexibility of hedge funds[1] (free investment CIUs) require the implementation of certain accounting standards, particularly in relation to financing operations.

Although the accounting framework which will govern CIUs covers a very broad range of operations, their transactions must respect the investment and operating restrictions established by the legal framework governing CIUs and the restrictions which CIUs voluntarily establish in their prospectuses. As a result, the existence of accounting standards does not imply authorisation for transactions if provisions exist which prohibit them.

On these lines it is considered that the compartments which may exist within a CIU[2] have a certain accounting autonomy. Thus, although there may be single models of annual accounts for a CIU even though it covers various compartments, separate

1 *IIC de Inversión Libre* ("IICIL" or hedge funds) are a specific type of financial CIU characterised by being able to invest in any type of financial asset and financial derivative instrument independently of its underlying, and as a result are not subject to the diversification and debt coefficients and commission limits of ordinary CIUs. They consequently constitute what in Anglo-Saxon terminology would be described as *Spanish onshore hedge funds*.

2 The concept of the CIU compartment was introduced in the last legal reform of the legal regime governing CIUs and, under a single contract or deed of formation, enables investment companies or funds to be structured into compartments or sub-funds which are distinguished by their different investment policy. In short, a typical concept of collective investment is being translated into Spanish legislation, being the "umbrella" fund or fund which covers different sub-funds, which can be found in several surrounding countries.

accounting is permitted which distinguishes between the assets and liabilities and income and expenses of one compartment in relation to others. This is important, since in general terms no joint and several liability is established between compartments, and furthermore investors will be under such liability in relation to particular compartments but not in relation to others.

A further point which merits mention for the purpose of profiling the scope of application of the CIU accounting rules is the exemption relating to rules on combinations of businesses. These rules regulate the manner in which operations must be accounted for in which one undertaking acquires control of one or more businesses. In the field of CIUs, the combination of businesses in general originates from the acquisition of shares or holdings in the capital of other undertakings in sufficient proportion to guarantee their control; they should consequently be valued at cost with recognition of deterioration, as the case may be. It must be taken into account that the legislation governing CIUs prohibits them from exercising a substantial influence over undertakings in which they invest.

This exemption from the rules on business combinations also covers master-feeder[3] structures, and therefore a subordinated fund will not have to value investments in the principal fund at their cost. The only exception to the foregoing would be combinations of businesses as a result of mergers between CIUs, which involves accounting by the absorbing CIU of the assets acquired and liabilities assumed of the CIUs absorbed.

In relation to formal and procedural questions of CIU accounting, it is necessary to distinguish between annual accounts, public statements and reserved information statements.

The annual accounts of a CIU are the balance sheet, profit and loss account, statement of changes in net worth and notes to the accounts[4], which must conform to the structure and content of the Spanish General Accounting Scheme, with certain adaptations to the nature of CIUs. These adaptations are particularly significant in the case of the balance sheet and profit and loss account, whose headings and accounts are adapted to the specific reality of CIUs, and in the Circular they are denominated public accounting statements. These public statements making up the annual accounts are supplemented by reserved accounting statements, without public dissemination, which are sent to the CNMV for the purpose of exercising the supervisory functions entrusted to it in relation to CIUs. A more detailed explanation of these accounting statements can be found in section five of this article.

3 Accounting principles, criteria and definitions

The fundamental aim of Circular 3/2008 is to show a true picture of the net worth, financial situation and profit and loss of collective investment undertakings, for

3 A subordinated fund or "feeder" is a fund which is characterised by investing the greater part of its assets (80% under Spanish legislation) in another fund, which will be the principal or "master" fund, and which is the one which makes the final investments in assets. In this manner, final investors invest in the subordinated funds which are therefore configured as mere vehicles for investment in the principal funds.

4 The cash flow statement, which may not be required if so established by legal provisions, is not required of CIUs as a result of its scant representative nature.

which general accounting principles are applied. As mentioned, CIUs, except for REIC, are open-ended financial entities in which individuals can make their investments and disinvestments at a price, which is the liquidating value of the institution. The liquidating value therefore represents the price of the proportional parts into which the net worth of CIUs is divided, which will constitute the units in funds and shares in companies.

The accounting of CIUs must take into account the need to determine the net worth which enables the liquidating value of undertakings to be calculated. The liquidating value is therefore a direct consequence of the accounting.

The need to determine the liquidating value of CIUs is illustrated when analysing application of the principle of going concern in the field of CIUs. This principle means that, in the absence of evidence to the contrary, management of the CIU will continue in the foreseeable future, and therefore application of the accounting principles and criteria does not have the purpose of determining the net asset value for the purpose of its total or partial transfer, nor the resulting amount in the event of liquidation. A distinction must nevertheless be made between a total or final liquidation, which means dissolution and extinction of the fund, and a liquidation for the purpose of permitting the entry and exist of investors. In this case, the liquidating value is fundamental.

Another principle which is of great importance in CIUs is that of prudence, pursuant to which profits will only be recorded which are obtained up to the closing date of the financial year, and all risks must be brought into account originating in the financial year or in a previous year as soon as they are known. The need to value the assets and liabilities of CIUs for the purpose of determining the price of the proportional parts of investors thus makes it necessary to consider latent gains not realised on assets in the portfolio of CIUs which, moreover, is permitted at the level of both European legislative provisions and at the level of the Commercial Code itself[5].

With respect to valuation principles, the accounting Circular sets out the criteria of reasonable value, amortized cost and historic cost. The Circular translates the legal concepts of effective value or estimated realisation value which appear in CIU-specific legislation when referring to net asset value, and assimilates them to accounting valuation principles. Consequently, depending on the type of asset, its effective or estimated realisation value will be its reasonable value, amortised cost or historic cost. The following section examines which value is applied to each asset.

With respect to the concept of reasonable value, which is that of most relevance in CIU portfolios, in the case of financial assets there is a hierarchy of valuation, such that in the presence of an active market[6] reasonable value is determined from the pric-

5 Section 30 *bis* of the Commercial Code, in sub-section 1, permits valuation at reasonable value of financial assets which form part of a trading portfolio, are classified as available for sale, or are derivative financial instruments, as well as the financial liabilities which form part of a trading portfolio or are financial derivative instruments. Furthermore, sub-section 5 provides for application of reasonable value to other financial instruments on the terms determined by regulations, within the limits established by international financial reporting standards adopted by European Union regulations, and regulations may establish the obligation to value other asset elements other than financial instruments at their reasonable value, provided that the said elements are valued on a sole basis in accordance with this principle in the said European Union regulations.

6 A market is considered active if firm quotation prices are easily and regularly available through an exchange, a significant number of financial intermediaries, price fixing services or similar mechanisms, and

es of transactions executed in it. In the absence of an active market, other valuation methods and techniques are used, which are also specified in the following section.

In the case of real estate CIUs, the legislation itself establishes a valuation principle which responds to the concept of reasonable value, which is the appraisal value of real estate determined in accordance with legislative provisions which exist for the purpose[7].

4 Accounting rules and accounting for transactions

4.1 Classification of assets and timing adjustments

The new Spanish General Accounting Scheme establishes different categories of financial assets based on the different management which may take place in respect of them[8].

For their part, CIUs are configured as collective investment instruments which receive contributions from the public for investment in property, rights and securities, under certain criteria detailed in the prospectus. In other words, the portfolio of a CIU comprises a group of assets managed by management companies with capacity for the purpose and with adequate risk control procedures and whose return is assessed on the basis of its reasonable value in accordance with a documented investment or risk management strategy. This is precisely the definition established by the Spanish General Accounting Scheme for the category of "Other financial assets at reasonable value with changes to profit and loss account", and which is that which is therefore applied to the financial investment portfolio of CIUs.

Consequently, financial assets included in the portfolio of the CIU will be valued at their reasonable value and variations in this value, even if not realised, will be attributed to profit and loss. This is all consistent with the need to determine the estimated realisation value of the assets of the CIU for the purpose of calculating the liquidating value of the institution.

With respect to the remaining financial assets of the CIU, such as cash and banks, outstanding commission balances and other similar items, given their auxiliary operational nature, and therefore falling outside the investment policy of the CIU, the foregoing classification is not applied but that of loans and items receivable. Consequently, all these assets will be valued at their amortised cost, i.e. updating cash flows at the initial rate of return of the transaction. Of course, in the case of loss in value as a result of reduction or delay in expected flows, the appropriate correction must be made. It will be possible to make a valuation at nominal value in the case of short term items in which the financial effect of updating flows is not significant.

these prices reflect actual market transactions which regularly take place between parties acting under conditions of mutual independence.

7 The rules for calculation of appraisal value of real estate are set out in Order ECO/805/2003, of 27 March, modified by orders EHA/3011/2007 and EHA/564/2008.

8 The classification categories of the Spanish General Accounting Scheme are: loans and items receivable, investments maintained until maturity, assets available for sale, assets maintained for trading, other assets at reasonable value with changes to profit and loss account.

A parallel reasoning can be applied with respect to the financial liabilities of CIUs. Those which form part of the portfolio, such as financial derivatives with creditor balance and those other liabilities which arise from the obligation to repurchase assets sold (as a result of selling securities taken on loan, or provided as security, or temporarily transferred), provided that the transaction is permitted for the type of CIU in question, will be valued at reasonable value with changes to profit and loss account. Liabilities falling outside the portfolio and of an auxiliary or operating nature, such as current account overdrawings to meet repayments within the limits permitted by legislation, will on the other hand be considered debits and items payable and will be valued at their amortised cost.

The real estate included in real estate CIUs merits separate mention. In these undertakings, as in financial CIUs, it is necessary to value their net worth in order to calculate liquidating value. An obligation is consequently established to value real estate at its reasonable value or appraisal value, as previously indicated. Nevertheless, taking into account the more permanent nature of the investments, a similar treatment is given to that of financial assets available for sale and therefore variations in reasonable value of real estate are attributed to net worth under special headings. It should be emphasised that this form of valuation gives rise to no taxation in the year in which the variation has been attributed to net worth but will be taxed in the financial year in which the real estate is sold[9].

Another matter which must be specified is the regularity of valuation of the assets included in the portfolio of the CIU. This must concord to the frequency of calculating the liquidating value of the CIU, or must be more frequent if there are other provisions which so determine. In practice, in the field of financial CIUs, this means that the frequency of valuation will be daily in most cases.

4.2 Principles of valuation of financial assets

After clarifying the accounting classification criteria, the Circular is concerned with specifying what must be understood by reasonable value for the different categories of asset, based on the definition in the Accounting Scheme. In this respect, it must be taken into account that the Scheme firstly has a generalist vocation, as it must have, and secondly CIU legislation has achieved a considerable degree of specification in relation to the range of assets suitable for investment by CIUs. The Circular consequently specifies how reasonable value is determined of the different families of eligible assets.

In the case of asset instruments, i.e. shares, reasonable value is an almost immediate concept since the closing price is taken into account as such of the market which is most representative by volume (i.e. the most liquid). In order for the Circular to cover as extensive as possible a range, index funds[10] are allowed not to use market closing price but the price at the time of fixing the closing index for the day, such that correspondence is ensured, within permitted deviations, between the evolution of liquidating value of the fund and that of the index.

9 In other words, in relation to latent gains no liability will be recognised for current tax, but a liability for deferred tax.

10 Funds which replicate or reproduce an index, and which are regulated by Section 38.2.d) of the Collective Investment Undertaking Regulations, commonly receive the name of "index funds". These funds must have a "tracking error" or maximum deviation with respect to the reference index, of 5%.

The valuation of securities representing debt gives rise to greater difficulties however, since we cannot talk of closing prices and, in addition, as mentioned in the previous section, it is not frequent to have active markets with prices from which reasonable value can be extracted. Alternative valuation methods will thus have to be used which maximise the use of observable market data. These include valuations based on prices disseminated by external sources, such as prices of information disseminators or contributors, provided that the source used is representative of the current situation of markets, particularly in terms of interest rates and liquidity and credit differentials. If internal valuation models are used, they must reflect market differentials in a manner as close as possible to the current situation of the issuer of the type of asset.

The techniques for valuation of securities representing debt referred to must be included in control procedures which guarantee their robustness, reliability and consistency. This consistency must be ensured with respect to the situation of markets, the investor CIU itself and the potential evolution of subscriptions and repayments, such that conflicts of interest are avoided between outgoing investors in relation to those who remain in the institution.

A similar valuation difficulty to that of instruments representing debt is found with derivative instruments not traded on organised markets, or OTC derivatives. In these OTC derivatives the manager must in fact calculate a theoretical value of the instrument which maximises observable market data at any time, particularly volatility, and which must be compared with the prices provided by the counterparty of the OTC derivative for the purpose of determining its reasonable value.

It is interesting to highlight the principle of valuation of one particular type of asset, deposits. In this respect, the Circular lays down an obligation to calculate the reasonable value of deposits by updating their flows. The difference between this form of valuation and that of amortised cost lies in that the flows will be updated not at the original rate for the transaction but at a rate which reflects market interest rates and the credit risk of the issuer at any time. In short, the principle set out in the conceptual framework of the Spanish General Accounting Scheme is being applied, pursuant to which accounting of transactions (and therefore their valuation) must take place based on their financial reality and not just on their legal form. In this respect, it must be borne in mind that although a deposit is not transferred or sold, its financial flows are equivalent to a promissory note, for example, if it is a deposit with liquidation of interest on maturity.

Mention should finally be made of the valuation of investments by CIUs in other CIUs. This will take place at the corresponding liquidating value of the institution, unless the CIU is admitted to trading on a market and prices exist obtained from third party sale and purchase transactions. In other words, in the field of listed CIUs the same philosophy of active market is being translated into the legislation which was previously examined in the case of securities representing debt. In the particular case of investments by CIUs in hedge funds or funds of hedge funds[11], since normal practice with these institutions is to use estimated liquidating values, the

11 Section 36.1.j) of the CIU Regulations permits investments by CIUs in hedge funds, funds of hedge funds and similar foreign CIUs, up to a maximum of 10% of net worth and provided that the prospectus of the institution which intends to make these investments expressly and clearly makes reference to this, including detailed information regarding the investment, the risks involved and the criteria for their selection.

use of these is permitted, whether in the case of preliminary estimates of definitive liquidating value, or of securities at intermediate dates between definitive values. In the case of funds of hedge funds these estimated values may only be applied to 10% of their net worth[12].

4.3 Principles of valuation of real estate investments

In relation to investments by real estate CIUs, the initial valuation of the real estate will be made at the acquisition price, which will include the necessary purchase expenses, including non-deductible taxes. If the real estate is under construction, the initial valuation will be made at the amount paid up in relation to the work carried out.

This initial valuation will be maintained until the first appraisal is carried out which, as previously stated, constitutes the reasonable value of the real estate in the portfolio of real estate CIUs[13].

If the appraisal gives rise to gains, they will be attributed to net worth in an account for adjustments as a result of value changes, unless it is the write-back of a loss recognised in profit and loss. In the case of losses, they will be attributed to the profit and loss account, provided that there is insufficient balance to offset it in the account for adjustments in value previously mentioned.

There are particular cases of valuation of real estate, such as completed real estate in process of refurbishment, the reasonable value of which will be its appraisal value after deducting the final forecast cost of work not carried out. In the case of real estate at the design or construction stage, its reasonable value will be amounts paid up for work carried out plus revaluations generated in accordance with the most recent appraisal value, weighted by the percentage of work carried out on the property. Investments in real estate holding companies and leasing entities will be valued at their theoretical book value, provided that the underlying real estate is valued in accordance with the rules established for real estate CIUs.

The reasonable value of real estate at the construction stage may be modified during the period of validity of the appraisal report in order to incorporate a change in value deriving from the degree of progress with work. To this end, there must be certification of the percentage of work carried out from the supervising professionals or appraiser at the date on which it is intended to take in the new reasonable value.

Furthermore, in the case of conditional appraisals, until the appraiser has issued an express reasoned statement regarding lifting of the conditions, reasonable value of the real estate investment will be taken as the lower of the most recent appraisal value without conditions and the conditional appraisal value.

It should finally be taken into account that there may be other CIUs which invest in real estate apart from real estate CIUs, as in the case of variable capital investment companies (*SICAVs*) which invest in real estate for own use in order to engage in their activity. This real estate is also subject to the valuation rules previously referred to, and an appraisal must be made at least annually. By thus applying this form of

12 Section 44 of the CIU Regulations obliges funds of hedge funds to invest a minimum of 60% of their net worth in hedge funds or similar foreign CIUs.

13 Real estate CIUs are obliged to appraise their investments in real estate at least annually, and also at the time of sale, unless there has been an appraisal in the previous six months.

valuation to property which does not form part of the portfolio of the SICAV the significant impacts are avoided which could occur to the liquidating value of the SICAV in the event of sale of real estate valued at cost, which would be contrary to the interests of participants who have been repaid. In short, it is a further example of adaptation of the accounting rules to the idiosyncrasies of CIUs as open-ended structures.

4.4 Accounting for particular transactions

In this section certain accounting rules are examined which are specific in the field of CIUs, such as those relating to own asset instruments, transactions in foreign currencies and tax on profit.

Own asset instruments are units in the case of investment funds and shares in the case of investment companies.

With respect to units and shares it should be stated that as a first approximation they could be considered as liabilities given their repayable nature deriving from the open-ended nature of CIUs. This is not the interpretation which must prevail, however, since shares and units in CIUs present defining features which are characteristic of asset instruments and not of liability instruments, such as that they are contributions by members and holders, they represent the ownership of the latter of the CIU, and on its liquidation they rank behind creditors. Furthermore, account must be taken of the classification as asset instruments which is made by the Spanish General Accounting Scheme itself in respect of shares and units in CIUs.

In short, the units and shares of CIUs are considered and treated for accounting purposes in the Circular as own asset instruments, although they are not fully equivalent to the own asset instruments of ordinary mercantile companies. This special idiosyncrasy was set out in the name of the specific accounts and headings on the Balance Sheet relating to these instruments. Thus, the headings of "Assets attributed to members and participants" and "Repayable funds" are included, instead of the headings "Net worth" and "Own funds", respectively.

Looking at foreign currency transactions, the Circular sets out the accounting concept of functional currency which, given the nature and legal regime of CIUs, is assimilated to the currency of denomination of the CIU. In other words, although in general terms the functional currency is defined as the currency of the principal environment in which an undertaking operates, it is considered that what is truly determining in the case of CIUs is the currency in which it is denominated and in which all its transactions must be recorded, independently of the fact that the CIU invests in assets denominated in different currencies. In short, predominance is given to the operating dimension of the CIU rather that its investment capacity in different markets.

