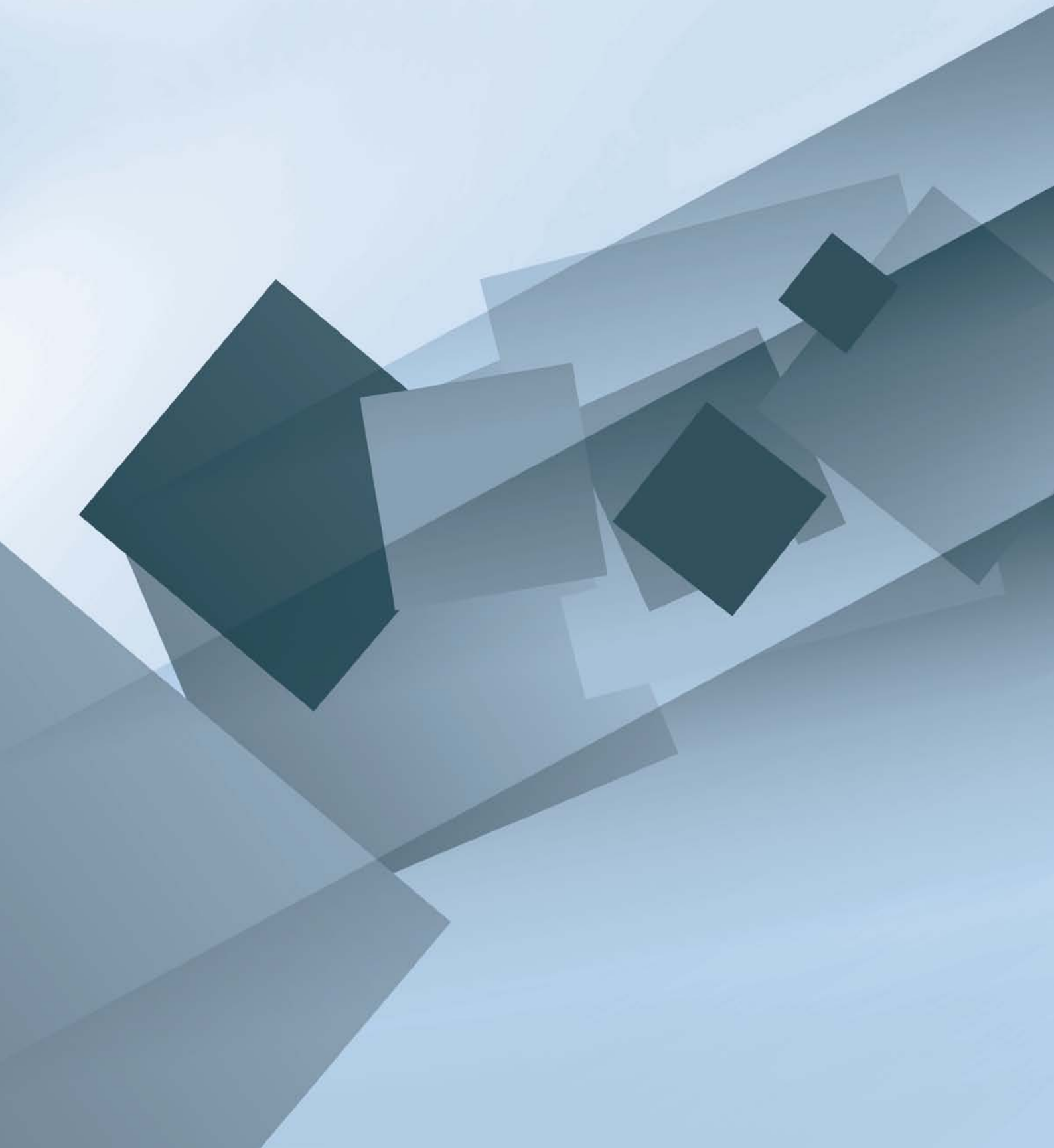




CNMV BULLETIN
Quarter I
2013



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Table of contents

I	Securities markets and their agents: situation and outlook	9
II	Reports and analyses	61
	Empirical study on the bans on short selling in Europe in 2011 and 2012	63
	Carlos Aparicio Roqueiro	
	An analysis of the design and impact on the financial transaction tax	89
	Proposed by the European Commission	
	Ramiro Losada	
	Annual corporate governance report of listed companies in 2011	117
	Sergio Rodríguez and Ángel Domínguez	
III	Regulatory novelties	137
	Financial advisory firms in Spain	139
	Maribel Herrero	
IV	Legislative annex	151
V	Statistics annex	155

Abbreviations

ABS	Asset-Backed Security
AIAF	Asociación de Intermediarios de Activos Financieros (Spanish market in fixed-income securities)
ANCV	Agencia Nacional de Codificación de Valores (Spain's national numbering agency)
ASCRI	Asociación española de entidades de capital-riesgo (Association of Spanish venture capital firms)
AV	Agencia de valores (broker)
AVB	Agencia de valores y bolsa (broker and market member)
BME	Bolsas y Mercados Españoles (operator of all stock markets and financial systems in Spain)
BTA	Bono de titulización de activos (asset-backed bond)
BTH	Bono de titulización hipotecaria (mortgage-backed bond)
CADE	Central de Anotaciones de Deuda del Estado (public debt book-entry trading system)
CCP	Central Counterparty
CDS	Credit Default Swap
CEBS	Committee of European Banking Supervisors
CEIOPS	Committee of European Insurance and Occupational Pensions Supervisors
CESFI	Comité de Estabilidad Financiera (Spanish government committee for financial stability)
CESR	Committee of European Securities Regulators
CMVM	Comissão do Mercado de Valores Mobiliários (Portugal's National Securities Market Commission)
CNMV	Comisión Nacional del Mercado de Valores (Spain's National Securities Market Commission)
CSD	Central Securities Depository
EAFI	Empresa de Asesoramiento Financiero (financial advisory firm)
EBA	European Banking Authority
EC	European Commission
ECB	European Central Bank
ECLAC	Economic Commission for Latin America and the Caribbean
ECR	Entidad de capital-riesgo (venture capital firm)
EIOPA	European Insurance and Occupational Pensions Authority
EMU	Economic and Monetary Union (euro area)
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
ETF	Exchange-Traded Fund
EU	European Union
FI	Fondo de inversión de carácter financiero (mutual fund)
FIAMM	Fondo de inversión en activos del mercado monetario (money-market fund)
FII	Fondo de inversión inmobiliaria (real estate investment fund)
FIICIL	Fondo de instituciones de inversión colectiva de inversión libre (fund of hedge funds)
FIL	Fondo de inversión libre (hedge fund)
FIM	Fondo de inversión mobiliaria (securities investment fund)
FSB	Financial Stability Board
FTA	Fondo de titulización de activos (asset securitisation trust)
FTH	Fondo de titulización hipotecaria (mortgage securitisation trust)