The Circular also incorporates the categories of monetary and non-monetary items which are contained in the Spanish General Accounting Scheme, considering in general that cash and banks and securities representing debt are monetary items, and asset and real estate instruments are non-monetary. In the case of the portfolio of CIUs, this distinction between monetary and non-monetary is not important, since variations deriving from conversion to the functional currency of the CIU of transactions denominated in a different currency, whether monetary or non-monetary items, come together in variations in reasonable value and are thus attributed to the profit and loss account. On the other hand, exchange differences on cash and banks and credit and debit items in general, which it will be recalled are valued at amortised cost, are recognised under a specific heading. Finally, in the residual case of non-monetary items off-portfolio, such as real estate and fixtures, they do not give rise to exchange differences since their historic cost is taken into account along with the exchange rate at the date of origination of the transaction.

Finally, with respect to accounting for tax on the profits of the CIU, the principle is adopted of the Spanish General Accounting Scheme which gives preference to the assets and liabilities approach compared to income and expenses. In this case the distinction is incorporated between expense/income for current tax and expense/income for deferred tax, a consequence of the timing differences deriving from the different valuation, accounting and fiscal, attributed to the elements making up the annual accounts to the extent that they have an effect on the future tax burden. These timing differences are those which, in short, give rise to assets and liabilities in with regard to deferred tax.

In this respect, the general principle, in accordance with the principle of prudence, is always to recognise liabilities for deferred tax and, with respect to assets for deferred tax, to recognise them only to the extent that it is likely that the undertaking will have future tax gains which permit application of these assets. In the case of CIUs, estimating this possibility of future profits is particularly uncertain since it is equivalent to predicting the future behaviour of financial markets. For this reason, if a CIU has tax losses to set off, they may only be recognised when the CIU has profits and a current expense is being recorded for profits tax, which will be set off as it accrues. In short, this rule is intended to prevent assets arising on the balance sheets of CIUs in respect of tax credits whose realisation may be substantially uncertain.

There is an exception to the foregoing accounting rule when CIUs exist with compartments in which some have profits and others losses. In this case, it must be taken into account that the taxpayer in respect of the CIU is the latter as a whole, not the compartments, such that in order that the CIU as a whole can benefit from lower taxation the rule permits the application of tax losses to be set off against one or more compartments with the present profits of one or other compartment. Clearly, the limit of set-off will be the series of profits of the different compartments.

5 Model annual accounts and reserved information statements of CIUs

The Circular introduces two series of model public and reserved statements for CIUs, one for financial CIUs and another for real estate CIUs. The public models are the balance sheet and profit and loss account, which are accompanied by reserved information statements. These must all be sent remotely to the CNMV and must be signed jointly by the management company or self-managed company and by the depository.

In relation to the public models, it should be stressed that there will be one balance sheet and one profit and loss account for each compartment, and a balance sheet and profit and loss account for the CIU as a whole, which receive the name of aggregate balance sheet and aggregate profit and loss account. These aggregate accounts will be drawn up by simple addition of the accounting balances on the individual accounts of the compartments, with elimination of common transactions.

With respect to the reserved information statements, their regularity may be quarterly and, more frequently, monthly, and they set out a series of data necessary for the supervision of CIUs. This data in particular includes daily liquidating value and net worth, as appropriate, and above all that relating to details of individual positions of the portfolios of the CIU or of its compartments, both cash investments and in derivatives, and the portfolio of real estate of real estate CIUs.

Furthermore, with respect to reserved information statements, it is worth highlighting that there are different levels of breakdown based on the structure of the CIU, i.e. whether it has different compartments and/or classes of holdings or series of shares. In this manner all statements which refer to portfolios must be at compartment level, or at the level of the CIU if it does not have compartments, whilst the statements setting out data such as liquidating value and commissions will be at the level of class or series.

Before completing the consideration of information models, it is worthwhile making a comment regarding hedge funds and funds of hedge funds. Only public models and more simplified reserved statements are required from the former[14], since the profile of their investments give rise to a lesser stringency in supervisory efforts. On the other hand, funds of hedge funds, by constituting the vehicle for access by retail investors to hedge funds, must provide the same statements as ordinary CIUs of a financial nature. In both cases the two CIUs have longer periods to send the information.

In relation to the annual accounts of CIUs, they will comprise the public model balance sheet and profit and loss account and be accompanied by a statement of changes to net worth and notes to the accounts.

With respect to the notes to the accounts, which complete, amplify and comment on the annual accounts, the Circular refers to the model of the Spanish General Accounting Scheme, although it introduces certain qualifications. Thus, in the case of financial CIUs detailed information must be given regarding compartments, such as their tax situation, proportional part of common expenses which they bear and investments which they make in other compartments. With respect to real estate CIUs, information must be included in the notes to the accounts on options, contracts for guarantee or minimum return which may affect the reasonable value of the real estate and the obligations to third parties arising from the real estate.

6 Conclusions

Collective investment undertakings are investment instruments present in all developed financial systems and combine advantages inherent in economies of scale and synergy of collective management with investor protection, risk diversification, transparency and liquidity.

14 The model reserved statements of hedge funds are the hedge fund models set out in Circular 1/2006, of 3 May, on Hedge Funds.

This specific nature of CIUs has in several countries given rise to CIU accounting being governed by their own accounting rules, separate from international accounting standards, and with a full distinction being made in accounting for determining net worth and calculating the liquidating value of the CIU.

This has not been the approach adopted by the specific legislation of Spanish CIUs, which establishes that the accounting law represented by the Commercial Code, the Companies Act and the Spanish General Accounting Scheme must be applied to CIUs, subject to the specific aspects which may be necessary. Thus, what CNMV Circular 3/2008 has done has been to adapt the general accounting doctrinal body to the specific nature of CIUs. In other words, it has attempted to issue a series of accounting rules which respect the general body of doctrine principally represented by the Spanish General Accounting Scheme, but at the same time taking account of the particular features of collective investment and therefore minimising the uncertainties which general accounting standards could create among information generators and users.

These specific accounting rules for CIUs will in the final instance permit their net worth to be determined and valued and therefore the liquidating value of the institution calculated, which is the parameter pursuant to which investments and disinvestments in CIUs will be made, and which is used as reference for determining its profitability.

In accordance with the above, it should be indicated that not all of the work has been concluded with Circular 3/2008. In complementary manner, the CNMV has also approved Circular 6/2008, of 26 November, on determination of liquidating value and operational aspects of CIUs which, based on the accounts defined in Circular 3/2008, details the manner of calculating the liquidating value of CIUs from an operational point of view.

In short, both circulars constitute a whole which seeks maximum efficiency and transparency in the process of fixing the prices of CIUs and in the clarity and reliability of financial information, which will benefit one of the CNMV objectives, which is the protection of investors.

The new legislation on periodic public reports by Collective Investment Undertakings and position statements

Gonzalo Palencia Garrido-Lestache (*)

* Gonzalo Palencia Garrido-Lestache is a member of the CNMV Supervisory Division.

1 Introduction

The new CNMV Circular 4/2008, of 11 September, on the content of quarterly, half-yearly and annual reports by collective investment undertakings (CIUs) and position statements (hereinafter the Circular), implements Sections 17 and 18 of the Collective Investment Undertakings Act and 24 and following of Royal Decree1309/2005, of 4 November, promulgating the Regulations under the Collective Investment Undertakings Act (hereinafter the CIU Regulations).

With respect to the position statement, Circular 4/2008 introduces a novel standardised model which must be sent to unit holders and shareholders. The previous legislation on specification of the functions of depositories (Order of July 1992) authorised the CNMV to implement a standardised model position statement, but this model was not developed. The current legislation on the functions of depositories, Order EHA/596/2008, of 5 March, also authorises the CNMV to develop this model and it is now, with promulgation of Circular 4/2008, that the standardised model position statement has been implemented.

This Circular basically sets out the contents of Schedule B of the annex to Directive 85/611/EEC (modified by Directive 2004/39/EC). As will be seen, the Circular broadens the information which must be provided, which becomes more comprehensible and will facilitate knowledge by investors of the results and prospects of their investment.

The Circular also repeals the previous legislation on quarterly reports, in particular CNMV Circulars 1/1991, of 23 January, on the content of quarterly reports of CIUs to their members and holders, and CNMV Circular 1/1999, of 14 January, on quarterly reports and prospectuses of investment funds. It consequently achieves uniformity in two senses: firstly, it consolidates previous aspects and ends the legislative fragmentation existing up to now, and secondly it specifies how the information to be completed is to be drawn up, which will enable it to be more uniform and comparable between CIUs. This article will deal in detail with the importance of this comparability characteristic.

The article is structured into six sections. Section two describes the principal novelties incorporated by the Circular and makes a brief comparison with the previous legislation. Section three comments on the calculations and formulas contained in the Circular. Finally, an analysis in greater detail is made of the content of the annexes (section four) and position statement (section five). The article ends with various conclusions which are set out in section six.

The Circular comes into force on 31 March 2009. Any information provided to the CNMV with reference to periods ending on subsequent dates must conform to the new legislation. In other words, in relation to reports the reference date will be 30 June 2009 and in relation to position statements the reference date will be 30 April

2009 in the event that transactions have taken place in that month, otherwise the reference date will be transferred to the following corresponding period.

2 Novelties of the new Circular. General aspects

The implementation of Sections 17 and 18 of the CIU Act and 24 and following of the CIU Regulations by the Circular implies *de facto* regulation of the content of the quarterly, half-yearly and first part of the annual reports (second six months of the financial year).

The annual report is divided into two parts, a first part which corresponds to the periodic public report for the second half of the financial year, and a second part which, in accordance with Section 27 of the CIU Regulations, comprises the annual accounts, management report and audit report. The Circular does not regulate the content of the second part of the annual report.

There are two quarterly reports, corresponding to the first and third quarters of the year (reference dates of 31 March and 30 September, respectively). Under the previous legislation the reports could be complete or abbreviated. The difference between the two lay in that in abbreviated reports (models which were contained in Circular 1/1999) certain aspects were not reported, such as details of portfolio composition and open positions in derivatives, counterparty risk, market risk, etc.

With the new Circular the difference between the complete and simplified reports lies in that in the third section of the standardised reports (financial investments), the former incorporate full details of the portfolio (position to position) and the latter do so at the level of sub-totals or totals. The first case relates to complete reports and the second is reserved for simplified reports.

The unit holder or shareholder must therefore be provided with the following information:

a) Before subscription: he must be provided with the most recent half-yearly report and, on prior request, the second part of the published annual and quarterly reports. These reports will be simplified, unless the participant elects for the complete reports, a possibility provided by the second paragraph of Rule 3 of the Circular.

b) Periodic information: the successive half-yearly and annual reports must be sent to him. The quarterly reports will only be mandatory if requested. The unit holder or shareholder may nevertheless waive the right to periodic information. The waiver of sending the annual and half-yearly report will imply waiver of the quarterly report. This waiver can be revoked.

The Circular incorporates the novelty that in the case of remote contracting it authorises a formal procedure to request the sending of reports by remote means. Although CNMV Circular 1/91 already provided that information could be sent by any means of electronic or computerised transmission, the regulation now progresses in the use of more up-to-date terms, such as being able to indicate an e-mail address, carry out transactions through a website, etc.

The periods for sending the information have not changed (one month to send it both to unit holders and shareholders as well as to the CNMV). It must be emphasised, however, that a period of five months is laid down from closing of the financial year to send the second part of the annual report to the participant.

On the other hand, under the previous legislation the CNMV had to be sent both complete and abbreviated reports (if taking up the model under CNMV Circular 1/99). With the new Circular the CNMV must now be sent only the complete report. This information must be signed twice, by the depository and by the CIU Management Company or investment company.

By way of novelty, it can be mentioned that reports will be sent in XBRL language (*Extensive Business Reporting Language*). This language was created to simplify the treatment of financial reports. The treatment of data is hugely simplified since the information is structured by labels, which permits information to be made uniform.

Comparability is facilitated by the fact that the information is more uniform and simple to process. This possibility of comparison will mean greater transparency of information provided to unit holders and shareholders. This will without doubt result in better decision-making, save costs in time and provide investors with greater knowledge of the prospects and evolution of their investments.

3 Information figures

This section comments on a series of figures set out in Circular 4/2008. This data will simplify the information received by investors.

3.1 Expenses ratio

In order that investors can ascertain the cost structure of the CIU in which he invests, the Circular provides that information on these costs must take the form of ratios of direct and indirect expenses.

The previous legislation already established, in the section on fund behaviour, that it was necessary to report on all expenses borne by the CIU (management commission, depository commission, external expenses, etc.) in relation to daily average assets and liabilities for the period, expressed as a percentage. This Circular explains in detail the procedure for calculating the two ratios (direct and indirect or "synthetic").

3.1.1 Ratio of direct expenses

The ratio of direct expenses, or TER (*Total Expenses Ratio*) expresses the total expenses borne by a CIU in a period in relation to the figure of average net assets. In this manner investors can ascertain the level of expenses borne by a CIU and compare it with other similar.

The numerator must include all direct expenses borne by the CIU, which include expenses such as management and depository commissions, fees, audit services, etc. and those others which are directly attributable to the fund. The calculation of the direct expenses ratio will not include commissions on sale of financial assets, in accordance with the criterion adopted by the CESR.

3.1.2 Indirect expenses or synthetic ratio

Since the ratio of direct expenses, or TER, does not express the entire cost structure incurred by a CIU, since the numerator only includes direct costs, the Circular incorporates another ratio, that of indirect expenses or synthetic ratio. The ratio of indirect expenses must thus be reported when the investment policy of the CIU consists of investing more than 10% of its assets in other CIUs.

In order to calculate this ratio the TER will be taken, to which will be added, as the case may be, the subscription and repayment commissions borne on the investment in the underlying CIU. This will be weighted by the percentage represented by the underlying CIU in relation to the net assets of the investor CIU.

In the event that the CIU subject to investment does not calculate the TER, the impossibility of calculating it must be reported. Nevertheless, the ratio of indirect expenses will have to be estimated based on the management and deposit commission of the underlying CIU. The calculation, in this second case, will be made in the same manner as seen previously, with the qualification that the TER would have to be replaced by the management and deposit commissions established by the CIU subject to investment.

The management commission of the underlying CIU will be deemed to be net of rebates. In the event that the Manager of the underlying CIU rebates part of the management commission, this rebate will be taken into account when calculating the ratio of indirect expenses or synthetic ratio. The rebate received will be deducted from the management commission established by the underlying CIU.

3.2 Portfolio rotation index

This is another novelty established by the Circular. An index of portfolio rotation must be included in reports, which will constitute an additional indicator of the importance of intermediary costs since they are excluded in calculating the ratio of direct expenses. In this manner the investor, even though not aware explicitly of the amount of the portfolio transaction costs, will by means of the rotation index have an approximate indicator of the intermediary costs of financial assets borne by the CIU.

Its calculation is very simple. The sum of subscriptions and repayments which have taken place in the reference period will be deducted from total sales and purchases also taking place in the reference period: and the foregoing will be divided by the average net assets of the CIU.

Consequently, in order to calculate the portfolio rotation index no account will be taken of sales and purchases of securities resulting from subscriptions or repayments. It was considered that these sales and purchases do not form part of the management of a portfolio and therefore should not be included in the rotation index.

3.3 Return, or performance

The calculation of return does not present novelties. The Circular provides that the return obtained by the investor in the last five years must be reported. Nevertheless, the novelty can be highlighted that if the investment policy of the CIU has been changed in its explanatory prospectus, there is no need to report on historic return until data is available to be included in reports.

In addition, the Circular provides that there must be reporting on the following:

a) In the case of referenced funds, the return or performance of the reference index and the correlation.

b) In the case of funds which reproduce or replicate an index, the deviation must be included in relation to the index to be reproduced (*tracking error*). This latter indicator reports that a CIU deviates, voluntarily or involuntarily, from its reference indicator.

3.4 Volatility

Historic volatility had already been reported previously: specifically, Circular 1/1991 provided for its calculation by typical deviation of daily return calculated for a 12 month period.

The new Circular specifies and clarifies various aspects in relation to the calculation. It thus provides that historic volatility will be the annualised typical deviation of return for the corresponding period. It will be annualised on the basis of the frequency of calculating liquidating value. Consequently, if a CIU calculates liquidating value daily the result will be multiplied by a root of 365. In the case of monthly calculation it will be multiplied by a root of 12.

It must be taken into account that the return which will serve as the basis for calculation of typical deviation will be determined by naperian logarithms in accordance with the following expression: ln VL d / VL d-1.

CIUs must report in the section on "behaviour" of the report on the historic volatility of liquidating value. If the prospectus provides for a reference index, the volatility of this reference index must be included. If the prospectus does not provide for a reference index there must be reporting on the historic volatility of the Ibex 35 and of the one-year treasury bill.

Investors are thus provided with a risk measurement, as is volatility, in order that it can be compared with that of their investment. The volatility of the Ibex 35 and of the Bill also provides references for investors. The Ibex 35 was chosen since it is the most significant reference index at national level, and in the case of the one-year treasury bill, because it represents a risk-free asset[1].

1 The index of one-year treasury bills which will serve as the basis for estimating volatility is calculated in the following manner: Index t = index (t-1) x (Price t / Price (t-1)).

3.5 Value at Risk

The Circular incorporates a risk measurement, Value at Risk (VaR), in order that investors can compare potential loss under normal conditions in respect of their investment against that of other CIUs.

The explanations contained in reports on VaR must transmit to holders that this risk measure is a question of measuring the maximum possible loss which may occur in an investment based on the results produced by that investment in the past.

VaR is defined in the Circular as the maximum which can be lost in a period of one month if the behaviour of the CIU in the last five years is repeated. The level of confidence established is 99%. It will take the sixty most recent available observations, although its calculation will take place at the time when twelve observations are available.

4 Content of the Circular

As indicated at the beginning, the Circular regulates the standardised models for half-yearly, quarterly and first part of annual reports. The annexes to the Circular contain the standardised models which are sent to unit holders and shareholders. The models have been classified on the basis of the different types of CIU which exist in our legislation but, in particular, provide for the new categories of CIU introduced by the CIU Regulations. The information to be provided to investors is thereby adapted, on the basis of the nature of the CIU, in order that it can be comparable.

The models set out in the Circular, and contained in its different annexes, are:

Annex 1: Model for Securities Investment Funds.

Annex 2: Model for Variable Capital Investment Companies.

Annex 3: Model for Real Estate Investment Funds.

Annex 4: Model for Real Estate Investment Companies.

Annex 5: Model for Listed Investment Funds.

Annex 6: Model for Hedge Funds and Funds of Hedge Funds.

Annex 7: Model for Hedge Companies and Hedge Fund Variable Capital Investment Companies.