IAASB	International Auditing and Assurance Standards Board
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
IIC	Institución de inversión colectiva (UCITS)
IICIL	Institución de inversión colectiva de inversión libre (hedge fund)
IIMV	Instituto Iberoamericano del Mercado de Valores
IOSCO	International Organization of Securities Commissions
ISIN	International Securities Identification Number
LATIBEX	Market in Latin American securities, based in Madrid
MAB	Mercado Alternativo Bursátil (alternative stock market)
MEFF	Spanish financial futures and options market
MFAO	Mercado de Futuros del Aceite de Oliva (olive oil futures market)
MIBEL	Mercado Ibérico de Electricidad (Iberian electricity market)
MiFID	Markets in Financial Instruments Directive
MMU	CNMV Market Monitoring Unit
MoU	Memorandum of Understanding
OECD	Organisation for Economic Co-operation and Development
OICVM	Organismo de inversión colectiva en valores mobiliarios (UCITS)
OMIP	Operador do Mercado Ibérico de Energía (operator of the Iberian energy derivatives market)
P/E	Price/earnings ratio
RENADE	Registro Nacional de los Derechos de Emisión de Gases de Efectos Invernadero (Spain's national register of greenhouse gas emission permits)
ROE	Return on Equity
SCLV	Servicio de Compensación y Liquidación de Valores (Spain's securities clearing and settlement system)
SCR	Sociedad de capital-riesgo (Venture capital company)
SENAF	Sistema Electrónico de Negociación de Activos Financieros (electronic trading platform in Spanish government bonds)
SEPBLAC	Servicio Ejecutivo de la Comisión de Prevención del Blanqueo de Capitales e infracciones monetarias (Bank of Spain unit to combat money laundering)
SGC	Sociedad gestora de carteras (portfolio management company)
SGEGR	Sociedad gestora de entidades de capital-riesgo (venture capital firm management company)
SGFT	Sociedad gestora de fondos de titulización (asset securitisation trust management company)
SGIIC	Sociedad gestora de instituciones de inversión colectiva (UCITS management company)
SIBE	Sistema de Interconexión Bursátil Español (Spain's electronic market in securities)
SICAV	Sociedad de inversión de carácter financiero (open-end investment company)
SII	Sociedad de inversión inmobiliaria (real estate investment company)
SIL	Sociedad de inversión libre (hedge fund in the form of a company)
SIM	Sociedad de inversión mobiliaria (securities investment company)
SME	Small and medium-sized enterprise
SON	Sistema Organizado de Negociación (multilateral trading facility)
SV	Sociedad de valores (broker-dealer)
SVB	Sociedad de valores y Bolsa (broker-dealer and market member)
TER	Total Expense Ratio
UCITS	Undertaking for Collective Investment in Transferable Securities

I Securities markets and their agents: situation and outlook

Contents

1	Executive summary	13
2	Macro-financial setting	15
	2.1 International economic and financial developments	15
	2.2 National economic and financial developments	23
	2.3 Outlook	31
3	Spanish markets	33
	3.1 Equity markets	33
	3.2 Fixed-income markets	40
4	Market agents	45
	4.1 Investment vehicles	45
	4.2 Investment firms	52
	4.3 UCITS management companies	58
	4.4 Other intermediaries: venture capital	59

List of exhibits

Exhibit 1:	Incorporation of the Asset Management Company for Assets Arising from Bank Restructuring (SAREB)	25
Exhibit 2:	The shadow banking system: latest FSB recommendations	32
Exhibit 3:	Amended legislation on the prospectus and transparency requirements of securities issuers	39
Exhibit 4:	ESMA guidelines on remuneration policies under the Alternative Investment Fund Managers Directive (AIFMD)	49
Exhibit 5:	The CNMV's adoption of the ESMA guidelines on suitability requirements	56

1 Executive summary

- Global economic activity deteriorated with some intensity in the second half of 2012. European economies were the worst affected, due to the contractionary impact of fiscal policy in certain countries, on top of weaker foreign trade and the fallout in the real economy from successive waves of debt market turmoil. In this last sphere, policy actions at national and European level and progress in the ongoing restructuring of the region's financial system have ushered in a calmer mood since summer 2012 which continues to this day.¹ The absence of inflationary pressures in major economic areas has kept official interest rates running at historical lows. And the latest forecasts augur world growth of 3.5% in 2013 and 4.1% in 2014, with emerging market economies again to the fore.
- The performance of international financial markets through second-half 2012 and the first months of 2013 reflected the gradual unwinding of tensions from the peak levels of last July. In debt markets, particularly, the trends associated with recent stress episodes reverted with some force, triggering a run-down in the secondary market yields of the government bonds of more fragile economies and a limited increase in those of the most solid sovereign issuers, accompanied in equity markets by a price surge that has lasted almost straight through from the middle months of 2012. Primary debt markets too recouped some of their dynamism, with private corporates leading the way. Another welcome development has been the remission of credit risk contagion between the public sectors of European economies.
- Spanish GDP contracted by an annual 1.9% in the closing quarter of 2012 for a full-year average of -1.4% (-0.9% and -0.6% respectively in the euro area). Inflation spiked in October at 3.5% due to rising energy prices and the hike in VAT but has since eased substantially (2.8% in February), leaving the differential vs. the euro area at just over one point. Employment shrank by 4.4% in the course of 2012, while the jobless rate reached year-end levels of 26% against a backdrop of falling unit labour costs. The general government deficit closed at nearly 7.0% of GDP (9.4% in 2011), excluding aid to the financial sector, which summed a further 3.3%. Leading forecasters say the Spanish economy will remain in recession through 2013 and manage a small advance in 2014.
- The Spanish financial system is in the thick of a restructuring and recapitalisation drive which has been gathering momentum since last June's ap-

1 The closing date for this report is 15 March.

peal to the EU for financial assistance. As part of the process, banks have begun to transfer their problematic assets to the Asset Management Company for Assets Arising from Bank Restructuring (SAREB). Banking business, meantime, will likely stay slow in the near term due to the weakness of domestic activity.