Annex 8: Model Position Statement.

The structure of reports now comprises nine sections, as follows:

1. Investment policy and currency of denomination.
2. Financial data.
3. Financial investments.
4. Relevant events.

5. Explanatory annex on relevant events.

6. Connected transactions and other information.

7. Explanatory annex on connected transactions and other information.

8. Information and warnings at the request of the CNMV.

9. Explanatory annex of the periodic report.

The most representative aspects of each of the models listed are indicated below, taking into account that the base or standard model will be the first, i.e. that of securities investment funds. The remaining models maintain the structure of the first but the information to be provided varies based on the different types of CIU.

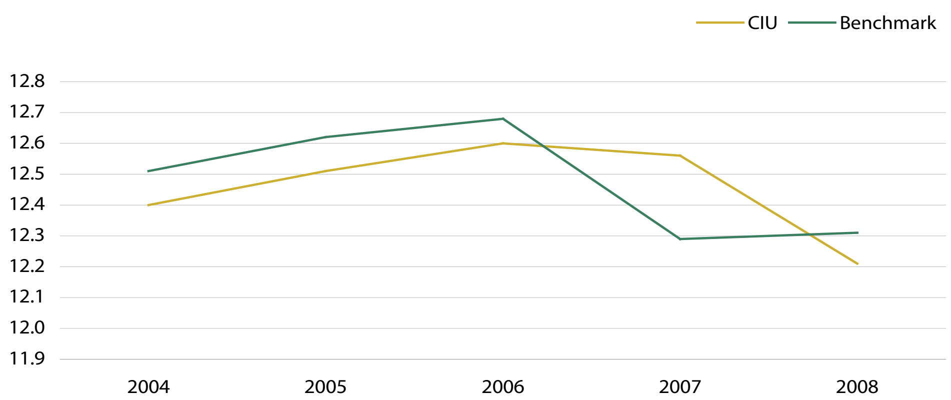
4.1 Securities investment funds

One of the novelties which must be included in the first annex, reserved for securities investment funds, is the rating of the depository[2]. It must further report on the average return obtained by the balances maintained with the depository and one-day repos.

In the case of referenced funds the return of the index must be reported and correlation and, in the case of funds which replicate or reproduce an index, on the deviation in relation to the index (*tracking error*).

Another novelty included by the Circular is information on what has been denominated "return extremes": in other words, minimum and maximum returns between two consecutive liquidating values occurring within the last quarter, the last year and the last three years. Furthermore, a graph must be included of evolution in liquidating value in the last five years. The graph must include evolution of the benchmark and, if the fund does not have one, evolution of the one-year treasury bill must be included, which we will consider as a risk-free asset.

Example of graph of evolution in liquidating value FIGURE 1

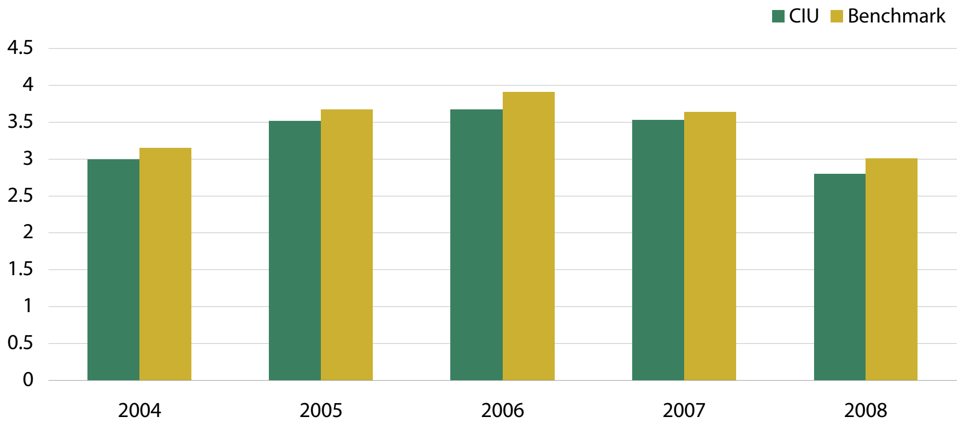


Source: own preparation.

2 When granted by a rating agency recognised by the CNMV.

A further graph must be included on quarterly-half-yearly return in the form of columns. In the case of quarterly reports the graph must include evolution in the last three years, in the case of half-yearly reports evolution in the last five years. The graph in column form must also contain the return of the benchmark. As in the previous case, if there is none it will be taken that it is the one-year treasury bill.

Example of graph of evolution of return in a quarterly report FIGURE 2



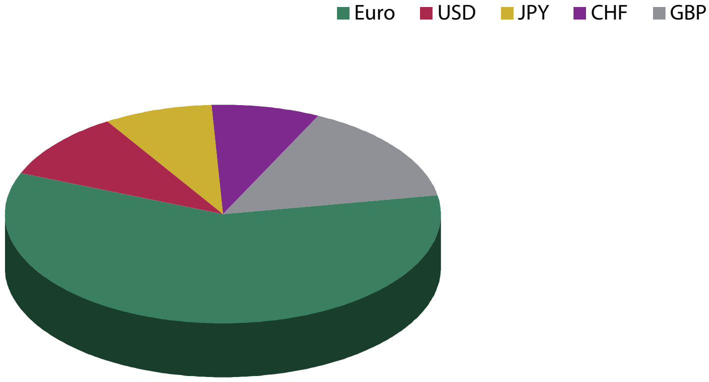
Source: own preparation.

Furthermore, a comparison must be included of average return in the reference period of funds managed by the manager. The funds must be grouped in accordance with their investment vocation defined in prospectus (monetary, euro fixed income, euro equity, etc.). The return of each group of funds must be calculated on the basis of their average net assets in the period.

New categories are also added in presentation of portfolio composition. Under the previous legislation a distinction was made between fixed income (temporary acquisitions, monetary and others) and equities. The portfolio is now classified between fixed income and equities (distinguishing whether listed, not listed or pending admission to listing, public or private), collective investment undertakings, deposits and risk capital entities.

A graph must further be added in the form of a pie chart of financial investments in accordance with the most adequate criteria estimated by the management company, such as rating, currency, sector, etc. Between one and four charts must be included per fund or compartment. The maximum categories in each graph will be five. A category entitled "Other" will be established, as the case may be, which will comprise what is not included in the remainder.

Example of distribution of financial investments FIGURE 3



Source: own preparation.

In relation to positions in derivatives, the Circular provides that as from now reporting will be at the level of the underlying. The information must be presented in four columns, the first including details of the underlying, the second the type of financial instrument (option, future, warrant, etc.), the third the nominal committed and the fourth the investment objective (hedging, investment or specific return objective).

Another novelty consists of inclusion of a specific item (number eight) in the model report, which relates to information and warnings at the request of the CNMV. Although the previous legislation provided for the possibility that the regulator may require inclusion in reports of such additional information as it considered necessary, a specific section is now included in order to complete this information, as appropriate.

Section nine of the model report concludes with an explanatory annex on the periodic report. The purpose of this annex is to explain, clarify and comment on the other previous sections. In general terms it replaces the management report. This annex contains a minimum of information although any additional explanatory comments may be included as considered desirable.

4.2 Variable capital investment companies

The second annex, relating to variable capital investment companies (*SICAVs*) particularly includes the following obligations:

- It must be stated whether the company is listed on the alternative stock exchange (*MAB*) or on a securities exchange.
- If quoted on a securities exchange the maximum and minimum quotation must be indicated for the period, as well as the quotation at its end. It must further report on the average daily volume of trading and its frequency (number of days quoted/number of days on which the share could be quoted).
- It must further report the volume and percentage of capital held by each major shareholder.

4.3 Real Estate Investment Funds

A novelty is included to the effect that in order to calculate the ratio of direct expenses the numerator must include the specific expenses deriving from its real estate nature, such as appraisal, insurance, property management, property associations, repairs, refurbishment and conservation, etc.

4.4 Real Estate Investment Company

In this case the Circular provides that it must state whether the real estate investment company is listed or not and that returns must be calculated taking into account theoretical share values.

4.5 Listed Investment Funds

The novelties are:

- It must state in the investment policy that it is a fund which reproduces an index.
- Its denomination must be indicated.
- The strategy followed in order to replicate or reproduce an index must be mentioned.
- The risk measures must be reported in the same manner as for a securities investment fund, adding the volatility of the index reproduced.

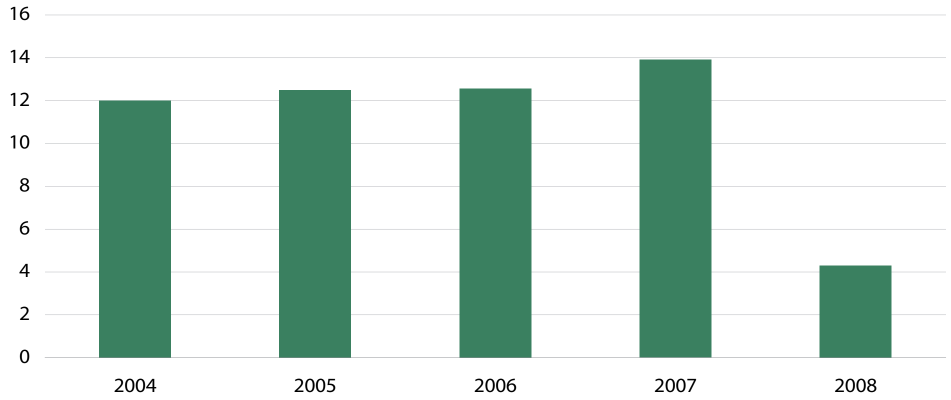
4.6 Hedge funds (*fondos de inversion libre*) and Funds of Hedge Funds

In this case, the Circular lays down the following obligations:

- The alternative management strategies used must be detailed, whether by the investor CIU or by the underlying.
- The policy of investment in liquid assets and management of liquidity to meet repayments must be reported.
- With respect to the returns graph, solely the absolute return to be achieved need be included[3].

3 A reference index is not included because Hedge Funds do not have an index as an objective, but to obtain absolute returns independently of evolution of the market.

Example of graph of return of a Hedge Fund or Fund of Hedge Fund FIGURE 4



Source: own preparation.

5 Position statement

The Depository Order of March 2008 (in Section 10) authorises the CNMV to implement the contents of the position statement and establish a model form. For its part, Section 4.3 of the CIU Regulations provides that CIU Management Companies or depositories must send a position statement to holders with a regularity of at least monthly. If movements have not occurred in the period the obligation is shifted to the following period. In any event, it will be mandatory to send it at least once per year. It provides that it will be the CIU Management Company or depository, when the latter is commercialiser, which are under an obligation to send the position statement.

Annex 8 of Circular 4/2008 provides for three sections and one warning. The first section relates to transactions carried out in the month of the position statement. This first section must report on the number of shares or units subscribed for or repaid, the gross and net amount of the transaction and the subscription or repayment commissions which have arisen, as the case may be.

The second section relates to the global position of the unit-shareholder. It must report on the number of units or shares and amount subscribed of each position maintained, as well as the liquidating and cash value maintained at the reference date.

When all or part of the management commission is calculated on the basis of results through a system of individual charge, it must include the following wording: "The liquidating value of the fund, and therefore its return, does not incorporate the effect of the individual charge to the holder of the management commission on results"[4]. The warning which must be contained in the position statement relates to the fact that calculation of average return does not take account of subscription or repayment commissions.

A further two novelties of the Circular are the obligation to report the return of the final position of the holder and average period of the final position in each CIU, which must be included in the position statement. The previous legislation required

4 Information obligation established by Section 5 of the CIU Regulations.

that the investor be informed of the value of his final position and in this new Circular the investor must be informed not only of his final position but of the return which he has obtained in a particular period.

Further information novelties can finally be highlighted which must be included in the position statement: (1) it report on whether the transaction derives from a transfer or is set in a periodic subscription programme, (2) on the monetary gain, and (3) on the date of request for the transaction in the case of CIUs which do not publish daily liquidating value.

6 Conclusions

The Circular repeals the previous legislation on quarterly reports, ending a legislative fragmentation which has existed up to now. The models set out in the different annexes of the Circular are classified taking into account the new categories of CIU introduced by the CIU Regulations.

Approval of the Circular has implemented a standardised model of position statement. This will report to investors not only on their final position but on the return obtained in a particular period.

Entry into force of the Circular will mean that the information received by unit holders and shareholders is more structured, simplified, standardised and comprehensible.

The reports incorporated by the new Circular 4/2008, as a result of the new manner of structuring them and the Circular detailing the manner of completion, will make them more comparable and uniform. Sending reports to the CNMV in XBRL language will without doubt contribute to this objective of comparability and uniformity.

This will all mean greater transparency in processing and dissemination of information which is sent to unit holders and shareholders.

7 Bibliography

Jimeno Moreno, J. P. (2004): *Los mercados financieros y sus matemáticas*. Options & Futures Institute. Madrid.

Jorion P. (2001): *Value At Risk*. Mc Graw Hill. New York.

IV Legislative annex

The new legislation of national scope promulgated since publication of the CNMV bulletin for the third quarter of 2008 is as follows, in chronological order:

- Royal Decree 1642/2008, of 10 October, establishing the amounts guaranteed referred to by Royal Decree 2606/1996, of 20 December, on the Credit Institutions Deposit Guarantee Fund, and Royal Decree 948/2001, of 3 August, on investor indemnity systems.

  The European Union Economic and Financial Affairs Council of 7 October of 2008 resolved to raise the minimum coverage threshold of deposit guarantee systems to 50,000 euros per holder and institution. On these lines this Royal Decree increases to 100,000 euros per holder and institution the protection of the Credit Institutions Deposit Guarantee Fund established by Royal Decree 2606/1996, of 20 December, and of the Investment Guarantee Fund established by Royal Decree 948/2001, of 3 August, for securities dealers and brokers.

- Royal Decree-Act 6/2008, of 10 October, creating the Fund for the Acquisition of Financial Assets.

  In order to promote the financing of undertakings and citizens by financial institutions, this Royal Decree-Act creates the Fund for the Acquisition of Financial Assets (*Fondo para la Adquisición de Activos Financieros* – FAAF), attached to the Ministry of Economy and Finance which manages and directs it through a Governing Board and an Executive Committee, subject to control by Parliament and the Comptroller-General of the State Administration.

  The FAAF, with provision charged to General State Budgets in the amount of 30,000 million euros, which can be extended to 50,000 million euros, will invest in financial instruments issued by credit institutions and securitization funds, backed by credits granted to individuals, undertakings and non-financial entities. The financial instruments in which the Fund for the Acquisition of Financial Assets will invest will be of maximum quality and be determined based on the principles of objectivity, transparency, efficiency, return and diversification.

- Royal Decree-Act 7/2008, of 13 October, on Urgent Measures in the Financial-Economic Field in relation to the Concerted Action Plan of Euro Zone Countries.

  In coordination with other Euro Zone States, this Royal Decree-Act authorises two types of measure: the grant of State guarantees for new financing operations by credit institutions, and the State acquisition of securities suitable for strengthening the own funds of credit institutions.

  With respect to the grant of guarantees, and without prejudice to subsequent issue of a Ministerial Order implementing this Royal Decree-Act, a maximum amount is established of 100,000 million euros for the grant of State guarantees for issues of notes, bonds and debentures admitted to trading on Spanish official secondary markets made by credit institutions resident in Spain and the subsidiaries of foreign institutions if they engage in significant activity in Spain. It is provided that the guarantee may be extended to other bank instruments such as interbank deposits.

With respect to the State acquisition of securities to strengthen the own funds of credit institutions, this measure, which is described as exceptional, will be adopted at the request of the institution on prior report from the Bank of Spain, and without application of the restrictions established by the Act for the computability of own funds.

- Order EHA/3064/2008, of 28 October, modifying the Order of the Ministry of Economy and Finance of 26 July of 1989, in implementation of Section 86 of the Securities Market Act (*Ley del Mercado de Valores*), and the Order of the Ministry of Economy and Finance of 24 September of 1993, on real estate investment companies and funds, in order to authorise the Spanish National Securities Market Commission (*Comisión Nacional del Mercado de Valores*) to implement certain aspects in the accounting field of undertakings supervised and of the calculation of coefficients and limits of collective investment undertakings.

  This Order regulates two distinct aspects of the securities market legislation. It firstly modifies the Order of the Ministry of Economy and Finance of 26 July of 1989, in implementation of Section 86 of the Securities Market Act in order to extend the authorisation for the CNMV to implement accounting rules for all undertakings referred to by Section 84.1 of the Securities Market Act: governing companies of official secondary markets, Systems Company, central counterparty entities, Stock Exchanges Company, investment services firms and their agents, management company of the Investment Guarantee Fund and members of official secondary markets or the body which clears and settles their transactions.

  It furthermore modifies the Order of the Ministry of Economy and Finance of 24 September of 1993, on real estate investment companies and funds, authorising the CNMV to specify certain aspects of accounting and calculation of coefficients and limits related to this type of collective investment undertaking.

- Order EHA/3118/2008, of 31 October, in implementation of Royal Decree-Act 6/2008, of 10 October, creating the Fund for the Acquisition of Financial Assets.

  This Order implements various aspects relating to the organisation and functioning of the Fund for the Acquisition of Financial Assets (FAAF). It provides that auctions shall be the procedure used for selecting the assets which are to be acquired by the FAAF. It also determines the bids which may be made by credit institutions and securitization funds, which may be competitive —in which the institutions indicate the interest rates at which they are prepared to offer the assets— or non-competitive —awarded at the minimum interest rate accepted in the auction—. Furthermore, an obligation is established to give publicity to resolutions of the Governing Board of the FAAF and a duty to publish in the Official State Gazette, amongst others, resolutions regarding the investment directives of the Fund. The Order finally creates a technical committee to advise the FAAF, with participation by specialists from different institutions.

- Circular 5/2008, of 5 November, of the CNMV, on statistical information requirements regarding assets and liabilities of European Union collective investment undertakings, published in the Official State Gazette of 19 November of 2008.

CNMV Circular 2/1998, of 27 July, and its subsequent modifications, established the requirements for statistical information which monetary CIUs had to send to the CNMV in order that this information could be used by the ECB to monitor monetary policy within the Economic and Monetary Union. Regulation (EC) no. 958/2007 of the ECB extends the requirement periodically to send statistical information to CIUs which were not under an obligation pursuant to CNMV Circular 1/2007.

This Circular is applicable to all compartments, or CIUs in the event that they lack compartments, which are registered in the CNMV Registry, whose information policy or vocation is not monetary, nor whose investment policy or vocation is that of investing in monetary CIUs or compartments, nor in those included in the list of MFI published by the ECB. The information relates to balances of securities in portfolio and transactions, value by value (with breakdown of their portfolio by individualised securities) and with monthly regularity in general, although the possibility is allowed of quarterly sending for those undertakings which constitute a small percentage of the sector.