- The aggregate profits of non-financial listed corporations fell by 45% in full-year 2012 to 12.65 billion euros as activity continued to stagnate. Their debt levels, meantime, dropped by 4.1% to 296 billion euros.
- Spanish equity markets entered a bull phase at end-July 2012 that has continued through the first months of 2013, helped by strongly improving market liquidity and diminished volatility. The Ibex 35 was able to follow up its full-year loss of 4.7% with a 5.5% advance in the first quarter of 2013, mirroring the performance of other key European indices. Gains extended to practically all market sectors and indices, though trading stayed thin by historical standards. The late-July flare-up in debt market turmoil prompted the CNMV, along with its Italian counterpart, to impose a new short-selling ban, which in Spain's case was later rolled over to 31 January 2013.
- Domestic fixed-income markets returned to something like normality in the closing months after the trials of mid-year, and have conserved this calmer mood through the first quarter of 2013. The result has been a sizeable reduction in the short and long bond yields of economic agents, and a narrowing of their credit spreads. In particular, the Spanish ten-year bond was yielding 4.9% at mid-March this year, almost three points below the peak levels of late July 2012 (7.6%), while the spread vs. the German *Bund* was down to 344 bp (against its 635 bp high). There was evidence too of a significant decoupling between the price movements of Spanish government bonds and shares. In primary markets, the volume of debt issues filed with the CNMV expanded 23.8% in 2012 as far as 357.8 billion euros, though the rhythm has noticeably slackened in the first months of 2013.
- Assets under management in investment funds declined by 6.3% in 2012 to 124 billion euros on the sustained flow of unit-holder redemptions (portfolio returns were positive in the period). Liquidity conditions continued to improve, delivering a 1.3 point reduction in the ratio of less-liquid assets as far as 4.3% at the 2012 close. Management companies were able to grow their profits 4.1% thanks to cost contention and increased revenues from sources other than UCITS management. The industry has begun this year on a more buoyant note with some drift over from bank deposits, though constraints on households' saving capacity point to tough times still ahead.
- Investment firm business remained depressed as market turmoil cut heavily into trading volumes, their main income source. The result was a net profits slump of 78% to 50.3 million euros, and a sharp deterioration in the earnings figures of loss-making firms, though their numbers did not increase. The number of firms on the register also reduced further in 2012, even though bank sector restructuring has so far exerted only a limited impact in corporate terms. Solvency conditions, meantime, continued in the comfort zone.

- The report includes five exhibits:
 - The first sets out the main characteristics and operational mechanisms of the newly constituted Asset Management Company for Assets Arising from Bank Restructuring (SAREB).
 - The second runs through the key conclusions of the FSB's analysis on five targeted areas of shadow banking activity.
 - The third exhibit summarises recent legislative changes affecting the prospectus and transparency requirements applicable to securities issuers.
 - Exhibit four considers the key elements of ESMA's recently approved guidelines on the remuneration policies of alternative fund managers in the light of the Alternative Investment Fund Managers Directive (AIFMD).
 - Finally, the fifth offers a description of ESMA's 2012 guidelines clarifying certain aspects of MiFID suitability requirements and the steps taken by the CNMV to facilitate company compliance.

2 Macro-financial setting

2.1 International economic and financial developments

The international financial climate has improved modestly since the third quarter of 2012, particularly among the economies worst hit by the debt crisis, giving new impetus to equity markets and restoring risk premiums to more manageable levels. Meantime, capital flows to emerging market economies have been gaining momentum. In Europe, the austerity programmes launched by governments, the restructuring of the financial systems most damaged by the crisis, and a series of EU-level decisions to preserve financial stability throughout the zone, have dispelled part of the uncertainty weighing on market agents.

The international financial climate has brightened somewhat in these past months...

After surprising on the upside in the third quarter, activity again appeared to soften as the year drew to a close. GDP growth was uneven across the main economic regions. Advance was strongest in the United States and Japan, with rates nearing 2%, and the emerging markets, with a combined rate ahead of 5%. In Europe, something of a gap emerged between the core economies, especially Germany and France, which outperformed in the opening quarters, and the periphery countries, which stayed stuck in recession for almost all of 2012 (see table 1).

...though activity remains sluggish, especially in Europe.

Inflation in main advanced economies has held more or less steady² after the steep run-down of the first six months, to begin 2013 with rates ranging from 1.6% in the United States to 2.7% in the United Kingdom. The outlier was again Japan, with

Persistently low-key inflation in advanced economies ...

² In the euro area, annual inflation has fallen more sharply from 2.5% in October 2012 to 1.8% in February 2013.

full-year inflation of zero percent. Consumer price stability was favoured by domestic demand weakness in most economies and lessening pressure from commodity prices, especially energy. Core inflation too held to an even course, with only occasional spikes in some economies due to tax measures or hikes in tariff prices.

Gross domestic product (annual % change)

TABLE 1

	2009	2010	2011	2012	IMF ¹	
					2013F	2014F
World	-0.7	5.3	3.9	3.2	3.5 (-0.1)	4.1 (-0.1)
United States	-3.0	2.4	1.8	2.2	2.0 (-0.1)	3.0 (0.1)
Euro area	-3.8	2.0	1.6	-0.5	-0.2 (-0.3)	1.0 (-0.1)
Germany	-5.1	4.0	3.1	0.9	0.6 (-0.3)	1.4 (0.1)
France	-3.0	1.6	1.7	0.0	0.3 (-0.1)	0.9 (-0.2)
Italy	-5.5	1.8	0.6	-2.2	-1.0 (-0.3)	0.5 (=)
Spain	-3.7	-0.3	0.4	-1.4	-1.5 (-0.1)	0.8 (-0.2)
United Kingdom	-3.9	1.8	0.9	0.0	1.0 (-0.1)	1.9 (-0.3)
Japan	-5.5	4.7	-0.5	1.9	1.2 (=)	0.7 (-0.4)
Emerging	2.8	7.5	6.3	5.1	5.5 (-0.1)	5.9 (=)

Source: IMF, Thomson Datastream and Eurostat.

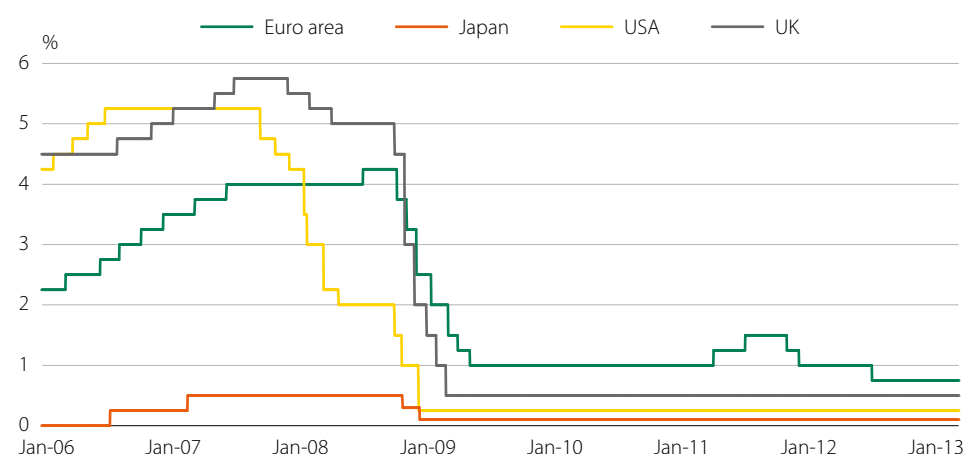
1 In brackets, change with respect to the last published forecast. IMF, forecast published January 2013 versus October 2012.

...allows interest rates to be kept at lows.

With inflation expectations anchored at low levels in most major economies, official interest rates were either left untouched versus mid-year 2012 or lowered even further, as in the case of the euro area.³ Official rates in the United States, euro area, United Kingdom and Japan closed February 2013 at historical lows of 0.25%, 0.75%, 0.5% and 0.1%, respectively. As previous years, unconventional measures were the monetary instrument of choice, primarily the purchase of financial assets.

Official interest rates

FIGURE 1



Source: Bloomberg. Data to 15 March.

3 The ECB cut official euro-area rates by 25 bp to 0.75% at the start of July 2012.

Tensions on international financial markets have lessened considerably since the third quarter of 2012, particularly in Europe. Easier financing conditions have allowed the most elevated sovereign spreads to come down appreciably, boosted prices on equity markets, and helped reopen debt markets for Europe's banks, which were able to scale back their recourse to Eurosystem funding. A number of factors underlie this improvement. Some relate to the ECB's decision to do "whatever is needed" to preserve the single currency, particularly its announcement of a conditional bond-buying program, and declarations by EU leaders on the need to advance towards banking and fiscal union. Equally vital have been the fiscal austerity programmes set in train by many euro-area economies.

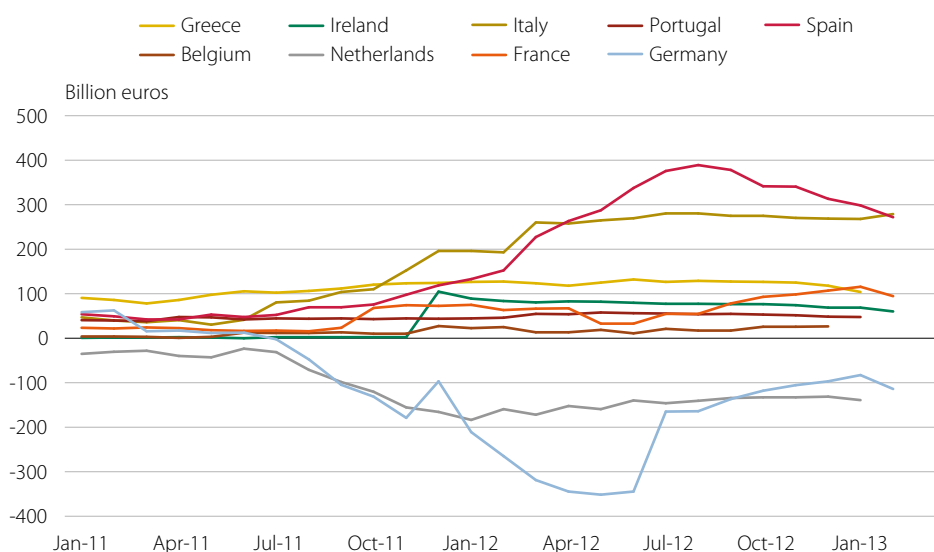
Policy actions in Spain and Europe have calmed the mood on financial markets since the third quarter of 2012...

Gross borrowing from the Eurosystem has fallen slightly in recent months on banks' more fluid access to debt markets, though levels remain elevated (above 1.1 trillion euros). As we can see from figure 2, net creditor and debtor positions by country have evolved towards a lesser reliance by Spanish banks and more stable borrowings by their Italian peers. Though entities have repaid almost 236 billion euros of the total borrowed in the ECB's two special long-term refinancing operations (LTROs) of 22 December 2011 and 1 March 2012, the cost of this kind of funding remains very advantageous for those European banks not yet able to tap primary markets in conditions of normality.

...and allowing the region's banks to rely a little less on Eurosystem funding.

(Net) Eurosystem funding

FIGURE 2



Source: Bloomberg, Banco de España and Bank of Greece. Data to February for Spain, Italy, France, Germany and Ireland, and to January for remaining countries except Belgium (December). In Greece's case, the data refer to the net liabilities of OMFIs (other monetary financial institutions) with the Bank of Greece, which factor not only Eurosystem borrowings but also the Emergency Liquidity Assistance (ELA) which provisionally replaced Eurosystem funding.

In long-term debt markets, the more settled mood of late 2012 and the first months of 2013 has taken some of the strain off the sovereign bond yields of more vulnerable economies, while prompting a limited increase in safe-haven yields. As figure 3 shows, the main beneficiaries were the Portuguese and Irish bonds, whose yields dropped to mid-March levels of around 6% and less than 4% respectively. Both countries, moreover, have successfully renewed their issuance programmes on pri-

Government bond yields fall in more fragile economies as market tensions abate...

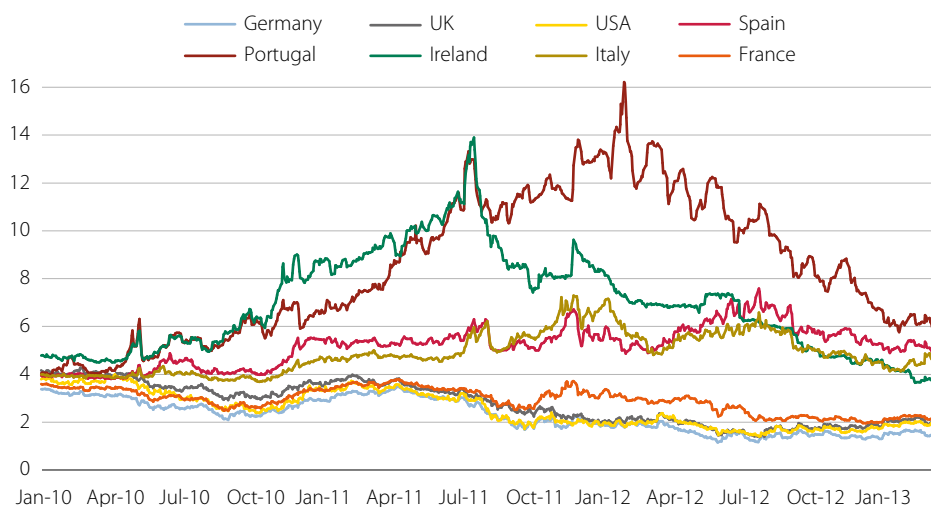
mary markets⁴ following receipt of European financial assistance. Meantime, yields on Spanish and Italian bonds, the worst affected by the last bout of market turbulence, receded more than two points from mid-2012 highs as far as 4.9% and 4.6% respectively at the closing date for this report.

Finally, 10-year German, UK and U.S. yields, which had registered record lows of around 1.15%, 1.38% and 1.40% respectively at the height of market tensions, tended to stabilise or move slightly higher in the first weeks of 2013. By mid-March, their yields were oscillating between the 1.5% of the German *Bund* and the 2% of the U.S. benchmark.

...accompanied by limited rises in the yields of safe-haven economies ...

Ten-year government bond yields

FIGURE 3



Source: Thomson Datastream. Data to 15 March.

...the combined result being a substantial decrease in risk spreads on sovereign debt...