- Order EHA/3291/2008, of 7 November, establishing the procedure for communication by depository financial institutions of abandoned personal property and balances.

  Section 18 of Act 33/2003, of 3 November, on the Assets of Public Administrations, accords ownership to the General State Administration of securities, money and other personal property deposited in financial institutions and in respect of which no steps have been taken by those concerned which imply exercise of their right of ownership within a period of twenty years. This Order, which is not applicable to the Caja General de Depósitos, regulates the obligations in this respect of Spanish financial institutions and the branches in Spain of financial institutions of other European Union Member States. In this respect, the following obligations could be highlighted: the content is established of communications regarding abandoned balances which must be sent to the Ministry of Economy and Finance in the first quarter of each year, an obligation is established for financial institutions to contact the customer at the last known address three months before the prescription period of twenty years referred to elapses, and finally the right of individuals is established to obtain certification from financial institutions of handover of the property to the General State Administration.

- Order EHA/3364/2008, of 21 November, in implementation of Section 1 of Royal Decree-Act 7/2008, of 13 October, on Urgent Measures in the Economic-Financial Field in relation to the Concerted Action Plan of Euro Zone Countries.

  This Order, pursuant to Royal Decree-Act 7/2008, of 13 October, regulates various matters relating to the grant of State guarantees for new financing operations carried out by credit institutions resident in Spain.

  It can firstly be highlighted that the characteristics are specified of these guarantees in relation to the regulation contained in the Royal Decree-Act: they are granted with waiver of the benefit of requiring that remedies be exhausted against principal debtor, they are deemed granted on an irrevocable and unconditional basis, and do not cover the exchange rate risk in foreign currency issues, which in any event will be for account of the issuer.

Secondly, the characteristics are also laid down of the operations which may be guaranteed by this type of guarantee: they will be issues of notes, bonds or debentures, not subordinated or guaranteed, with a maturity period of between three months and three years, with redemption by a single payment and without incorporating options or other derivative instruments or any element which makes risk assessment difficult, and with a minimum amount in each issue of not less than 10 million euros.

Thirdly, the procedure is regulated for applying for guarantees, and it can be emphasised that guarantees are granted to each credit institution in proportion to its participation in credit to other resident sectors; it finally provides that the Directorate General for the Treasury and Financial Policy must notify the Bank of Spain, as the case may be, of enforcement of guarantees granted, and the amounts are fixed of commissions which are accrued by the guarantees granted in favour of the State.

- Order EHA/3465/2008, of 26 November, modifying Order EHA/2688/2006, of 28 July, on collaboration agreements in relation to Funds for Investment in State Debt.

  This Ministerial Order modifies various aspects of Order EHA/2688/2006, of 28 July, on collaboration agreements in relation to Funds for Investment in State Debt in order that funds for investment in State Debt (Fondtesoro) can, for the purpose of complying with the investment coefficients, treat the bonds issued by the "FTPymes" guaranteed by the State as State Debt.

- Circular 6/2008, of 26 November, of the CNMV, on determination of liquidating value and operational aspects of collective investment undertakings.

  The Circular on the liquidating value of CIUs establishes the rules applicable in calculation of this figure, which represents the price of units or shares into which the net assets of a CIU is divided. For these purposes the Circular determines the net assets of the CIU on the basis of accounting figures, in order to then calculate its liquidating value, with special attention to cases in which there are compartments and classes of units or series of shares within the CIU. The Circular further regulates a series of operational aspects of CIUs, such as rules relating to attributing management commission on results, legal coefficients and operating parameters of CIUs which replicate or reproduce indices and CIUs which take an index as reference.

- Circular 7/2008, of 26 November, of the CNMV, on accounting rules, annual accounts and reserved information statements of investment services firms, collective investment undertaking management companies and risk capital undertaking management companies.

  The Circular modifies the accounting system of investment services firms (ESI), of collective investment undertaking management companies (SGIIC) and of risk capital undertaking management companies (SGECR), in order to adapt it to the new accounting framework established in the Spanish General Accounting

Scheme (*Plan General de Contabilidad*) promulgated by Royal Decree 1514/2007, of 16 November, taking into account the particular legal and operational nature of such undertakings. However, in certain aspects it has been necessary and desirable to maintain criteria and approaches contained in the previous legislation, such as the consolidation obligation of horizontal groups.

One novelty introduced by the Circular is extension of the definition of reasonable value to financial instruments with no market or with a market with little activity, in order to promote the use of reasonable value when it facilitates correct risk management. The definitions are also extended of other novel concepts such as "effective interest rate", or "deterioration". The Circular further establishes rigid conditions for reclassification of assets between the different defined categories. Very strict criteria are established for removal of financial assets and accounting for gains as adjustments to net worth as a result of valuation of financial assets available for sale and their definition is clarified in the solvency field. The Circular also incorporates a specific rule on income from provision of services and, as the case may be, financial expenses and trading losses, which includes principles for attributing them to profit and loss account.

The Circular also shows a model balance sheet which classifies financial assets in accordance with their nature based on valuation principles. Finally, it is essential to highlight the importance of the transparency required of managers of supervised undertakings which are responsible for accounting policy, explaining it, disclosing it to the market and complementing it with specific information. In this respect, the contents of the notes to the accounts and management report include a description of the financial risks assumed and their management and hedging policies.

- Circular 8/2008, of 10 December, of the CNMV, approving the models to which announcements and applications for authorisation of public takeover bids must conform.

  In implementation of Royal Decree 1066/2007, of 27 July, on the system of public takeover bids (OPAs), the model announcement of public offer for acquisition of securities of listed companies is established, in order to ensure that from the outset all investors can ascertain the necessary information in order to adequately assess the operation in question. The basic principle is established that the announcement must be truthful, clear, complete and, when the information so requires, quantified. An option was made to include a single model announcement for all types of takeover bid, and also taking in the possibility that instead of making the takeover bid announcement the bidder can directly submit the written application for authorisation for the bid, which will have to contain virtually the same information as the Circular lays down for announcement of the bid.

  The Circular firstly establishes that the announcement must warn that the bid is subject to the requisite authorisation by the CNMV. The Circular secondly fixes the content of the announcement: the bidder must be identified as well as the person or body which has adopted the resolution to formulate the bid, the approximate forecast period must be established for submission of the application for authorisation of the bid and the type of bid, the holding of the bidder in the company concerned must be reported, and the characteristics of the company affected by the bid, the number of securities and percentage to which the bid will extend, the nature of the consideration offered indicating, as the case may be, whether securities are offered in exchange and providing certain information regarding them. It must also report on the conditions to which the bid is subject, the need to obtain any administrative authorisation, the existence of agreements with other shareholders of the company concerned, with its board of directors or any of its members, the intention of the bidder regarding exclusion of the securities of the company concerned from the stock exchange and regarding the exercise of right of compulsory sale. All this information must be adapted as appropriate in the case of competing bids, bids for exclusion or as a result of reduction in capital by acquisition of own shares. Finally, the announcement must contain a warning regarding the obligations to notify major holdings and transactions in shares which are applicable in the case of takeover bids, and must further warn of suspension of the liquidity agreement of the company concerned if there is one.

- Circular 9/2008, of 10 December, of the CNMV, on accounting rules, reserved and public information statements, and annual accounts of governing companies of official secondary markets, excluding the Bank of Spain, of governing bodies of multilateral trading systems, of the Systems Company, of central counterparty entities, of the Stock Exchanges Company, of companies which own all shares of governing bodies of official secondary markets and of multilateral trading systems, and of other clearing and settlement systems of markets which are created pursuant to the provisions of the Securities Market Act.

  This Circular, of accounting scope, extends to all resident trading and post-trading securities market infrastructures, except for the Book Entry Public Debt Market (*Mercado de Deuda Pública en Anotaciones*). It aims to update the rules and models for reserved and public financial statements in force up to now in order to adapt them to legislative changes in the accounting field which have taken place in Spain in the last year in order to bring about international harmonisation based on European Union legislation, and specifically the accounting framework represented by the new Spanish General Accounting Scheme (*Plan General de Contabilidad* – PGC).

  This legislative adaption in the accounting field has been undertaken taking account of the legal and operational idiosyncrasies of the different resident trading and post-trading market infrastructures, bearing in mind the accounting principles and standards contained in the new PGC. This Circular does not consequently contain accounting legislation developments in relation to the treatment of transactions and events laid down by the new PGC, but solely the accounting treatment which these market infrastructures must apply to those transactions and events which, as a result of their specific nature, are not covered by the corresponding regulatory implementations of commercial legislation.

  In short, this Circular, applicable to periodic public and reserved monthly, quarterly and annual information which is prepared as from 1 January 2009 and to the information on annual closing of the 2008 financial year of companies or entities within its scope, aims to make uniform and adapt the accounting and activity information which these companies must send to the Spanish National

Securities Market Commission (CNMV) or must make public, to the accounting principles and criteria in force at the present time.

- Royal Decree-Act 10/2008, of 12 December, adopting financial measures to improve the liquidity of small and medium-sized enterprises and other complementary economic measures.

  In the light of the circumstances of credit restriction and financial crisis, several measures are adopted by means of this Royal Decree-Act. The important modifications must be highlighted to business legislation which are introduced in its Sole Additional Provision and Final Provision One. It firstly establishes, for a period of two financial years from entry into force of the legislation, that losses as a result of deterioration of tangible fixed assets, of real estate investments and of inventories will not be computed for determination of cases of mandatory reduction in capital under the Companies Act (*Ley de Sociedades Anónimas*) nor for determination of the grounds for dissolution of the company laid down by the Companies Act and the Limited Liability Companies Act. It secondly amends Section 36 of the Commercial Code in order that variations in the value of instruments used in cash flow coverage operations are not taken into account in the calculation of net worth, such that they do not affect the distribution of profits or grounds for mandatory reduction in capital or dissolution of the company.

  Furthermore, this Royal Decree-Act provides a mediation line for the *Instituto de Crédito Oficial* in the amount of five thousand million euros in order to meet the working capital financing requirements of small and medium-sized enterprises which, being solvent and viable, are subject to a temporary situation of credit restriction.

- Order EHA/3748/2008, of 23 December, amending Order EHA/3364/2008, of 21 November, implementing Section 1 of Royal Decree-Act 7/2008, of 13 October, on Urgent Measures in the Economic-Financial Field in relation to the Concerted Action Plan of Euro Zone Countries.

  This Ministerial Order modifies various aspects of Order EHA/3364/2008, of 21 November, relating to the grant of State guarantees for new issues of notes, bonds and debentures made by credit institutions. The Order firstly provides that the State guarantee may cover the exchange rate risk in the case of issues made in foreign currencies. Secondly, the previous Order is corrected to the effect that obtaining the State guarantee is not conditional on the credit institutions having previously made issues in Spain, it being sufficient that the credit institution has its registered office in Spain. Thirdly, it extends the period, until 15 December of 2009, granted to credit institutions to make issues guaranteed by the State.

  This Ministerial Order finally, by means of an additional provision, modifies various aspects of Order EHA/3118/2008, of 31 October, in implementation of Royal Decree-Act 6/2008, of 10 October, by which the Fund for the Acquisition of Financial Assets (FAAF) is created. In particular, it permits registration, clearing and settlement services of regional scope to take part in the settlement of acquisition operations by the FAAF of securities admitted to trading on a single Securities Exchange.

- Circular 10/2008, of 30 December, of the CNMV, on financial advisory firms.

  This Circular regulates various aspects relating to the organisational requirements of financial advisory firms (*empresas de asesoramiento financiero* – EAFI) and the documentation which must be provided to the CNMV for authorisation and registration as an EAFI; it also systematises the legislation on EAFIs contained in the Securities Market Act and in Royal Decree 217/2008, on investment services firms and other entities which provide investment services.

  The more novel matters firstly include a provision that formation and registration of an EAFI will not be necessary for the provision of advice carried out in the scope of another professional activity not regulated by the Securities Market Act, provided that provision of this advice is not specifically remunerated, nor for the provision of advisory services in an ancillary manner in the framework of a professional activity, provided that the latter is regulated by laws or regulations or by a professional code which does not exclude provision of this service.

  With respect to application for authorisation of EAFIs, it provides that in the event that the EAFI elects for a combination of the two financial requirements laid down by the Royal Decree (capital plus civil liability insurance) submission of a report will be required from an independent expert indicating compliance with the financial requirements. With respect to the knowledge and experience required of directors and general managers of EAFIs and of EAFIs themselves who are individuals, it details that the experience must relate to advisory functions in the investment field or others related to the securities market, and that for the purpose of assessing knowledge the possession of qualifications and certificates evidencing knowledge of these matters may be taken into account.

- Circular 11/2008, of 30 December, of the CNMV, on accounting standards, annual accounts and reserved information statements of risk capital undertakings.

  The accounting Circular on risk capital undertakings has the purpose of adapting these undertakings to the new Spanish General Accounting Scheme (*Plan General de Contabilidad*), and further introducing specific accounting rules which take into account the nature of these undertakings. In this adaptation the different classifications of financial assets are taken into account which will apply to these undertakings and principles introduced for determining reasonable value, in particular with respect to securities not listed on organised secondary markets, which will constitute typical risk capital investments. Rules are further introduced regarding the structure and content of the annual accounts and reserved statements of risk capital undertakings.

- Circular 12/2008, of 30 December, of the CNMV, on solvency of investment services firms and their groups subject to consolidation.

  The Circular seeks to adapt the regulatory framework of solvency of financial undertakings in the European Union to Spanish investment services firms and their consolidation groups. The new Capital Accord of the Committee on Banking Supervision of the Bank for International Settlements is set out in

Community Directives 2006/49/EC of the European Parliament and Council, of 14 June of 2006, on adaption of the capital adequacy of investment firms and credit institutions (consolidation), and 2006/48/EC of the European Parliament and Council, of 14 June of 2006, relating to the taking up and pursuit of the business of credit institutions.

With the two-fold purpose of firstly avoiding regulatory arbitrage, and secondly facilitating integration of the different types of undertakings in consolidation groups subject to supervision, it establishes a parallel between the rules regulating the solvency of credit institutions and those contained in this text. Provisions have nevertheless been incorporated for the specific features inherent in investment services firms.

Special mention should be made of the use of model forms in this Circular for sending information common with those for credit institutions, which will facilitate the gathering and dissemination of information, not only by national supervisors but also by all European solvency supervisors, for the first time making a comparison possible of data on financial institutions at European scale.

V Statistics annex

1 Markets

1.1 Equity

Share issues and public offerings[1]

TABLE 1.1

	2005	2006	2007	2007 IV	2008 I	II	III	IV[2]
CASH VALUE[3] (Million euro)	2,960.5	5,021.7	23,757.9	7,398.7	9.5	356.6	40.8	7,397.1
Capital increases	2,803.4	2,562.9	21,689.5	6,823.1	0.0	356.6	40.8	7,397.1
Of which, primary offerings	0.0	644.9	8,502.7	4,683.3	0.0	292.0	0.0	0.0
With Spanish tranche	0.0	303.0	4,821.4	2,037.6	0.0	292.0	0.0	0.0
With international tranche	0.0	342.0	3,681.4	2,645.8	0.0	0.0	0.0	0.0
Secondary offerings	157.1	2,458.8	2,068.5	575.6	9.5	0.0	0.0	0.0
With Spanish tranche	54.7	1,568.1	1,517.1	432.4	9.5	0.0	0.0	0.0
With international tranche	102.5	890.7	551.4	143.3	0.0	0.0	0.0	0.0
NO. OF FILES[4]	27	30	35	12	1	4	2	3
Capital increases	25	21	26	7	0	4	2	3
Of which, primary offerings	0	8	8	4	0	2	0	0
Of which, bonus issues	6	0	0	0	0	0	0	0
Secondary offerings	2	14	12	7	1	1	0	0
NO. OF ISSUERS[4]	24	23	29	10	1	4	2	3
Capital increases	23	18	24	7	0	4	2	3
Of which, primary offerings	0	6	6	4	0	2	0	0
Secondary offerings	1	10	8	5	1	1	0	0

1 Total files registered with the CNMV (including supplements of initial files).
2 Available data: November 2008.
3 Does not include registered amounts that were not carried out.
4 Includes all registered offerings, including the issues that were not carried out.

Primary and secondary offerings. By type of subscriber

TABLE 1.2

Million euro	2005	2006	2007	2007 IV	2008 I	II	III	IV[1]
PRIMARY OFFERINGS	0.0	644.9	8,502.7	4,683.3	0.0	292.0	0.0	0.0
Spanish tranche	0.0	303.0	4,646.2	2,035.0	0.0	282.0	0.0	0.0
Private subscribers	0.0	8.7	2,841.0	830.5	0.0	191.5	0.0	0.0
Institutional subscribers	0.0	294.3	1,805.2	1,204.5	0.0	90.5	0.0	0.0
International tranche	0.0	342.0	3,681.4	2,645.8	0.0	0.0	0.0	0.0
Employees	0.0	0.0	175.2	2.6	0.0	10.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
SECONDARY OFFERINGS	157.1	2,458.8	2,068.5	575.6	9.5	0.0	0.0	0.0
Spanish tranche	54.7	1,565.0	1,505.7	430.8	9.5	0.0	0.0	0.0
Private subscribers	27.3	390.0	393.9	88.4	0.0	0.0	0.0	0.0
Institutional subscribers	27.3	1,175.0	1,111.8	342.4	9.5	0.0	0.0	0.0
International tranche	102.5	890.7	551.4	143.3	0.0	0.0	0.0	0.0
Employees	0.0	3.1	11.4	1.6	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

1 Available data: November 2008.

Admission to listing. Files registered at the CNMV

TABLE 1.3

	2005	2006	2007	2007 IV	2008 I	II	III	IV[1]
NOMINAL VALUE (Million euro)								
With issuance prospectus	498.0	963.4	5,894.3	5,562.1	13.3	25.5	127.4	8.4
Capital increases	494.0	575.9	5,687.2	5,439.6	13.3	25.5	127.4	8.4
Of which, primary offerings	0.0	145.3	5,424.4	5,419.8	0.0	0.0	100.0	0.0
Secondary offerings	4.0	387.5	207.1	122.5	0.0	0.0	0.0	0.0
Without issuance prospectus	167.3	564.7	8,366.1	6,438.4	274.7	448.1	223.3	107.3
NO. OF FILES								
With issuance prospectus	26	18	22	8	2	1	4	1
Capital increases	25	13	18	6	2	1	4	1
Of which, primary offerings	0	5	6	4	0	0	1	0
Secondary offerings	1	9	7	4	0	0	0	0
Without issuance prospectus	27	61	72	16	9	12	7	9

1 Available data: November 2008.

Companies listed[1]

TABLE 1.4

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[2]
Total electronic market[3]	126	135	143	143	141	139	140	140
Of which, without Nuevo Mercado	115	124	142	142	141	139	140	140
Of which, Nuevo Mercado	11	11	1	1	0	0	0	0
Of which, foreign companies	5	6	5	5	5	5	5	5
Second Market	14	12	11	11	10	9	8	8
Madrid	2	2	2	2	2	2	2	2
Barcelona	10	9	9	9	8	7	6	6
Bilbao	0	0	0	0	0	0	0	0
Valencia	2	1	0	0	0	0	0	0
Open outcry ex SICAV	47	38	31	31	29	29	29	29
Madrid	22	16	13	13	13	13	13	13
Barcelona	28	24	20	20	19	19	19	19
Bilbao	14	10	9	9	8	8	8	8
Valencia	18	13	9	9	7	7	7	7
Open outcry SICAV	3,111	744	8	8	5	4	4	3
MAB[4]	-	2,405	3,287	3,287	3,322	3,362	3,364	3,354
Latibex	32	34	34	34	34	35	35	35

1 Data at the end of period.
2 Available data: November 2008.
3 Without ETF (Exchange Traded Funds).
4 Alternative Stock Market.