The sovereign risk spreads of a wide set of European economies, as derived from yield spreads and CDS premiums, have receded with force in recent months in line with government bond yields. As we can see from figure 4, the 5-year CDS of Spanish and Italian bonds⁵ dropped below 300 bp around mid-March in contrast to the 600 bp peaks of July 2012, while those of sounder European economies crept below 200 bp. In some cases, these CDS spreads marked a return to the levels preceding the first turbulence outbreak of 2010.

...and less contagion of sovereign credit risk.

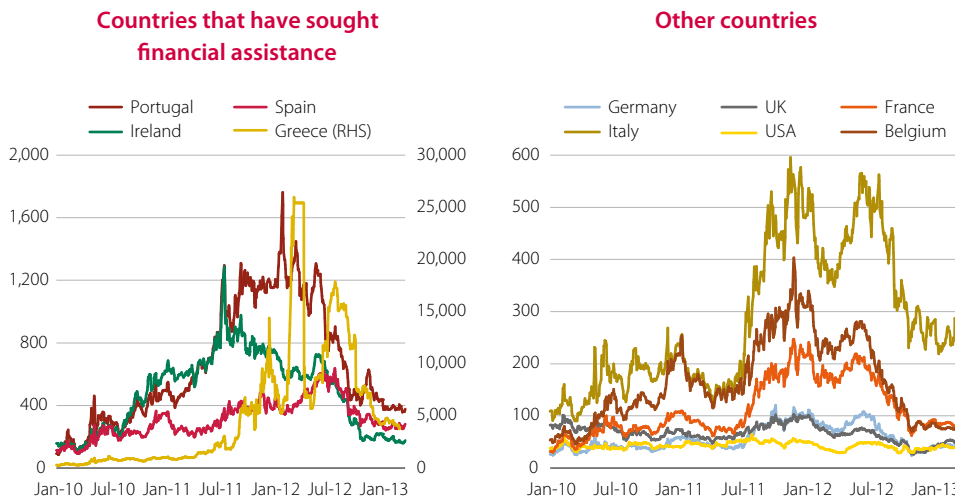
In this more benign risk climate, contagion indicators point to a dwindling spillover between euro-area public sectors, and between the financial and sovereign sector (see figure 5).

4 Generally, the bonds placed had maturities below five years, except one Irish issue in the ten-year tenor.

5 In Italy, the political vacuum opened up after the general elections of 24 and 25 February and Fitch's announcement on 8 March that it would downgrade the country's debt (from A- to BBB+ with a negative outlook) have partially reversed the downtrend in bond yields and risk spreads. In effect, political uncertainty and a stalled policy of structural reforms have dealt an adverse shock to the recession-mired Italian economy, and are the reasons behind its revise-down, the agency says.

Sovereign credit spreads, 5-year CDS

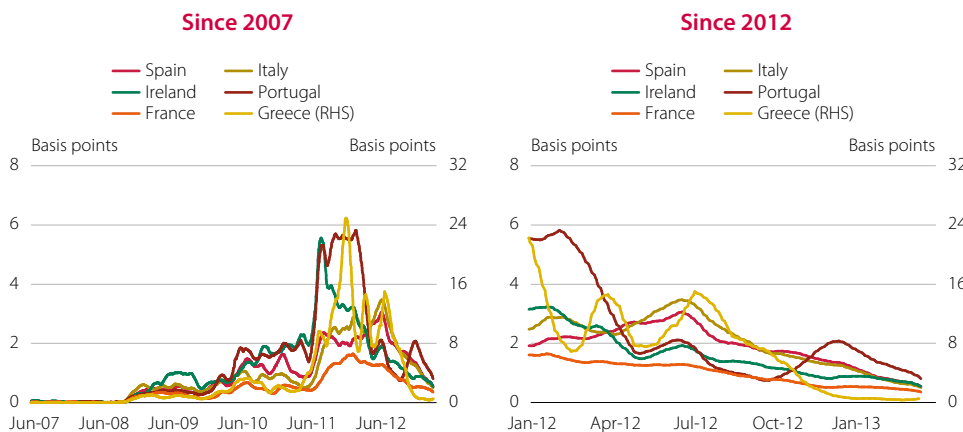
FIGURE 4



Source: Thomson Datastream. Data to 15 March.

Sovereign credit risk contagion in the euro area¹

FIGURE 5

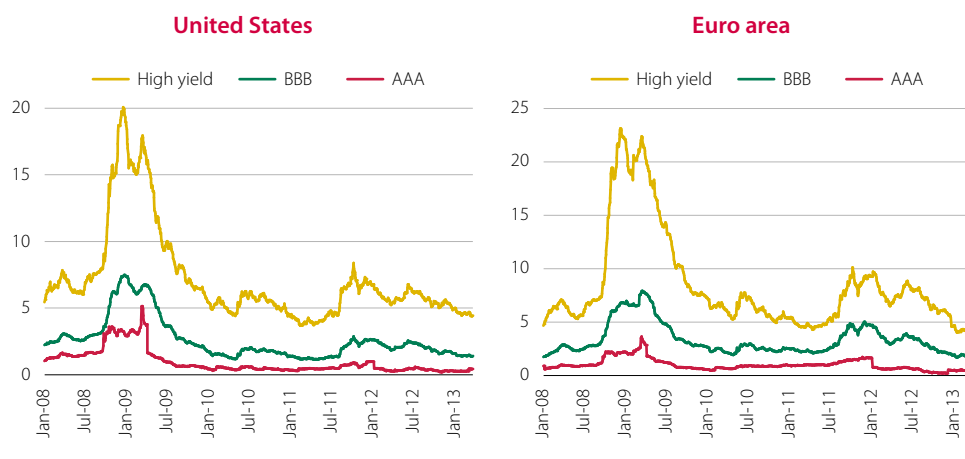


Source: Thomson Datastream and CNMV. Data to 15 March 2013.

- 1 Defined as the impact on German sovereign CDS of contemporaneous shocks in the CDS of Spain, Italy, Ireland, Portugal, Greece and France equivalent to 1% of the CDS spread at that point in time. Results are the product of two components. The first measures the degree of contagion from one country to another taken as the percentage change in the German sovereign CDS that is exclusively explained by a contemporaneous variation in the CDS spread of one of the above six countries. This percentage is based on the decomposition of the variance of the estimated prediction error using an autoregressive vector model (ARV) with two variables – the impacted variable (change in the German sovereign CDS) and the shock-generating variable (change in the sovereign CDS of Spain, Italy, Ireland, Portugal, Greece or France) – and two retardations. Estimates are implemented through a moving window of the one hundred periods prior to the first prediction period. The second component measures the credit risk of the shock emitter, as approximated from its CDS. Finally, the resulting series is smoothed using a moving average of thirty trading sessions.

The sovereign debt crisis unfolding in Europe over the last few years has not only fuelled a flight to quality into the bonds of safer economies; it has also piled investors into private corporate debt. As we can see from figure 6, heavy buying of corporate bonds has helped to contain their risk spreads, even through periods of stress, while tempting corporate borrowers back to the markets in both the United States and Europe.