Capitalisation[1]

TABLE 1.5

				2007	2008			
Million euro	2005	2006	2007	IV	I	II	III	IV[2]
Total electronic market[3]	616,659.5	813,765.1	892,053.8	892,053.8	780,720.1	739,386.7	634,275.0	508,109.2
Of which, without Nuevo Mercado	607,167.8	800,148.0	891,875.7	891,875.7	780,720.1	739,386.7	634,275.0	508,109.2
Of which, Nuevo Mercado	9,491.8	13,617.1	178.1	178.1	0.0	0.0	0.0	0.0
Of which, foreign companies[4]	64,312.7	105,600.9	134,768.6	134,768.6	120,418.7	133,614.0	94,553.7	61,694.9
Ibex 35	411,712.5	512,828.0	524,651.0	524,651.0	455,694.3	412,258.4	374,922.1	312,794.3
Second Market	444.2	392.7	286.8	286.8	217.1	167.1	112.5	110.3
Madrid	9.2	18.9	27.8	27.8	23.2	25.9	24.1	23.0
Barcelona	291.2	184.2	259.0	259.0	193.9	141.1	88.3	87.3
Bilbao	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valencia	143.8	189.6	0.0	0.0	0.0	0.0	0.0	0.0
Open outcry ex SICAV	6,874.8	7,905.3	7,444.9	7,444.9	7,228.8	6,672.3	5,850.5	5,430.3
Madrid	3,486.7	2,698.1	1,840.6	1,840.6	1,810.9	1,562.0	1,475.4	1,472.4
Barcelona	3,129.2	4,966.3	4,627.8	4,627.8	4,963.8	4,698.4	3,966.4	3,642.5
Bilbao	405.9	59.5	108.2	108.2	107.3	27.0	27.0	44.2
Valencia	836.1	741.9	1,206.5	1,206.5	994.2	971.7	885.3	763.5
Open outcry SICAV	33,171.1	9,284.1	245.4	245.4	200.2	184.2	175.2	154.1
MAB[5]	0.0	29,866.3	41,659.8	41,659.8	39,298.0	39,001.1	37,788.9	35,721.7
Latibex	216,111.3	271,641.8	427,773.6	427,773.6	389,629.9	712,179.3	529,494.2	430,465.9

1 Data at the end of period.
2 Available data: November 2008.
3 Without ETF (Exchange Traded Funds).
4 Foreign companies capitalisation includes their entire shares, whether they are deposited in Spain or not.
5 Alternative Stock Market.

Trading

TABLE 1.6

				2007	2008			
Million euro	2005	2006	2007	IV	I	II	III	IV[1]
Total electronic market[2]	847,652.2	1,144,562.9	1,653,354.8	430,021.7	377,897.7	315,693.7	285,162.3	189,409.2
Of which, without Nuevo Mercado	818,653.2	1,118,546.1	1,627,369.5	425,558.0	377,886.2	315,693.7	285,162.3	189,409.2
Of which, Nuevo Mercado	28,999.0	26,016.8	25,985.3	4,463.7	11.4	0.0	0.0	0.0
Of which, foreign companies	15,115.1	11,550.3	7,499.3	1,018.2	552.1	382.4	206.9	184.9
Second Market	25.9	49.3	192.9	11.8	3.2	17.5	9.7	0.3
Madrid	1.8	7.2	8.9	0.8	0.5	1.7	0.1	0.2
Barcelona	22.9	41.6	182.3	11.0	2.7	15.9	9.6	0.1
Bilbao	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valencia	1.3	0.5	1.7	0.0	0.0	0.0	0.0	0.0
Open outcry ex SICAV	887.1	737.6	792.7	258.6	38.5	22.5	58.1	7.4
Madrid	198.2	257.9	236.1	92.7	17.5	7.2	45.6	2.4
Barcelona	667.0	297.8	402.8	29.1	17.6	14.7	12.2	4.8
Bilbao	13.4	159.9	0.1	0.0	0.0	0.0	0.0	0.1
Valencia	8.4	22.0	153.8	136.7	3.3	0.6	0.4	0.1
Open outcry SICAV	5,022.8	4,580.6	361.6	15.2	5.9	2.7	7.2	7.0
MAB[3]	0.0	1,814.2	6,985.2	2,240.4	1,966.1	1,646.1	1,406.3	1,557.9
Latibex	556.7	723.3	868.2	215.6	305.9	199.3	136.2	77.3

1 Available data: November 2008.
2 Without ETF (Exchange Traded Funds).
3 Alternative Stock Market.

Trading on the electronic market by type of transaction[1]

TABLE 1.7

Million euro	2005	2006	2007	2007 IV	2008 I	II	III	IV[2]
Regular trading	798,934.5	1,080,117.5	1,577,249.5	389,841.9	354,712.5	304,979.6	279,188.2	186,070.3
Orders	488,416.3	658,839.2	985,087.6	246,015.5	245,239.9	185,997.3	183,639.9	125,003.7
Put-throughs	82,403.1	105,910.7	155,085.1	38,761.4	34,574.7	29,644.2	22,654.9	14,359.6
Block trades	228,115.1	315,367.7	437,076.8	105,064.9	74,898.0	89,338.1	72,893.4	46,707.0
Off-hours	27,863.0	11,651.6	18,301.5	5,902.5	4,260.1	2,425.3	1,341.7	1,178.9
Authorised trades	4,773.4	4,052.0	4,189.6	640.3	374.6	533.1	974.9	933.5
Art. 36.1 SML trades	1.3	6,439.7	0.0	0.0	0.0	0.0	0.0	0.0
Tender offers	6,682.8	18,094.6	26,284.3	20,079.8	14,049.1	3,412.1	0.0	0.0
Public offerings for sale	226.3	3,264.0	11,177.4	9,237.9	0.0	0.0	292.0	0.0
Declared trades	2,298.9	10,347.9	2,954.4	233.6	836.3	20.2	33.0	24.0
Options	5,268.0	8,279.8	10,240.4	3,227.0	2,450.3	2,579.7	1,693.1	519.5
Hedge transactions	1,615.4	2,315.7	2,957.8	858.8	1,214.7	1,743.7	1,639.5	683.1

1 Without ETF (Exchange Traded Funds).
2 Available data: November 2008. ye ETF (Exchange Traded Funds).

Margin trading for sales and securities lending

TABLE 1.8

Million euro	2005	2006	2007	2007 IV	2008 I	II	III	IV[1]
TRADING								
Securities lending[2]	393,964.1	550,850.4	835,326.9	213,637.3	159,984.9	175,820.7	138,864.1	85,153.5
Margin trading for sales of securities[3]	152.2	379.9	555.4	136.3	189.5	135.2	149.4	107.4
Margin trading for securities purchases[3]	465.0	511.9	411.3	84.5	52.7	35.1	33.6	25.4
OUTSTANDING BALANCE								
Securities lending[2]	66,737.5	62,058.2	79,532.9	79,532.9	69,068.6	66,326.8	58,394.2	45,708.3
Margin trading for sales of securities[3]	28.5	73.6	112.4	112.4	97.8	57.8	62.3	28.9
Margin trading for securities purchases[3]	52.3	70.1	59.4	59.4	30.7	28.2	31.2	8.2

1 Available data: November 2008.
2 Regulated by Article 36.7 of the Securities Market Law and Order ECO/764/2004.
3 Transactions performed in accordance with Ministerial Order dated 25 March 1991 on the margin system in spot transactions.

1.2 Fixed income

Gross issues registered[1] at the CNMV

TABLE 1.9

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[2]
NO. OF ISSUERS	155	159	173	75	59	65	48	45
Mortgage covered bonds	9	11	10	4	7	13	5	4
Territorial covered bonds	2	5	4	1	7	0	0	1
Non-convertible bonds and debentures	49	46	41	3	5	13	16	7
Convertible bonds and debentures	4	1	0	0	0	0	0	0
Backed securities	53	61	77	34	16	26	18	17
Commercial paper	68	68	80	35	26	21	11	20
Of which, asset-backed	3	3	3	0	0	1	0	1
Of which, non-asset-backed	65	65	77	35	26	20	11	19
Other fixed-income issues	1	0	2	0	0	0	0	0
Preference shares	6	9	5	0	4	1	2	0
NO. OF ISSUES	263	335	334	84	74	94	62	62
Mortgage covered bonds	21	37	32	5	11	20	8	7
Territorial covered bonds	3	6	8	1	7	0	0	1
Non-convertible bonds and debentures	93	115	79	3	7	22	18	16
Convertible bonds and debentures	4	1	0	0	0	0	0	0
Backed securities	54	82	101	40	18	30	23	18
Commercial paper	80	83	106	35	27	21	11	20
Of which, asset-backed	3	3	3	0	0	1	0	1
Of which, non-asset-backed	77	80	103	35	27	20	11	19
Other fixed-income issues	1	0	3	0	0	0	0	0
Preference shares	7	11	5	0	4	1	2	0
NOMINAL AMOUNT (Million euro)	414,253.9	523,131.4	648,757.0	154,568.4	117,526.8	134,468.4	90,553.9	84,619.1
Mortgage covered bonds	35,560.0	44,250.0	24,695.5	2,525.0	1,250.0	10,120.0	1,685.0	945.0
Territorial covered bonds	1,775.0	5,150.0	5,060.0	110.0	1,020.0	0.0	0.0	800.0
Non-convertible bonds and debentures	41,907.1	46,687.5	27,416.0	257.0	604.1	3,743.6	4,215.1	1,239.3
Convertible bonds and debentures	162.8	68.1	0.0	0.0	0.0	0.0	0.0	0.0
Backed securities	69,044.3	91,607.7	141,627.0	52,819.0	28,657.0	34,386.4	11,736.1	39,617.3
Spanish tranche	28,746.5	30,885.7	94,049.0	51,309.0	28,657.0	32,993.2	10,606.9	39,617.3
International tranche	40,297.8	60,722.1	47,578.0	1,510.0	0.0	1,393.2	1,129.2	0.0
Commercial paper[3]	264,359.5	334,457.0	442,433.5	98,857.4	85,899.6	86,118.5	72,867.7	42,017.5
Of which, asset-backed	2,767.5	1,992.7	464.8	85.0	133.0	48.0	94.0	43.0
Of which, non-asset-backed	261,592.0	332,464.3	441,968.7	98,772.4	85,766.6	86,070.5	72,773.7	41,974.5
Other fixed-income issues	89.3	0.0	7,300.0	0.0	0.0	0.0	0.0	0.0
Preference shares	1,356.0	911.0	225.0	0.0	96.0	100.0	50.0	0.0
Pro memoria:								
Subordinated issues	11,078.5	27,361.5	47,158.3	16,196.9	2,312.5	1,944.9	1,574.5	3,852.2
Underwritten issues	94,368.0	92,213.5	121,608.5	32,701.5	6,533.5	7,573.4	2,114.5	4,215.2

1 This Includes the volume of issues admitted to trading without register issuance prospectuses.
2 Available data: November 2008.
3 The figures for commercial paper refer to the amount placed in the year.

Issues admitted to trading on AIAF

TABLE 1.10

				2007	2008			
Nominal amount in million euro	2005	2006	2007	IV	I	II	III	IV[1]
Total	425,137.4	507,525.3	640,096.2	144,959.2	121,675.6	131,470.5	102,755.3	75,398.2
Commercial paper	263,728.9	332,328.4	439,787.3	98,821.1	89,157.4	85,450.1	74,588.8	42,097.6
Bonds and debentures	56,771.5	45,155.4	30,006.9	2,704.9	507.0	3,164.6	4,878.2	753.3
Mortgage covered bonds	31,600.0	43,720.0	27,195.5	2,575.0	1,225.0	8,145.0	3,300.0	980.0
Territorial covered bonds	1,775.0	2,650.0	7,450.0	0.0	930.0	200.0	0.0	800.0
Backed securities	67,480.5	83,042.5	135,149.5	40,858.1	29,760.2	34,410.8	19,938.3	30,767.3
Preference shares	3,781.5	629.0	507.0	0.0	96.0	100.0	50.0	0.0
Matador bonds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

1 Available data: November 2008.

AIAF. Issuers, issues and outstanding balance

TABLE 1.11

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
NO. OF ISSUERS	384	438	492	492	509	526	526	542
Commercial paper	66	69	73	73	74	73	72	71
Bonds and debentures	82	80	92	92	91	91	93	93
Mortgage covered bonds	12	14	14	14	17	22	22	22
Territorial covered bonds	3	5	7	7	11	11	11	11
Backed securities	211	257	316	316	333	352	366	378
Preference shares	42	46	50	50	52	52	52	52
Matador bonds	20	20	15	15	15	14	14	13
NO. OF ISSUES	2,836	3,681	4,314	4,314	4,410	4,693	4,767	4,646
Commercial paper	1,724	2,242	2,493	2,493	2,480	2,669	2,670	2,499
Bonds and debentures	329	398	445	445	442	452	457	458
Mortgage covered bonds	54	83	111	111	121	140	144	148
Territorial covered bonds	8	11	19	19	25	26	26	27
Backed securities	631	856	1,157	1157	1249	1314	1,376	1,421
Preference shares	58	65	71	71	75	76	78	78
Matador bonds	32	26	18	18	18	16	16	15
OUTSTANDING BALANCE[2] (Million euro)	448,679.3	588,942.3	758,559.8	758,559.8	772,385.6	809,241.1	812,631.3	813,211.1
Commercial paper	57,719.4	70,778.6	98,467.6	98,467.6	96,152.7	101,545.3	90,658.5	78,208.7
Bonds and debentures	103,250.7	131,107.8	139,586.3	139,586.3	132,397.1	131,568.3	132,099.8	124,579.8
Mortgage covered bonds	90,550.0	129,710.0	150,905.5	150,905.5	152,130.5	160,275.5	163,475.5	164,065.5
Territorial covered bonds	7,575.0	9,525.0	16,375.0	16,375.0	16,305.0	16,505.0	16,505.0	17,305.0
Backed securities	164,810.0	222,866.1	328,924.6	328,924.6	351,003.4	374,939.4	385,434.9	404,624.5
Preference shares	22,486.6	23,115.6	23,062.6	23,062.6	23,158.6	23,258.6	23,308.6	23,308.6
Matador bonds	2,287.6	1,839.2	1,238.2	1,238.2	1,238.2	1,148.9	1,148.9	1,118.9

1 Available data: November 2008.
2 Nominal amount.

AIAF. Trading

TABLE 1.12

				2007	2008			
Nominal amount in million euro	2005	2006	2007	IV	I	II	III	IV[1]
BY TYPE OF ASSET	877,812.1	910,493.9	1,127,477.7	291,041.6	338,568.2	594,085.2	612,731.3	637,152.5
Commercial paper	408,185.0	489,069.5	568,009.6	124,955.9	130,792.9	134,918.8	158,880.3	115,906.4
Bonds and debentures	86,585.7	82,421.1	87,035.7	15,580.9	19,036.9	23,289.2	20,573.0	12,881.6
Mortgage covered bonds	60,060.9	70,113.5	80,811.2	24,196.7	17,036.8	42,302.2	47,216.7	12,888.1
Territorial covered bonds	2,740.1	3,659.1	7,749.8	1,649.6	4,669.9	1,276.3	711.3	2,863.4
Backed securities	313,778.5	257,628.9	378,005.2	123,504.1	166,049.8	391,436.8	384,574.7	491,577.7
Preference shares	4,046.2	4,647.8	4,492.4	1,153.4	976.0	860.0	774.5	1,033.5
Matador bonds	2,415.7	2,954.1	1,373.8	0.9	6.0	1.9	0.9	1.8
BY TYPE OF TRANSACTION	877,812.1	910,493.9	1,127,477.7	291,041.6	338,568.2	594,085.2	612,731.3	637,152.5
Outright	322,819.1	386,368.8	416,477.9	97,807.4	99,070.8	102,383.8	82,146.1	72,329.4
Repos	284,520.0	330,839.9	441,362.7	94,131.8	84,487.7	87,594.2	110,322.5	70,187.6
Sell-buybacks/Buy-sellbacks	270,473.0	193,285.1	269,637.1	99,102.3	155,009.7	404,107.3	420,262.6	494,635.5

1 Available data: November 2008.

AIAF. Third-party trading. By purchaser sector

TABLE 1.13

				2007	2008			
Nominal amount in million euro	2005	2006	2007	IV	I	II	III	IV[1]
Total	591,837.2	702,608.8	837,308.5	184,318.1	178,672.7	182,988.0	188,253.0	137,516.6
Non-financial companies	218,139.5	260,108.1	364,490.6	82,132.5	73,182.6	74,341.5	73,146.1	45,166.1
Financial institutions	218,381.1	247,876.4	282,816.9	69,024.8	71,161.5	76,965.1	89,107.6	69,761.0
Credit institutions	71,118.9	83,999.1	99,492.0	26,550.0	25,715.4	31,458.1	31,066.3	29,742.1
CIS[2], insurance and pension funds	138,580.4	145,911.5	152,429.2	34,195.3	39,714.3	40,498.2	38,242.5	26,432.2
Other financial institutions	8,681.8	17,965.8	30,895.6	8,279.5	5,731.7	5,008.8	19,798.7	13,586.7
General government	5,629.4	7,058.9	7,762.4	1,108.1	1,224.6	1,965.7	907.8	1,463.8
Households and NPISHs[3]	14,433.3	23,675.9	28,534.8	3,749.2	3,656.6	3,609.7	2,951.3	2,166.4
Rest of the world	135,253.9	163,889.4	153,703.8	28,303.5	29,447.4	26,106.1	22,140.3	18,959.2

1 Available data: November 2008.
2 Collective Investment Schemes.
3 Non-profit institutions serving households.

Issues admitted to trading on equity markets. Files registered at the CNMV

TABLE 1.14

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
NOMINAL AMOUNTS (Million euro)	1,234.6	68.1	7,000.0	7,000.0	0.0	0.0	0.0	0.0
Non-convertible bonds and debentures	1,140.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Convertible bonds and debentures	94.6	68.1	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	7,000.0	7,000.0	0.0	0.0	0.0	0.0
NO. OF FILES	6	1	1	1	0	0	0	0
Non-convertible bonds and debentures	3	0	0	0	0	0	0	0
Convertible bonds and debentures	3	1	0	0	0	0	0	0
Others	0	0	1	1	0	0	0	0

1 Available data: November 2008.

Equity markets. Issuers, issues and outstanding balances

TABLE 1.15

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
NO. OF ISSUERS	56	57	53	53	53	52	56	57
Private issuers	39	40	40	40	40	40	44	45
Non-financial companies	12	10	6	6	6	6	6	6
Financial institutions	27	30	34	34	34	34	38	39
General government[3]	17	17	13	13	13	12	12	12
Regional governments	3	3	3	3	3	3	3	3
NO. OF ISSUES	267	264	249	249	245	248	262	267
Private issuers	122	131	133	133	133	133	151	153
Non-financial companies	22	18	12	12	10	10	10	10
Financial institutions	100	113	121	121	123	123	141	143
General government[3]	145	133	116	116	112	115	111	114
Regional governments	92	89	83	83	81	84	80	83
OUTSTANDING BALANCES[2] (Million euro)	16,323.0	17,105.4	25,654.7	25,654.7	25,583.8	26,027.7	27,916.8	28,987.6
Private issuers	5,507.3	6,784.3	14,958.1	14,958.1	14,800.1	14,609.4	16,764.9	17,160.4
Non-financial companies	835.4	492.1	452.5	452.5	381.2	381.2	381.2	381.1
Financial institutions	4,671.9	6,292.2	14,505.6	14,505.6	14,418.9	14,228.2	16,383.7	16,779.4
General government[3]	10,816.1	10,321.1	10,696.6	10,696.6	10,783.7	11,418.3	11,151.9	11,827.2
Regional governments	8,457.2	8,319.8	8,862.6	8,862.6	9,100.3	9,535.4	9,269.6	9,944.9

1 Available data: November 2008.
2 Nominal amount.
3 Without public book-entry debt.

Trading on equity markets

TABLE 1.16

				2007	2008			
Nominal amounts in million euro	2005	2006	2007	IV	I	II	III	IV[1]
Electronic market	220.0	257.3	444.8	316.3	537.7	366.0	189.3	405.8
Open outcry	4,538.3	5,009.9	7,154.3	4,023.6	1,873.2	123.2	4,656.8	792.4
Madrid	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Barcelona	4,404.2	4,879.6	7,040.1	3,998.2	1,829.1	87.6	4,626.3	749.9
Bilbao	9.2	24.8	7.5	2.1	1.6	1.0	2.8	0.6
Valencia	124.8	105.5	106.7	23.2	42.6	34.7	27.6	41.9
Public book-entry debt	36.1	35.6	33.6	8.7	8.8	11.7	6.7	14.3
Regional governments debt	83,204.0	84,443.6	84,178.3	21,152.6	16,972.7	19,324.8	16,948.8	12,947.9

1 Available data: November 2008.

Organised trading systems: SENAF y MTS. Public debt trading by type

TABLE 1.17

				2007	2008			
Nominal amounts in million euro	2005	2006	2007	IV	I	II	III	IV[1]
Total	219.6	175.1	95.8	32.8	27.3	21.2	20.2	7.4
Outright	71.0	94.3	58.6	15.2	19.5	6.1	8.5	3.1
Sell-buybacks/Buy-sellbacks	148.5	80.2	37.2	17.6	7.8	15.1	11.7	4.3
Others	0.1	0.6	0.0	0.0	0.0	0.0	0.0	0.0

1 Available data: November 2008.

1.3 Derivatives and other products

1.3.1 Financial derivatives markets: MEFF

Trading on MEFF TABLE 1.18

				2007	2008			
Number of contracts	2005	2006	2007	IV	I	II	III	IV[1]
Debt products	46	15	13	4	4	4	2	1
Debt futures[2]	46	15	13	4	4	4	2	1
Ibex 35 products[3, 4]	5,490,958	7,119,853	9,288,909	2,176,326	2,346,726	1,894,015	2,256,855	1,499,645
Ibex 35 plus futures	4,935,648	6,408,961	8,435,258	1,931,745	2,042,491	1,654,458	1,934,608	1,210,700
Ibex 35 mini futures	114,563	159,830	286,574	75,552	84,643	71,975	84,677	66,719
Call mini options	232,825	288,542	227,535	82,293	76,766	60,052	106,673	114,500
Put mini options	207,922	262,521	339,542	86,736	142,826	107,529	130,897	107,727
Stock products[5]	29,728,916	33,655,790	34,887,808	13,011,176	12,300,311	19,168,497	15,788,553	8,855,979
Futures	18,813,689	21,229,811	21,294,315	8,637,161	8,519,578	14,797,445	11,983,940	6,326,844
Call options	6,803,863	7,664,125	6,775,525	2,097,371	1,585,176	1,571,132	1,673,144	1,316,183
Put options	4,111,364	4,761,854	6,817,968	2,276,644	2,195,557	2,799,920	2,131,469	1,212,952
Pro-memoria: MEFF trading on Eurex								
Debt products[6]	1,440,370	1,117,956	1,059,113	219,959	342,976	220,077	132,608	62,401
Index products[7]	1,080,801	1,423,441	1,371,250	265,783	348,341	268,663	275,658	145,999

1 Available data: November 2008.
2 Contract size: 100 thousand euros.
3 The number of Ibex 35 mini futures (multiples of 1 euro) was standardised to the size of the Ibex 35 plus futures (multiples of 10 euro).
4 Contract size: Ibex 35 * 10 euros.
5 Contract size: 100 Stocks.
6 Bund, Bobl and Schatz futures.
7 Dax 30, DJ EuroStoxx 50 and DJ Stoxx 50 futures.

1.3.2 Warrants, option buying and selling contracts, and ETF (Exchange Traded Funds)

Issues registered at the CNMV TABLE 1.19

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
WARRANTS[2]								
Premium amount (Million euro)	1,840.0	5,144.3	8,920.3	2,513.7	3,173.0	3,153.2	3,087.6	1,348.6
On stocks	1,180.8	3,697.6	6,215.1	1,836.7	2,257.1	1,663.2	1,576.8	534.7
On indexes	559.9	1,064.9	2,311.2	529.1	726.8	1,270.1	1,385.3	685.9
Other underlyings[3]	99.3	381.8	394.0	147.8	189.1	219.9	125.5	128.1
Number of issues	1,720	4,063	7,005	2,126	2,791	1,928	2,523	911
Number of issuers	6	8	7	7	7	7	6	5
OPTION BUYING AND SELLING CONTRACTS								
Nominal amounts (Million euro)	112.2	206.8	151.0	20.0	12.0	45.0	20.0	0.0
On stocks	87.8	196.2	145.0	20.0	12.0	45.0	20.0	0.0
On indexes	16.4	0.6	0.0	0.0	0.0	0.0	0.0	0.0
Other underlyings[3]	8.0	10.0	6.0	0.0	0.0	0.0	0.0	0.0
Number of issues	13	12	9	2	1	2	1	0
Number of issuers	4	4	3	1	1	1	1	0

1 Available data: November 2008.
2 Includes issues not requiring a prospectus by application of the new regulations.
3 Includes the following underlying: baskets of stocks, exchange rates, interest rates and commodities.

Equity markets. Warrants and ETF trading

TABLE 1.20

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
WARRANTS								
Trading (Million euro)	2,142.3	2,907.4	5,129.6	1,206.7	892.9	684.1	701.7	505.3
On Spanish stocks	1,431.7	1,803.9	3,200.7	788.0	521.5	362.8	333.5	284.1
On foreign stocks	155.8	294.7	474.2	104.6	47.0	50.4	30.9	12.9
On indexes	516.8	727.4	1,376.6	297.7	303.2	231.1	295.7	173.2
Other underlyings[2]	38.0	81.4	78.1	16.5	21.2	39.8	41.6	35.0
Number of issues[3]	2,520	4,284	7,837	4,083	4,144	4,214	4,219	3,557
Number of issuers[3]	8	9	9	9	9	8	8	9
CERTIFICATES								
Trading (Million euro)	69.8	58.8	57.5	13.3	5.1	5.0	2.8	2.9
Number of issues[3]	15	14	18	17	17	21	17	19
Number of issuers[3]	5	5	4	4	4	4	4	4
ETF								
Trading (Million euro)	-	-	4,664.5	2,059.6	3,037.1	1,357.4	900.6	1,408.4
Number of funds	-	-	21	21	27	32	29	30
Assets[4] (Million euro)	-	-	885.8	885.8	1,994.7	2,212.6	2,111.2	na

1 Available data: November 2008.
2 Includes the following underlying: baskets of stocks, exchange rates, interest rates and commodities.
3 Issues or issuers which were traded in each period.
4 Foreign collective investment schemes including the investment volume marketed in Spain.
na: No available data.

1.3.3 Non-financial derivatives

Trading on MFAO[1]

TABLE 1.21

				2007	2008			
Number of contracts	2005	2006	2007	IV	I	II	III	IV[2]
On olive oil								
Extra-virgin olive oil futures[3]	21,145	35,079	46,405	9,721	13,586	14,610	7,530	8,355

1 Olive oil futures market.
2 Available data: November 2008.
3 Nominal amount of the contract: 1,000 kg.

2 Investment services

Investment services. Spanish firms, branches and agents

TABLE 2.1

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
Broker-dealers								
Spanish firms	46	47	46	46	49	51	50	50
Branches	96	108	102	102	109	80	85	86
Agents	6,562	6,610	6,657	6,657	6,674	6,526	6,546	6,546
Brokers								
Spanish firms	56	57	53	53	50	52	53	53
Branches	11	11	12	12	7	10	10	9
Agents	516	589	625	625	624	625	631	635
Portfolio management companies								
Spanish firms	17	15	11	11	11	11	10	10
Branches	4	4	4	4	4	4	4	4
Agents	14	5	6	6	5	5	5	6
Credit institutions[2]								
Spanish firms	206	204	201	201	200	200	200	200

1 Available data: November 2008.
2 Source: Banco de España.

Investment services. Foreign firms

TABLE 2.2

	2005	2006	2007	2007 IV	2008 I	II	III	IV[1]
Total	1,196	1,321	1,766	1,766	1,949	2,054	2,156	2,217
European Economic Area investment services firms	867	973	1,394	1,394	1,573	1,676	1,760	1,803
Branches	18	22	29	29	30	33	33	36
Free provision of services	849	951	1,365	1,365	1,543	1,643	1,727	1,767
Credit institutions[2]	329	348	372	372	376	378	396	414
From EU member states	320	339	363	363	367	369	387	405
Branches	38	44	52	52	55	56	56	56
Free provision of services	281	294	310	310	311	312	330	348
Subsidiaries of free provision of services institutions	1	1	1	1	1	1	1	1
From non-EU states	9	9	9	9	9	9	9	9
Branches	8	8	8	8	8	8	8	8
Free provision of services	1	1	1	1	1	1	1	1

1 Available data: November 2008.
2 Source: Banco de España.

Intermediation of spot transactions

TABLE 2.3

	III 2007				III 2008			
Million euro	Spanish Stock Exchange	Other Spanish markets	Foreign markets	Total	Spanish Stock Exchange	Other Spanish markets	Foreign markets	Total
FIXED-INCOME								
Total	6,698	2,604,288	256,176	2,867,162	5,557	2,152,306	369,162	2,527,025
Broker-dealers	6,447	189,464	43,066	238,977	5,085	265,006	45,982	316,073
Brokers	251	2,414,824	213,110	2,628,185	472	1,887,300	323,180	2,210,952
EQUITY								
Total	520,627	1,737	32,452	554,816	497,609	958	21,004	519,571
Broker-dealers	490,105	843	29,459	520,407	471,786	817	18,367	490,970
Brokers	30,522	894	2,993	34,409	25,823	141	2,637	28,601

Intermediation of derivative transactions[1]

TABLE 2.4

	III 2007				III 2008			
Million euro	Spanish organised markets	Foreign organised markets	Non-organised markets	Total	Spanish organised markets	Foreign organised markets	Non-organised markets	Total
Total	288,268	2,591,170	1,057,950	3,937,388	188,804	1,742,662	830,446	2,761,912
Broker-dealers	83,813	305,357	39,077	428,247	168,709	1,434,880	86,847	1,690,436
Brokers	204,455	2,285,813	1,018,873	3,509,141	20,095	307,782	743,599	1,071,476

1 The amount of the buy and sell transactions of financial assets, financial futures on values and interest rates, and other transactions on interest rates will be the securities nominal or notional value or the principal to which the contract reaches. The amount of the transactions on options will be the strike price of the underlying asset multiplied by the number of instruments committed.

Portfolio management. Number of portfolios and assets under management

TABLE 2.5

	III 2007			III 2008		
	Total	IIC[1]	Other[2]	Total	IIC[1]	Other[2]
NUMBER OF PORTFOLIOS						
Total	19,522	98	19,424	14,460	122	14,338
Broker-dealers	10,942	26	10,916	7,959	30	7,929
Brokers	4,102	36	4,066	3,455	57	3,398
Portfolio management companies	4,478	36	4,442	3,046	35	3,011
ASSETS UNDER MANAGEMENT (Thousand euro)						
Total	14,392,649	1,623,472	12,769,177	10,424,926	987,598	9,437,328
Broker-dealers	6,138,028	785,005	5,353,023	4,527,698	204,978	4,322,720
Brokers	3,476,861	548,258	2,928,603	2,451,981	553,315	1,898,666
Portfolio management companies	4,777,760	290,209	4,487,551	3,445,247	229,305	3,215,942

1 IIC: Collective investment schemes.
2 Includes the rest of clients, both covered and not covered by the Investment Guarantee Fund, an investor compensation scheme regulated by Royal Decree 948/2001.

Aggregated income statement. Broker-dealers

TABLE 2.6

Thousand euro[1]	2005	2006	2007	2007 IV	2008 I	II	III	IV[2]
I. FINANCIAL INCOME	57,653	17,325	-29,968	-29,968	-10,488	22,373	53,300	75,899
II. NET INCOME FROM SECURITIES TRADING	200,360	48,335	-224,173	-224,173	78,843	399,526	634,655	731,933
III. NET COMMISSION	653,273	775,377	893,803	893,803	195,164	368,472	502,553	566,125
Commission revenues	847,524	1,009,089	1,181,772	1,181,772	270,711	501,817	693,140	788,008
Brokering	526,241	629,952	775,418	775,418	186,711	343,910	484,674	557,769
Placement and underwriting	58,685	73,278	62,145	62,145	10,560	25,112	28,263	31,746
Securities deposit and recording	17,593	22,367	25,351	25,351	5,861	11,477	16,421	17,866
Portfolio management	20,599	23,883	29,649	29,649	5,946	9,893	13,886	15,177
Design and advising	52,180	55,918	65,083	65,083	7,729	12,781	17,039	20,768
Stocks search and placement	6	0	9	9	7	9	11	12
Market credit transactions	56	33	23	23	5	7	9	11
IIC subscription and redemption	118,871	141,312	138,481	138,481	30,202	55,621	74,113	79,912
Other	53,293	62,346	85,613	85,613	23,690	43,007	58,724	64,747
Commission expenses	194,251	233,712	287,969	287,969	75,547	133,345	190,587	221,883
IV. TOTAL NET REVENUES	911,286	841,037	639,662	639,662	263,519	790,371	1,190,508	1,373,957
V. OPERATING INCOME	498,362	395,105	180,892	180,892	144,447	553,546	864,482	1,013,740
VI. EARNINGS AFTER TAXES	266,734	430,651	540,390	540,390	151,025	301,711	361,479	400,727

1 Added amounts from the beginning of the year to the last day of every quarter. It includes companies removed through out the year.
2 Available data: October 2008.

Results of proprietary trading. Broker-dealers

TABLE 2.7

Thousand euro[1]	Total III 2007	Total III 2008	Financial income III 2007	Financial income III 2008	Securities portfolio III 2007	Securities portfolio III 2008	Other charges III 2007	Other charges III 2008
Total	-236,757	671,581	-15,840	53,300	-214,615	634,655	-6,302	-16,374
Money market assets and public debt	-17,193	-425	2,967	7,611	-20,160	-8,036	-	-
Other fixed-income securities	63,273	51,629	44,807	53,237	18,466	-1,608	-	-
Domestic portfolio	49,955	49,357	41,276	51,784	8,679	-2,427	-	-
Foreign portfolio	13,318	2,272	3,531	1,453	9,787	819	-	-
Equities	219,519	-998,729	83,233	50,338	136,286	-1,049,067	-	-
Domestic portfolio	140,601	-230,872	33,345	16,283	107,256	-247,155	-	-
Foreign portfolio	78,918	-767,857	49,888	34,055	29,030	-801,912	-	-
Derivatives	-337,463	1,709,089	-	-	-337,463	1,709,089	-	-
Repurchase agreements	-8,028	-11,717	-8,028	-11,717	-	-	-	-
Market credit transactions	0	0	0	0	-	-	-	-
Deposits and other transactions with financial Intermediaries	-148,603	-68,334	-148,603	-68,334	-	-	-	-
Other transactions	-8,262	-9,932	9,784	22,165	-11,744	-15,723	-6,302	-16,374

1 Added amounts from the beginning of the year to the last day of every quarter. It includes companies removed through out the year.