Corporate debt markets boom...

Spread vs. the 10-year government bond, in basis points¹

Source: Thomson Datastream and CNMV.

¹ In the euro area, versus the German 10-year benchmark.

...and bank sector issuance picks up slightly. Public debt issuance, meantime, continues in retreat.

Net issuance on international debt markets summed 4.6 trillion dollars in the full-year period, 22.2% less than in 2011. The decline traced to lower net sovereign debt issuance (down 17% to 3.6 trillion dollars), as countries persevered with fiscal tightening, and, in smaller measure, to the stall in financial institution placements in the year's opening months. As figure 7 shows, the net debt financing (less redemptions) of financial institutions in the United States and Europe stayed negative through 2012, albeit with modest improvement in the second half as market tensions eased. By instrument, outright issuance of both investment-grade and high-yield instruments picked up strongly in the year, while asset-backed securities (ABS) gained new steam, especially in the United States. But the main mover on primary markets was the non-financial corporate sector, with a deluge of sales that exceeded one trillion dollars, more than double the total of 2011, and breaking down 37% from U.S. and 32% from European issuers.

The primary debt market trends have been prolonged into 2013.

Data for the opening months of 2013 point to the persistence of these trends, i.e., a decrease in public debt issuance, a tentative return by the banks, and a sales boom in the corporate sector.

Leading stock indices began the year in bullish mood, with gains strongest in the U.S. and Japan,...

After a year that closed with most indices posting gains ahead of 10%, the stock markets of major advanced economies prolonged their bull run into 2013, with U.S. and Japanese indices leading by a comfortable margin (up nearly 10% and over 20% to mid-March respectively). In the United States, support came from the country's more buoyant activity, but also the agreement reached around the "fiscal cliff" and further stimulus from the Federal Reserve.⁶ Among the European indices, gains ranged from the 0.7% of Italy's Mib 30 to the 10% of the UK's FTSE 100 (see table 2). The more settled climate of the past few months has certainly boosted shares to some extent, but the weakness of growth, as confirmed by fourth-quarter data, continues to weigh on equity markets worldwide.

⁶ The most important being the September announcement of its third balance-sheet expansion programme (QE3), the December rollover of the government bond buying programme and, especially, its decision to keep interest rates low while unemployment is above 6.5%.

Net international debt issuance

FIGURE 7



Source: Dealogic. Half-year data. Data for the first half of 2013 run to 15 March, but are restated on a semi-annual basis to facilitate comparison.

Volatility in world equity markets has stayed subdued in recent months, despite creeping higher in Europe from early February on. In all, levels of historical and implied volatility are consistent with those we might expect in the absence of market turbulence.

...at a time of reduced volatility.

Performance of main stock indices¹

TABLE 2

%	2009	2010	2011	2012	1Q12	2Q12	3Q12	4Q12	1Q13 (to 15 March)			
									% prior qt.	% Dec	% y/y ²	
World												
MSCI World	27.0	9.6	-7.6	13.2	10.9	-5.8	6.1	2.1	7.9	7.9	9.4	
Euro area												
Euro Stoxx 50	21.1	-5.8	-17.1	13.8	6.9	-8.6	8.4	7.4	3.4	3.4	4.5	
Euronext 100	25.5	1.0	-14.2	14.8	8.3	-4.7	5.0	6.0	6.4	6.4	8.8	
Dax 30	23.8	16.1	-14.7	29.1	17.8	-7.6	12.5	5.5	5.7	5.7	12.4	
Cac 40	22.3	-3.3	-17.0	15.2	8.4	-6.6	4.9	8.5	5.6	5.6	6.9	
Mib 30	20.7	-8.7	-24.0	10.2	7.9	-11.3	8.6	6.0	0.7	0.7	-2.8	
Ibex 35	29.8	-17.4	-13.1	-4.7	-6.5	-11.3	8.5	6.0	5.5	5.5	1.6	
United Kingdom												
FTSE 100	22.1	9.0	-5.6	5.8	3.5	-3.4	3.1	2.7	10.0	10.0	8.8	
United States												
Dow Jones	18.8	11.0	5.5	7.3	8.1	-2.5	4.3	-2.5	10.8	10.8	9.7	
S&P 500	23.5	12.8	0.0	13.4	12.0	-3.3	5.8	-1.0	9.4	9.4	11.1	
Nasdaq-Cpte	43.9	16.9	-1.8	15.9	18.7	-5.1	6.2	-3.1	7.6	7.6	6.3	
Japan												
Nikkei 225	19.0	-3.0	-17.3	22.9	19.3	-10.7	-1.5	17.2	20.8	20.8	24.0	
Topix	5.6	-1.0	-18.9	18.0	17.3	-9.9	-4.2	16.6	22.3	22.3	21.3	

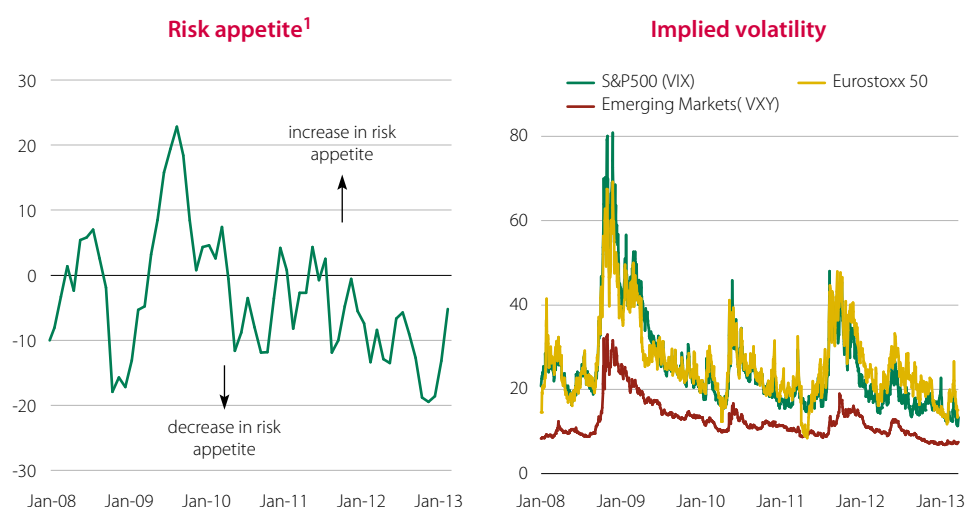
Source: Datastream.

1 In local currency.

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

Financial market indicators

FIGURE 8



Source: Thomson Datastream and CNMV.

1 State Street indicator.

2.2 National economic and financial developments

According to the latest Quarterly National Accounts data for the closing quarter of 2012, the national economy slowed by a further 0.5 points quarter on quarter to -0.8%, and by 0.3 points to 1.9% in year-on-year terms. On these results, real GDP contracted 1.4% in 2012, compared to the 0.4% growth of 2011. The activity stall was comparable to elsewhere in the euro area, where growth sank by 0.5 points to -0.6% quarter on quarter and by 0.3 points to -0.9% year on year.