Aggregated income statement. Brokers

TABLE 2.8

Thousand euro[1]	2005	2006	2007	2007 IV	2008 I	II	III	IV[2]
I. FINANCIAL INCOME	10,665	12,934	14,395	14,395	2,434	6,039	7,822	8,426
II. NET INCOME FROM SECURITIES TRADING	3,306	3,906	580	580	-939	-1,363	-2,026	-3,096
III. NET COMMISSION	184,113	233,447	237,403	237,403	41,507	82,530	115,919	128,724
Commission revenues	229,752	297,030	310,892	310,892	48,935	95,111	133,583	148,213
Brokering	97,948	114,111	131,976	131,976	19,349	33,728	47,825	54,055
Placement and underwriting	3,821	3,183	2,501	2,501	994	3,010	4,354	4,487
Securities deposit and recording	1,357	1,520	1,680	1,680	314	394	512	538
Portfolio management	14,868	28,672	27,457	27,457	5,847	11,966	16,783	17,880
Design and advising	2,664	2,360	2,224	2,224	252	1,550	2,181	2,589
Stocks search and placement	0	0	0	0	0	0	0	0
Market credit transactions	0	0	0	0	0	0	0	0
IIC subscription and redemption	46,171	68,513	74,918	74,918	9,679	17,156	24,309	26,849
Other	62,923	78,671	70,136	70,136	12,500	27,307	37,619	41,815
Commission expenses	45,639	63,583	73,489	73,489	7,428	12,581	17,664	19,489
IV. TOTAL NET REVENUES	198,084	250,287	252,378	252,378	43,002	87,206	121,715	134,054
V. OPERATING INCOME	66,420	95,026	98,596	98,596	9,302	14,001	19,259	20,712
VI. EARNINGS AFTER TAXES	38,264	62,449	86,017	86,017	9,427	15,919	25,623	27,186

1 Added amounts from the beginning of the year to the last day of every quarter. It includes companies removed through out the year.
2 Available data: October 2008.

Aggregated income statement. Portfolio management companies

TABLE 2.9

Thousand euro[1]	2005	2006	2007	2007 IV	2008 I	II	III	IV[2]
I. FINANCIAL INCOME	575	895	1,442	1,442	376	789	1,210	1,318
II. NET INCOME FROM SECURITIES TRADING	65	6	21	21	-32	-158	-159	-227
III. NET COMMISSION	17,164	15,195	15,501	15,501	3,459	6,583	9,382	10,228
Commission revenues	25,508	27,625	27,340	27,340	6,308	12,392	18,138	19,951
Portfolio management	18,813	22,068	22,545	22,545	5,203	10,243	15,157	16,730
Design and advising	4,380	4,951	2,614	2,614	637	1,226	1,677	1,797
IIC subscription and redemption	592	261	1,728	1,728	368	675	936	1,017
Other	1,723	345	453	453	100	248	368	407
Commission expenses	8,344	12,430	11,839	11,839	2,849	5,809	8,756	9,723
IV. TOTAL NET REVENUES	17,804	16,096	16,964	16,964	3,803	7,214	10,433	11,319
V. OPERATING INCOME	6,051	6,352	7,226	7,226	1,041	1,543	2,150	2,241
VI. EARNINGS AFTER TAXES	3,465	4,112	4,837	4,837	730	1,009	1,428	1,355

1 Added amounts from the beginning of the year to the last day of every quarter. It includes companies removed through out the year.
2 Available data: October 2008.

Surplus equity over capital adequacy requirements[1]

TABLE 2.10

Thousand euro	Surplus: Total amount	Surplus: %[2]	Number of companies according to its surplus percentage: < 50[3]	<100	<150	<200	<300	<400	<500	<750	<1000	>1000
Total	1,307,895	383.44	8	12	14	12	16	11	8	12	4	16
Broker-dealers	1,189,773	420.71	2	1	4	1	11	5	5	6	4	11
Brokers	97,339	237.05	5	10	8	8	4	5	3	6	0	4
Portfolio management companies	20,783	120.65	1	1	2	3	1	1	0	0	0	1

1 Available data: September 2008.
2 Average percentage is weighted by the required equity of each company. It is an indicator of the number of times, in percentage terms, that the surplus contains the required equity in an average company.
3 Includes all registered companies, even if they have not sent information.

Return on equity (ROE) before taxes[1]

TABLE 2.11

	Average[2]	Number of companies according to its annualized return: Losses	0-5%	6-15%	16-30%	31-45%	46-60%	61-75%	76-100%	>100%
Total	30.40	29	14	19	11	17	6	7	3	7
Broker-dealers	31.61	9	6	9	7	8	4	2	2	3
Brokers	23.78	17	6	7	3	8	2	5	1	4
Portfolio management companies	5.98	3	2	3	1	1	0	0	0	0

1 Available data: September 2008.
2 Average weighted by equity, %.

3 Collective investment schemes (IIC)*

Number, management companies and depositories of collective investment schemes registered at the CNMV

TABLE 3.1

	2005	2006	2007	2007 IV	2008 I	II	III	IV[1]
Total financial IIC	5,841	6,006	6,296	6,296	6,347	6,395	6,389	6,372
Mutual funds	2,723	2,850	2,954	2,954	2,956	2,968	2,954	2,946
Investment companies	3,118	3,149	3,290	3,290	3,328	3,365	3,369	3,361
Funds of hedge funds	-	2	31	31	38	39	41	40
Hedge funds	-	5	21	21	25	23	25	25
Total real estate IIC	13	17	18	18	17	17	17	17
Real estate investment funds	7	9	9	9	9	9	9	9
Real estate investment companies	6	8	9	9	8	8	8	8
Total foreign IIC marketed in Spain	260	340	440	440	465	490	535	559
Foreign funds marketed in Spain	115	164	225	225	241	253	290	308
Foreign companies marketed in Spain	145	176	215	215	224	237	245	251
Management companies	112	114	120	120	121	120	120	120
IIC depositories	135	132	126	126	126	126	126	126

1 Available data: November 2008.

* In this document, neither hedge funds nor funds of hedge funds are included in the figures referred to mutual funds.

Number of IIC investors and shareholders

TABLE 3.2

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
Total financial IIC	8,869,084	9,048,207	8,492,282	8,492,282	7,861,369	7,466,954	6,970,806	-
Mutual funds	8,450,164	8,637,781	8,053,049	8,053,049	7,420,379	7,023,292	6,520,089	6,179,177
Investment companies	418,920	410,403	434,156	434,156	434,167	433,651	439,395	-
Funds of hedge funds[2]	-	2	3,950	3,950	5,488	8,582	9,739	9,639
Hedge funds[2]	-	21	1,127	1,127		1,429	1,583	1,582
Total real estate IIC	119,113	151,053	146,353	146,53	145,036	141,876	136,245	128,739
Real estate investment funds	118,857	150,304	145,510	145,510	144,197	141,037	135,307	127,801
Real estate investment companies	256	749	843	843	839	839	938	938
Total foreign IIC marketed in Spain	560,555	779,165	850,931	850,931	729,321	697,732	648,457	-
Foreign funds marketed in Spain	104,089	144,139	142,782	142,782	137,933	124,446	112,064	-
Foreign companies marketed in Spain	456,466	635,026	708,149	708,149	591,388	573,286	536,393	-

1 Available data: October 2008. Real estate investment companies and foreign IIC send this information quarterly.
2 Provisional data in case of funds of hedge funds and hedge funds.

IIC total net assets

TABLE 3.3

				2007	2008			
Million euro	2005	2006	2007	IV	I	II	III	IV[1]
Total financial IIC	289,810.7	300,584.0	287,968.7	287,968.7	264,775.7	244,660.6	226,473.9	211,535.5
Mutual funds[2]	262,200.9	270,406.3	255,040.9	255,040.9	234,043.9	214,251.8	197,305.6	184,151.4
Investment companies	27,609.8	30,152.7	31,481.5	31,481.5	29,055.9	28,415.3	27,143.2	25,422.2
Funds of hedge funds[3]	-	0.6	1,000.6	1,000.6	1,129.6	1,389.6	1,427.5	1,384.4
Hedge funds[3]	-	24.4	445.8	445.8	546.3	603.9	597.7	576.9
Total real estate IIC	6,690.8	9,052.0	9,121.4	9,121.4	8,912.8	8,753.1	8,530.6	8,541.4
Real estate investment funds	6,476.9	8,595.9	8,608.5	8,608.5	8,563.8	8,394.0	8,166.7	8,175.9
Real estate investment companies	213.9	456.1	512.9	512.9	349.0	359.2	363.8	365.5
Total foreign IIC marketed in Spain	33,668.1	44,102.9	37,092.7	37,092.7	30,184.5	28,581.0	22,046.4	-
Foreign funds marketed in Spain	8,267.3	12,099.3	7,010.3	7,010.3	5,004.9	4,313.5	3,064.6	-
Foreign companies marketed in Spain	25,400.8	32,003.5	30,082.4	30,082.4	25,179.6	24,267.5	18,981.8	-

1 Available data: October 2008. Real estate investment companies and foreign IIC send this information quarterly.
2 For the third quarter 2008, mutual funds investments in financial IIC reached 16.3 billion euro.
3 Provisional data in case of funds of hedge funds and hedge funds.

Mutual funds asset allocation[1,2]

TABLE 3.4

				2007	2008			
Million euro	2005	2006	2007	IV	I	II	III	IV[3]
Asset	262,200.9	270,406.9	256,040.2	256,040.2	235,173.5	215,618.2	198,730.5	185,535.7
Cash	8,207.5	10,462.9	15,485.2	15,485.2	15,768.9	17,710.9	20,685.9	20,154.7
Portfolio investment	255,273.6	260,002.9	240,110.5	240,110.5	219,010.7	197,728.4	177,568.5	164,856.6
Domestic securities	123,683.6	127,355.4	134,700.7	134,700.7	128,697.2	115,902.8	105,206.6	100,540.7
Shares	11,602.1	13,806.8	11,600.7	11,600.7	8,137.3	6,802.7	5,501.0	4,314.0
Mutual funds units	17,255.9	17,322.8	18,720.4	18,720.4	17,772.2	15,822.3	13,745.3	11,806.6
Public money market assets	4,149.4	2,887.7	2,206.6	2,206.6	3,493.5	4,618.6	4,488.8	5,473.1
Other public fixed-income	10,088.7	9,891.6	8,708.7	8,708.7	6,608.3	6,299.7	6,334.9	5,426.0
Private money market assets	26,850.7	28,483.2	37,486.9	37,486.9	35,309.7	35,514.6	30,277.3	27,298.3
Other private fixed-income	18,835.6	23,105.3	24,251.5	24,251.5	23,039.2	22,873.3	20,884.5	19,456.6
Spanish warrants and options	483.1	603.3	553.2	553.2	344.0	414.4	309.7	261.0
Repos	34,417.8	31,229.4	31,172.4	31,172.4	33,992.7	23,557.0	23,664.2	26,504.8
Unlisted securities	0.2	25.4	0.2	0.2	0.2	0.2	0.9	0.2
Foreign securities	131,590.0	132,647.4	105,409.8	105,409.8	90,313.5	81,825.6	72,361.9	64,315.9
Euros	118,871.5	118,664.1	94,205.2	94,205.2	82,742.5	74,569.0	66,564.8	59,484.7
Shares	8,925.1	11,418.0	10,772.1	10,772.1	6,970.4	5,859.8	4,589.8	3,549.0
Mutual fund units	15,986.0	23,414.2	13,149.1	13,149.1	8,659.6	7,036.7	5,161.5	3,678.9
Fixed-income	90,220.7	78,933.4	65,972.8	65,972.8	64,362.8	59,588.6	55,157.3	50,896.3
Foreign warrants and options	3,739.7	4,898.7	4,311.2	4,311.2	2,749.7	2,083.0	1,654.6	1,359.0
Unlisted securities	0.0	0.0	0.0	0.0	0.0	0.8	1.6	1.6
Other	12,718.5	13,983.3	11,204.6	11,204.6	7,571.0	7,256.6	5,797.1	4,831.2
Shares	7,019.5	7,343.0	5,964.0	5,964.0	3,972.9	3,823.9	3,104.1	2,564.9
Mutual fund units	4,395.6	5,491.5	4,477.8	4,477.8	3,097.6	3,018.0	2,325.3	1,870.4
Fixed-income	1,204.8	1,011.7	631.1	631.1	413.5	386.2	336.8	356.7
Foreign warrants and options	97.2	136.0	130.8	130.8	86.4	27.7	30.2	38.5
Unlisted securities	1.4	1.2	0.9	0.9	0.8	0.8	0.7	0.7
Net balance (Debtors - Creditors)	-1,280.3	-58.8	444.5	444.5	393.9	178.8	476.1	524.5

1 Hedge funds are not included in these figures. The information is not available because hedge funds have different accounting regulation.
2 Provisional data in case of funds of hedge funds and hedge funds.
3 Available data: October 2008.

Investment companies asset allocation

TABLE 3.5

Million euro	2005	2006	2007	2007 IV	2008 I	II	III	IV[1]
Asset	27,610.0	30,152.7	31,481.5	31,481.5	29,055.9	28,415.2	27,143.2	25,422.2
Cash	728.9	802.2	1,182.2	1,182.2	1,457.3	1,938.4	2,759.1	2,343.0
Portfolio investment	26,884.9	29,294.1	30,037.4	30,037.4	27,440.2	26,306.3	24,131.2	22,946.7
Domestic securities	13,851.1	15,553.8	17,075.3	17,075.3	17,080.2	16,012.2	15,391.9	15,146.1
Shares	5,906.5	6,727.3	6,173.6	6,173.6	5,073.8	4,372.0	3,756.4	3,327.1
Mutual funds units	941.2	1,095.0	1,362.3	1,362.3	1,370.6	1,311.4	1,216.1	1,187.5
Public money market assets	128.1	463.4	382.8	382.8	386.6	348.3	403.9	460.3
Other public fixed-income	897.0	678.2	710.2	710.2	536.7	523.1	559.9	458.0
Private money market assets	359.1	555.4	1,568.6	1,568.6	1,854.6	2,199.0	2,102.8	1,870.7
Other private fixed-income	397.3	554.8	620.8	620.8	702.0	930.2	943.7	879.7
Spanish warrants and options	15.3	19.7	22.1	22.1	19.5	12.9	23.0	38.0
Repos	5,206.2	5,459.1	6,234.1	6,234.1	7,132.6	6,311.6	6,382.2	6,920.8
Unlisted securities	0.3	0.8	0.8	0.8	3.7	3.6	4.1	4.1
Foreign securities	13,033.8	13,740.3	12,962.2	12,962.2	10,360.0	10,294.1	8,739.3	7,800.5
Euros	9,178.6	9,847.7	9,413.7	9,413.7	7,768.0	7,711.5	6,568.0	5,938.4
Shares	2,885.6	3,379.9	3,367.7	3,367.7	2,319.8	2,083.2	1,633.1	1,324.3
Mutual fund units	3,351.6	4,169.1	3,826.1	3,826.1	3,252.4	3,148.5	2,419.5	2,119.2
Fixed-income	2,755.8	2,041.5	2,006.7	2,006.7	2,017.6	2,308.5	2,369.1	2,339.6
Foreign warrants and options	185.7	257.2	213.1	213.1	178.3	171.2	146.2	155.2
Unlisted securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	3,855.2	3,892.6	3,548.5	3,548.5	2,592.0	2,582.6	2,171.3	1,862.1
Shares	2,173.9	2,104.7	1,752.2	1,752.2	1,304.0	1,298.7	1,101.1	944.0
Mutual fund units	1,403.7	1,517.7	1,600.6	1,600.6	1,139.2	1,148.1	945.6	789.2
Fixed-income	270.0	234.8	183.2	183.2	138.9	123.4	111.9	119.3
Foreign warrants and options	7.5	11.3	12.5	12.5	9.9	12.3	12.7	9.6
Unlisted securities	0.1	24.1	0.0	0.0	0.0	0.0	0.0	0.0
Net balance (Debtors - Creditors)	-3.8	56.4	261.8	261.8	158.5	170.6	252.9	132.5

1 Available data: October 2008.

Financial mutual funds: number, investors and total net assets by category[1]

TABLE 3.6

	2005	2006	2007	2007 III	IV	2008 I	II	III
NO. OF FUNDS								
Total financial mutual funds	2,705	2,822	2,926	2,920	2,926	2,942	2,950	2,932
Fixed-income[2]	624	606	600	604	600	609	614	616
Mixed fixed-income[3]	217	212	204	203	204	203	197	195
Mixed equity[4]	222	222	207	216	207	206	205	204
Spanish equity	116	118	123	121	123	123	122	117
Foreign equity[5]	454	467	481	485	481	477	482	469
Guaranteed fixed-income	211	220	251	241	251	256	251	255
Guaranteed equity	514	559	590	589	590	592	601	600
Global funds	347	418	470	461	470	476	478	476
Funds of hedge funds[6]	-	2	31	30	31	38	39	41
Hedge funds[6]	-	5	21	17	21	25	23	25
INVESTORS								
Total financial mutual funds	8,450,164	8,637,781	8,053,049	8,467,203	8,053,049	7,420,379	7,023,292	6,520,089
Fixed-income[2]	3,071,656	2,960,879	2,763,442	2,869,191	2,763,442	2,620,712	2,498,451	2,389,795
Mixed fixed-income[3]	492,988	524,827	493,786	511,811	493,786	434,935	359,904	319,445
Mixed equity[4]	408,757	357,013	331,214	359,667	331,214	289,184	263,926	236,645
Spanish equity	365,301	317,386	288,210	343,208	288,210	219,842	204,259	180,472
Foreign equity[5]	1,199,460	1,258,426	1,089,868	1,184,871	1,089,868	942,733	907,345	758,463
Guaranteed fixed-income	455,237	497,540	549,108	540,637	549,108	552,116	542,500	552,515
Guaranteed equity	1,849,626	1,783,867	1,715,144	1,754,596	1,715,144	1,639,760	1,575,766	1,513,064
Global funds	607,139	937,843	822,277	903,222	822,277	721,097	671,141	569,690
Funds of hedge funds[6]	-	2	3,950	3,142	3,950	5,488	8,582	9,739
Hedge funds[6]	-	21	1,127	251	1,127	1,335	1,429	1,583
TOTAL NET ASSETS (Million euro)								
Total financial mutual funds	262,200.9	270,406.3	255,040.9	269,907.0	255,040.9	234,043.9	214,251.8	197,305.6
Fixed-income[2]	123,890.7	116,511.9	113,234.1	118,489.4	113,234.1	116,544.0	107,349.4	100,931.9
Mixed fixed-income[3]	14,625.8	15,314.5	13,011.9	14,142.3	13,011.9	10,551.0	8,488.5	7,175.8
Mixed equity[4]	10,005.6	10,149.2	8,848.0	9,753.4	8,848.0	6,811.6	5,990.9	5,092.8
Spanish equity	9,741.7	10,416.4	7,839.4	8,353.3	7,839.4	5,369.9	4,584.1	3,612.5
Foreign equity[5]	20,925.1	24,799.6	22,698.4	26,453.8	22,698.4	14,962.8	13,433.5	10,472.7
Guaranteed fixed-income	13,442.0	14,484.8	17,674.4	16,291.2	17,674.4	19,253.8	19,841.0	20,968.0
Guaranteed equity	45,839.8	44,796.6	42,042.1	43,365.6	42,042.1	38,521.4	35,633.2	33,782.8
Global funds	23,730.1	33,933.3	29,692.6	33,058.2	29,692.6	22,029.4	18,931.4	15,269.2
Funds of hedge funds[6]	-	0.6	1,000.6	829.2	1,000.6	1,129.6	1,389.6	1,427.5
Hedge funds[6]	-	24.4	445.8	210.2	445.8	546.3	603.9	597.7

1 Mutual funds that have sent reports to the CNMV (therefore mutual funds in a process of dissolution or liquidation are not included).
2 This category includes: Short-term fixed income, Long-term fixed income, Foreign fixed-income and Monetary market funds.
3 This category includes: Mixed fixed-income and Foreign mixed fixed-income.
4 This category includes: Mixed equity and Foreign mixed equity .
5 This category includes: Euro equity, Foreign equity Europe, Foreign equity Japan, Foreign equity USA, Foreign equity emerging countries and Other foreign equity.
6 Provisional data in case of funds of hedge funds and hedge funds.

Financial mutual funds: Detail of investors and total net assets by type of investors

TABLE 3.7

	2005	2006	2007	2007 IV	2008 I	II	III	IV[1]
INVESTORS	8,450,164	8,637,804	8,058,126	8,058,126	7,427,202	7,033,303	6,531,411	6,190,398
Individuals	8,202,638	8,389,315	7,818,701	7,818,701	7,206,815	6,827,129	6,340,598	6,008,226
Residents	8,101,310	8,292,264	7,725,443	7,725,443	7,116,692	6,740,765	6,259,219	5,930,143
Non-residents	101,328	97,051	93,258	93,258	90,123	86,364	81,379	78,083
Legal entities	247,526	248,489	239,425	239,425	220,387	206,174	190,813	182,172
Credit Institutions	1,634	1,609	2,276	2,276	1,130	1,192	1,163	1,042
Other resident Institutions	244,223	244,980	235,298	235,298	217,441	203,254	187,999	179,512
Non-resident Institutions	1,669	1,900	1,851	1,851	1,816	1,728	1,651	1,618
TOTAL NET ASSETS (Million euro)	262,200.9	270,431.3	256,487.3	256,487.3	235,719.8	216,245.3	199,328.8	186,113.3
Individuals	193,948.6	201,411.0	190,980.6	190,980.6	175,579.4	162,024.9	150,882.4	141,883.2
Residents	190,753.2	198,330.5	188,210.0	188,210.0	173,073.0	159,705.6	148,777.6	139,906.3
Non-residents	3,195.4	3,080.5	2,770.6	2,770.6	2,506.4	2,319.3	2,104.8	1,976.9
Legal entities	68,252.3	69,020.3	65,506.7	65,506.7	60,140.4	54,220.5	48,446.4	44,230.2
Credit Institutions	4,253.2	5,318.0	5,920.9	5,920.9	3,700.6	3,552.0	3,608.6	2,566.0
Other resident Institutions	62,749.8	61,646.6	57,670.6	57,670.6	54,904.4	48,892.1	43,178.0	40,256.7
Non-resident Institutions	1,249.4	2,055.7	1,915.2	1,915.2	1,535.4	1,776.4	1,659.8	1,407.5

1 Available data: October 2008.

Subscriptions and redemptions of financial mutual funds by category[1]

TABLE 3.8

Million euro	2005	2006	2007	2007 III	IV	2008 I	II	III
SUBSCRIPTIONS								
Total financial mutual funds[2]	169,807.0	194,787.4	180,943.6	42,610.5	41,508.2	47,016.2	33,450.6	23,895.9
Fixed-income	108,566.1	118,705.9	116,323.9	30,580.5	26,566.0	37,510.5	22,581.5	17,342.5
Mixed fixed-income	6,677.3	8,476.6	5,859.4	1,141.7	955.7	620.2	315.9	239.0
Mixed equity	2,065.2	2,783.6	2,749.8	635.6	452.2	278.9	606.0	250.9
Spanish equity	5,588.5	5,590.4	4,402.4	482.5	943.4	414.5	344.4	157.1
Foreign equity	14,006.2	17,662.3	16,631.5	3,215.9	2,971.3	1,867.3	1,545.7	926.3
Guaranteed fixed-income	6,923.9	6,126.2	9,161.3	2,191.3	2,981.1	3,286.2	2,983.5	2,692.4
Guaranteed equity	13,520.7	8,914.1	8,070.6	1,316.4	3,095.7	1,089.4	3,120.4	1,549.5
Global funds	12,459.2	26,528.3	17,744.2	3,046.3	3,542.7	1,949.1	1,953.1	738.3
Funds of hedge funds[4]	-	0.6	1,071.2	232.8	215.5	200.1	447.3	165.9
Hedge funds[4]	-	24.4	380.8	62.2	243.0	164.1	77.8	8.2
REDEMPTIONS								
Total financial mutual funds[3]	155,304.2	198,600.1	202,827.4	48,647.5	56,448.9	62,032.7	52,061.9	39,354.3
Fixed-income	107,150.9	127,469.1	122,178.3	28,982.4	32,605.9	35,049.1	32,357.6	24,503.3
Mixed fixed-income	4,339.6	7,048.4	7,809.6	2,049.5	2,128.0	2,861.9	1,891.3	1,437.2
Mixed equity	2,602.5	3,644.7	4,023.0	999.2	1,106.9	1,675.7	1,245.2	882.7
Spanish equity	5,323.3	7,824.6	6,723.3	1,429.0	1,682.8	1,979.7	733.9	868.4
Foreign equity	11,390.2	16,490.9	20,073.1	5,242.4	5,833.8	6,456.5	2,735.1	2,383.1
Guaranteed fixed-income	7,014.0	5,029.3	6,430.6	1,897.1	1,712.0	2,085.8	1,867.5	1,785.4
Guaranteed equity	8,931.6	11,830.1	11,602.6	2,142.1	4,437.3	3,647.6	5,929.2	3,924.0
Global funds	8,552.1	19,263.1	23,986.6	5,905.5	6,942.2	8,276.4	5,302.1	3,570.2
Funds of hedge funds[4]	-	0.0	65.9	11.1	53.2	98.7	234.5	101.5
Hedge funds[4]	-	0.1	2.6	0.45	2.1	50.9	26.5	14.5

1 Estimated data.
2 For the third quarter 2008, mutual funds subscriptions in financial IIC reached 1.3 billion euro.
3 For the third quarter 2008, mutual funds redemptions in financial IIC reached 3.2 billion euro.
4 Provisional data in case of funds of hedge funds and hedge funds.

Financial mutual funds asset change by category: Net subscriptions/redemptions and return on assets

TABLE 3.9

Million euro	2005	2006	2007	2007 III	IV	2008 I	II	III
NET SUBSCRIPTIONS/REDEMPTIONS								
Total financial mutual funds	14,444.3	-4,524.5	-21,877.7	-5,995.1	-14,990.5	-14,950.1	-18,602.1	-15,158.3
Fixed-income	1,445.5	-9,423.4	-5,852.4	1,601.6	-6,029.3	2,480.0	-9,672.7	-7,021.1
Mixed fixed-income	2,349.6	1,539.2	-1,942.0	-909.6	-1,163.6	-2,238.2	-1,739.2	-1,221.8
Mixed equity	-546.5	-854.7	-1,277.0	-367.8	-655.8	-1,391.2	-648.4	-636.4
Spanish equity	276.0	-2,219.4	-2,314.4	-940.2	-745.6	-1,561.2	-412.4	-606.9
Foreign equity	2,652.4	1,133.8	-3,342.6	-2,007.2	-2,817.5	-4,553.7	-1,156.9	-1,462.7
Guaranteed fixed-income	-354.4	1,018.9	2,714.6	294.6	1,174.5	1,190.9	1,041.5	979.4
Guaranteed equity	4,693.6	-3,021.1	-3,604.9	-802.2	-1,340.2	-2,564.4	-2,830.0	-2,545.1
Global funds	3,928.2	7,302.1	-6,258.9	-2,864.3	-3,412.9	-6,312.3	-3,183.9	-2,643.7
Funds of hedge funds	-	0.6	1,005.5	221.7	162.6	107.9	215.5	66.1
Hedge funds	-	24.3	164.7	61.8	241.0	113.3	51.4	-5.9
RETURN ON ASSETS								
Total financial mutual funds	11,670.2	12,733.7	6,517.0	-696.7	125.6	-6,045.6	-1,188.8	-1,808.9
Fixed-income	1,837.6	2,260.2	3,073.5	723.6	771.5	599.0	618.0	483.4
Mixed fixed-income	620.3	606.6	271.8	-30.6	15.6	-287.1	-111.9	-98.4
Mixed equity	1,053.4	984.2	261.5	-120.3	-39.4	-645.2	-172.3	-265.3
Spanish equity	1,623.7	2,882.9	768.3	-229.8	215.1	-908.3	-373.4	-394.2
Foreign equity	3,507.1	2,736.1	251.5	-942.1	-905.3	-3,191.1	-372.4	-1,463.8
Guaranteed fixed-income	222.8	112.3	334.7	164.0	42.8	188.7	-11.8	156.2
Guaranteed equity	1,635.5	1,995.2	1,105.8	25.0	144.6	-1,075.9	-719.8	140.2
Global funds	1,169.8	1,156.2	450.2	-286.3	-119.4	-725.7	-45.1	-366.8
Funds of hedge funds	-	0.0	-9.6	-16.7	4.8	5.5	23.3	-29.6
Hedge funds	-	0.1	0.2	-3.9	-5.3	-12.4	7.0	-1.9

Financial mutual funds return on assets. Detail by category

TABLE 3.10

% of daily average total net assets[1]	2005	2006	2007	2007		2008		
				III	IV	I	II	III
MANAGEMENT YIELDS								
Total financial mutual funds	5.87	5.73	3.45	0.02	0.32	-2.24	-0.30	-0.66
Fixed-income	2.31	2.51	3.32	0.79	0.85	0.68	0.71	0.63
Mixed fixed-income	6.18	5.30	2.98	0.11	0.44	-2.17	-0.84	-0.94
Mixed equity	12.96	11.31	4.25	-0.78	-0.01	-8.18	-2.18	-4.36
Spanish equity	20.10	30.10	9.14	-2.13	3.01	-15.02	-6.58	-9.21
Foreign equity	22.82	13.82	2.78	-2.95	-3.19	-18.34	-2.00	-11.67
Guaranteed fixed-income	2.45	1.67	3.25	1.22	1.02	1.16	0.09	0.91
Guaranteed equity	5.26	5.86	3.65	0.44	0.47	-2.32	-1.71	0.78
Global funds	7.41	4.84	2.57	-0.52	-0.07	-2.64	0.09	-1.90
Funds of hedge funds	-	ns	-1.36	-1.83	1.04	0.38	2.86	-1.88
Hedge funds	-	ns	0.57	-1.64	-0.69	-2.38	2.58	-0.31
EXPENSES. MANAGEMENT FEE								
Total financial mutual funds	1.07	1.04	1.00	0.25	0.24	0.23	0.22	0.22
Fixed-income	0.73	0.63	0.61	0.15	0.15	0.15	0.14	0.15
Mixed fixed-income	1.24	1.21	1.13	0.29	0.29	0.29	0.29	0.30
Mixed equity	1.69	1.63	1.54	0.39	0.39	0.38	0.38	0.39
Spanish equity	1.77	1.83	1.59	0.41	0.42	0.42	0.41	0.39
Foreign equity	1.80	1.78	1.70	0.41	0.41	0.42	0.41	0.41
Guaranteed fixed-income	0.77	0.75	0.62	0.17	0.16	0.14	0.13	0.13
Guaranteed equity	1.38	1.34	1.30	0.34	0.34	0.34	0.33	0.33
Global funds	1.41	1.26	1.16	0.25	0.26	0.28	0.27	0.27
Funds of hedge funds	-	ns	1.15	0.42	0.43	0.47	0.42	0.36
Hedge funds	-	ns	1.39	0.09	0.67	0.56	0.61	0.57
EXPENSES. DEPOSITORY FEE[2]								
Total financial mutual funds	0.10	0.09	0.09	0.02	0.02	0.02	0.02	0.02
Fixed-income	0.09	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Mixed fixed-income	0.11	0.10	0.09	0.02	0.02	0.02	0.02	0.02
Mixed equity	0.11	0.11	0.10	0.03	0.03	0.03	0.03	0.03
Spanish equity	0.11	0.11	0.11	0.03	0.03	0.03	0.03	0.03
Foreign equity	0.11	0.11	0.11	0.03	0.03	0.03	0.03	0.03
Guaranteed fixed-income	0.09	0.09	0.08	0.02	0.02	0.02	0.02	0.02
Guaranteed equity	0.11	0.11	0.10	0.03	0.03	0.03	0.03	0.03
Global funds	0.09	0.10	0.10	0.03	0.03	0.02	0.02	0.02
Funds of hedge funds	-	ns	0.06	0.02	0.02	0.02	0.03	0.02
Hedge funds	-	ns	0.33	0.05	0.05	0.04	0.05	0.05

1 The % refers to monthly average total net assets for the Hedge fund category.
2 Instead of the depository fee, the figures for the Hedge fund category refers to the financial expenses.
ns: it is not significant.

Mutual fund quarterly returns. Detail by category

TABLE 3.11

In %	2005	2006	2007	2007		2008		
				III	IV	I	II	III
Total financial mutual funds	5.00	5.59	2.73	-0.15	0.10	-1.96	-0.56	-0.79
Fixed-income	1.53	1.95	2.71	0.63	0.68	0.54	0.57	0.48
Mixed fixed-income	5.00	4.18	1.93	-0.16	0.18	-2.32	-1.29	-1.29
Mixed equity	11.85	10.34	2.69	-1.17	-0.40	-7.56	-2.91	-4.73
Spanish equity	20.60	33.25	8.02	-2.42	2.53	-12.01	-7.66	-9.73
Foreign equity	24.18	14.98	2.13	-2.80	-3.28	-15.06	-2.73	-11.31
Guaranteed fixed-income	1.66	0.83	2.78	1.03	0.84	1.02	-0.01	0.80
Guaranteed equity	3.95	4.66	2.44	0.13	0.12	-2.56	-1.94	0.42
Global funds	6.16	4.01	1.47	-0.70	-0.38	-2.56	-0.29	-2.17
Funds of hedge funds	-	ns	-0.43	-2.14	1.22	-2.31	2.20	-7.56
Hedge funds	-	ns	0.84	-2.20	-1.31	-1.95	1.48	-0.29

ns: it is not significant.

Management companies. Number of portfolios and assets under management

TABLE 3.12

	2005	2006	2007	2007	2008			
				IV	I	II	III	IV[1]
NUMBER OF PORTFOLIOS								
Mutual funds	2,723	2,850	2,954	2,954	2,956	2,968	2,954	2,953
Investment companies	2,989	3,049	3,181	3,181	3,217	3,256	3,261	3,256
Funds of hedge funds	-	2	31	31	38	39	41	41
Hedge funds	-	5	21	21	25	23	25	25
Real estate investment fund	7	9	9	9	9	9	9	9
Real estate investment companies	6	8	9	9	8	8	8	8
ASSETS UNDER MANAGEMENT (Million euro)								
Mutual funds	262,200.9	270,406.3	255,040.9	255,040.9	234,043.9	214,251.8	197,305.6	184,151.4
Investment companies	25,486.0	28,992.7	30,300.0	30,300.0	27,984.8	27,394.2	26,149.4	24,522.3
Funds of hedge funds	-	0.6	1,000.6	1,000.6	1,129.6	1,389.6	1,427.5	1,385.0
Hedge funds	-	24.4	445.8	445.8	546.3	603.9	597.7	576.9
Real estate investment fund	6,476.9	8,595.9	8,608.5	8,608.5	8,563.8	8,394.0	8,166.7	8,175.9
Real estate investment companies	213.9	456.1	512.9	512.9	349.0	359.2	363.8	365.5

1 Available data: October 2008.

Foreign Collective Investment schemes marketed in Spain

TABLE 3.13

				2007		2008		
	2005	2006	2007	III	IV	I	II	III
INVESTMENT VOLUME[1] (Million euro)	33,614.7	44,102.9	37,092.7	44,847.4	37,092.7	30,184.5	28,581.0	22,046.4
Mutual funds	8,267.2	12,099.3	7,010.3	10,530.7	7,010.3	5,004.9	4,313.5	3,064.6
Investment companies	25,347.4	32,003.5	30,082.4	34,316.7	30,082.4	25,179.6	24,267.5	18,981.8
INVESTORS/SHAREHOLDERS	560,555	779,165	850,931	834,914	850,931	729,321	697,732	648,457
Mutual funds	104,089	144,139	142,782	158,925	142,782	137,933	124,446	112,064
Investment companies	456,466	635,026	708,149	675,989	708,149	591,388	573,286	536,393
NUMBER OF SCHEMES	260	340	440	397	440	465	490	535
Mutual funds	115	164	225	197	225	241	253	290
Investment companies	145	176	215	200	215	224	237	245
COUNTRY								
Luxembourg	161	189	229	210	229	241	253	265
France	47	83	122	105	122	127	138	148
Ireland	35	46	52	50	52	59	59	63
Germany	11	12	15	15	15	15	15	16
UK	5	6	12	11	12	13	13	14
The Netherlands	1	1	1	1	1	1	1	1
Austria	-	1	5	1	5	5	5	22
Belgium	-	1	3	3	3	3	5	5
Malta	-	1	1	1	1	1	1	1

1 Investment volume: participations or shares owned by the investors/shareholders at the end of the period valued at that moment of time.

Real estate investment schemes

TABLE 3.14

				2007	2008			
	2005	2006	2007	IV	I	II	III	IV[1]
REAL ESTATE MUTUAL FUNDS								
Number	7	9	9	9	9	9	9	9
Investors	118,857	150,304	145,510	145,510	144,197	141,037	135,307	127,801
Asset (Million euro)	6,476.9	8,595.9	8,608.5	8,608.5	8,563.8	8,394.0	8,166.7	8,175.9
Return on assets (%)	5.35	6.12	1.27	1.27	1.16	0.89	0.35	0.08
REAL ESTATE INVESTMENT COMPANIES								
Number	6	8	9	9	8	8	8	8
Shareholders	256	749	843	843	839	839	938	938
Asset (Million euro)	213.9	456.1	512.9	512.9	349.0	359.2	363.8	365.5

1 Available data: October 2008. In this case, the return on assets is monthly.