Spain's GDP contracts 0.8% in the fourth quarter of 2012, for a full-year decline of 1.4%,...

The steeper fourth-quarter decline in activity reflected the ailing state of domestic demand, which detracted 4.7 points from GDP growth (-4.0 points in the third quarter). The contraction moreover extended to all components. In particular, private consumption declined by 3% in year-on-year terms (-2.1% vs. the prior quarter), due in part to consumers bringing forward purchases ahead of the September hike in VAT. Government consumption, meantime, decelerated by an additional point to -4.1% year on year. Finally, gross fixed capital formation dropped 0.5 points for a year-on-year rate of -10.3%. The equipment component lost a further point to 7.9%, while construction investment, down 12.3%, managed to smooth its decline by one decimal point.

...as more rapidly deteriorating domestic demand...

Net exports went some way to offsetting the extractive effect of domestic demand, with a positive contribution of 2.8 points (2.4 points in the previous quarter). Improvement here traced to faster falling imports, down from -3.4% to -5.4% year on year, while exports slowed their advance by one point to 3.2%, in response to the growth stall in Spain's main export market, the European Union.

...cancels out the positive input from the net exports side.

On the supply side, all sectors except agriculture, hunting and forestry, closed the fourth quarter in negative terrain. Industrial production slowed its rate of decline by 0.5 points to -2.9% year on year, but manufacturing industry contracted 0.2 points more than in the preceding quarter, as far as -3.6%. The decline in construction levelled off at -8.5%, improving 0.4 points on the previous quarter, and, finally, services shrank by a further 0.6 points to -1.2%. The largest decreases under this last head corresponded to financial and insurance activities, along with retail, transport, and hotels and catering. Finally, the primary sector, the only one in positive rates, saw growth decelerate 0.5 points to 1.9% in year-on-year terms.

All supply-side sectors, except agriculture, hunting and forestry, lost ground in the closing quarter.

Spanish inflation spiked in October at 3.5%, due to hikes in VAT and tariff prices, and renewed pressures from the energy component, but has since eased back to a February rate of 2.8% (2.7% in January). Core inflation too reached an October peak of 2.5%, then fell to 2.1% in December, before creeping back to 2.3% in February 2013. Spain's inflation differential with the euro area, which was negative over the first half of 2012, closed completely in August and has since widened steadily to 1.1 points.

Inflation rates have retreated from October highs thanks to lower energy taxes.

The latest figures on employment and joblessness confirm the parlous state of Spain's labour market. Employment, specifically, deteriorated by a further 0.1% as far as -4.7% year on year in the closing quarter (-4.4% in full-year 2012). This is equivalent to the net destruction of 805,000 jobs in one year. The unemployment rate climbed to 26% in the fourth quarter (25% in the third and 22.9% in the year-ago period), while the number of households with all members out of work rose by 258,700 to 1,833,700. Unit labour costs, finally, prolonged their descent (-3.4% in 2012) on higher productivity per worker (up by 3.2%) and a small decline in employee wages (-0.3%).

In the labour market, the year ended with employment down by 4.7% and the unemployment rate at 26%.

Spain: main macroeconomic variables (annual % change)

TABLE 3

	2009	2010	2011	2012	IMF ¹		EC ²	
					2013F	2014F	2013F	2014F
GDP	-3.7	-0.3	0.4	-1.4	-1.5	0.8	-1.4	0.8
Private consumption	-3.8	0.7	-0.9	-2.2	-2.4	0.7	-2.7	-0.2
Government consumption	3.8	1.5	-0.5	-3.7	-5.5	-1.4	-5.4	-1.1
Gross fixed capital formation, of which:	-17.9	-6.2	-5.3	-9.1	-5.8	-1.3	-6.6	-1.0
Construction	-16.6	-9.8	-9.0	-11.5	-7.6	-1.2	n.a.	n.a.
Machinery and equipment	-23.6	2.7	2.4	-6.6	-4.2	-1.8	-3.0	0.1
Exports	-9.8	11.2	7.7	3.0	3.9	4.1	4.2	5.7
Imports	-16.8	9.3	-0.8	-5.0	-3.1	1.6	-3.8	2.0
Net exports (growth contribution, p.p.)	2.5	0.3	2.3	2.5	2.1	0.9	2.6	1.3
Employment³	-6.3	-2.5	-1.7	-4.4	-2.4	1.6	-3.1	0.0
Unemployment rate	18.0	20.1	21.6	25.0	27.0	26.0	26.9	26.6
Consumer price index	-0.3	1.8	3.2	2.4	2.0	1.4	1.7	1.0
Current account balance (% GDP)	-4.8	-4.5	-3.5	-0.8	0.4	1.0	1.0	2.5
General government balance (% GDP)⁴	-11.2	-9.7	-9.4	-10.0	-6.4	-6.7	-6.7	-7.2
Public debt (% GDP)	53.9	61.5	69.3	83.9	93.2	98.7	95.8	101.0
Net lending (+)/borrowing (-) vs. the rest of the world (% GDP)⁵	-93.7	-88.9	-91.8	-92.9	-92.1	-88.8	n.a.	n.a.

Source: Banco de España, IMF and National Statistics Office (INE).

1 IMF forecasts of January 2013.

2 European Commission forecasts of February 2013.

3 In full-time equivalent jobs.

4 Figures for 2011 and 2012 include government aid to credit institutions amounting to 0.5% and 3.3% of GDP respectively.

5 The net lending/borrowing position of 2012 corresponds to the IMF forecast of January 2013.

n.a.: not available.

The general government deficit closed at 10% of GDP, of which 3.3 points were aid to the financial sector.

According to provisional budgetary execution figures, the general government deficit, excluding aid to the financial sector, closed the year at 70.82 billion euros, 6.7% of GDP, improving on the previous year's 95.27 billion (9% of GDP), likewise discounting the said aid.⁷ Breaking down the deficit figure by branch of government, we find the largest overspend in central government accounts (3.8% of GDP against 3% in 2011), followed by the autonomous communities (1.7% of GDP against 5% in 2011), local authorities (0.2% against 0.8% respectively) and Social Security (1% against 0.1%). Aid to financial institutions summed 3.3% of GDP in 2012 (0.5% in 2011), lifting the general government deficit as far as 10% (9.4% in 2011). Finally, general government debt swelled to 84.1% of GDP from 69.3% in 2011.⁸

7 In March, Eurostat, the EU statistics office, located Spain's general government deficit for 2012 at 6.98% of GDP excluding aid to the financial sector.

8 This 14.8 point increase in the 2012 public debt ratio responded mainly to the gap between expenditure and revenues (including interest expenses on public debt and aid to the financial sector), but other factors also intervened. Chief among them: i) the EFSM loan channelled through the FROB to recapitalise Group 1 credit institutions and provide capital to SAREB; ii) the Fund for the Financing of Payments to Suppliers (FFPP in its Spanish initials); iii) Spain's contribution to the European Financial Stability Facility (EFSF); iv) the issues of the Electricity Deficit Amortisation Fund (FADE in its Spanish initials); and, v) the 1.1% contraction in nominal GDP. It bears mention that the creation of the Regional Liquidity Fund (FLA in Spanish) will not add to the public debt, since the funds it raises for central government will be used to finance the redemption of autonomous community outstanding debt and cover their funding needs, thereby consolidating the cross-transfer of funds between central and regional government.

Exhibit 1: “Incorporation of the Asset Management Company for Assets Arising from Bank Restructuring (SAREB)”

SAREB was set up in November 2012 further to the memorandum of understanding on the provision of financial support to the Spanish banking system agreed between the Spanish and European authorities in July 2012.¹ Its corporate purpose is essentially the acquisition, efficient management and orderly disposal of the impaired real estate assets held by credit institutions in receipt of state aid, optimising their value while mitigating, as far as possible, their negative impact on Spanish economic agents.

SAREB has been incorporated as an unlisted public limited company under the supervision of the Banco de España, with a maximum duration of 15 years.² As regards financial structure, SAREB will draw its own funds from share capital and subordinated debt, but may also finance its activity through debt issues secured by the Spanish state.³ This debt will be subscribed for by credit institutions with assets transferred to SAREB and will be eligible as collateral for ECB credit operations. SAREB debt will be tradeable on the AIAF fixed-income market.

The company’s board of directors comprises fifteen members (five independent directors, four of them appointed by the FROB, and the remainder nominated by private investors), under a regime similar to that established for credit institution board members by Royal Decree 1245/1995. The same conditions will also apply to general managers and other senior executive officers. Its operations will be subject to the control of a series of committees, including a Monitoring Committee.

Given the difficulties of bringing SAREB’s management capabilities up to steam in a relatively short time, the day-to-day management of the transferred assets will initially correspond to the transferring entities, who will nonetheless hold no discretionary powers in their respect. The corresponding services will then be progressively contracted out to providers selected by procurement.

Assets will be divested through bank asset funds (BAFs), which are separate blocks of assets, without legal personality, composed of the assets and liabilities transferred to them by SAREB. These BAFs may be organised into independent compartments and are authorised to issue securities or contract other obligations against the assets held in each. They must also register with the CNMV, and their management and representation must be entrusted exclusively to a securitisation fund manager which meets the requirements contained in Law 9/2012 and its implementing regulations, under the continuing supervision of the CNMV.

SAREB will be governed by the requirements of the Capital Enterprises Law as regards the drawing-up of annual accounts, but may not elect to file abridged financial statements. It will also prepare a business report every six months setting out the essential information related to its activities during this period, the extent to which the targets established in its business plan have been met and explanations for any deviations from those targets. It will send this report to the Banco de España and the SAREB Monitoring Committee, who may call for any supple-

mentary disclosures they deem necessary. SAREB must also make all mandatory information regarding its annual accounts and management report publicly available.

The assets to be transferred to SAREB consist of foreclosed real estate assets with a net book value, after valuation adjustment, exceeding one hundred thousand euros, loans to property developers whose net book value exceeds two hundred and fifty thousand euros, and instruments representing the share capital of real estate sector companies which confer joint control or a significant influence. The FROB is also empowered to order the transfer of consumer or SME loans, home purchase mortgages and any assets whose degree of impairment could jeopardise the transferrer's viability, following a report from the Banco de España. In this first phase, the value of the total assets transferred to SAREB cannot exceed 90 billion euros, though the door is left open to raise this limit subject to a favourable report from the FROB.

The Banco de España determines the transfer value of the assets acquired by the SAREB on the basis of their estimated economic value minus certain discounts.⁴ These additional adjustments means the transfer prices set for SAREB acquisitions do not automatically stand as a valuation benchmark for the real estate assets of non-segregating financial institutions. The average transfer price estimated by Banco de España represents a discount of around 63% over the book value of the assets (79.5% for land, 63.2% for ongoing uncompleted developments and 54.2% for completed homes). In the case of funding to developers, the average discount will be a lower 45.6%, including adjustments of 32.4% for completed projects and 53.6% for loans granted to finance urban land.

On a conservative estimate, the SAREB is expected to obtain a return on equity (ROE) over its lifetime of an annual 14%. It has so far acquired assets from Group 1 banks with a gross book value of 71 billion euros, comprising 54 billion in developer loans and 17 billion in foreclosed properties.⁵ In exchange, the transferring entities have received SAREB issued debt for the sum of 37 billion euros. The difference between this last amount, reflecting the cash value or transfer price of the assets taken on, and their gross carrying value produced a hole of 34 billion euros, which was filled through a 37 billion euro injection of public funds (via the FROB) borrowed from the European Financial Stability Mechanism (EFSM). Removing these problematic assets from bank balance sheets, including "doubtful" property developer loans, took a sizeable chunk from the December balance of bank non-performing loans (down 24 billion to 167 billion euros), lowering the NPL ratio by one full point to 10.4%.

1 SAREB was incorporated under Law 9/2012 of 14 November, on the restructuring and resolution of financial institutions and its implementing regulation, Royal Decree 1559/2012 of 15 November on the legal regime applying to asset management companies.

2 The state's participation (through the FROB) in SAREB's capital may at no point exceed 50%. The company, accordingly, is not consolidated in general government accounts, but appears in the category of non-monetary financial institution under "Other financial intermediaries" beside the likes of securitisation funds and broker-dealer firms.

3 To prepare it for receiving the impaired assets of Group 1 (nationalised banks) and Group 2 (banks with capital shortfalls unable to meet them without recourse to state aid), SAREB was set up with own funds of 4.80 billion euros, comprising 25% share capital (1.20 billion euros, 55% from private investors and

the rest from the FROB) and subordinated debt (3.60 billion in mandatorily convertible bonds, 54% placed with private investors and the rest acquired by the FROB). Own funds raised amount to 9.4% of the cash value of assets under management (51 billion euros).

- 4 Estimates of economic value start from the baseline scenario of the stress tests conducted by consultancy firm Oliver Wyman, completed in September 2012, which used a valuation horizon of two years. Discounts applied allow for the longer duration of the SAREB business plan (15 years), the market volatility of the transferred assets, the associated operating and interest expenses, discounts on block portfolio disposals, execution costs, the cost of recovering delinquent loans and general expenses.
- 5 The gross book value of the assets transferred to the SAREB by Group 2 entities stood at 20 billion euros in February 2013, compared to a transfer value of 14 billion euros. Their acquisition was financed through the issue of SAREB senior debt.

The Spanish financial sector again had to fight on two fronts: the business weakness brought about by the stall in domestic activity and the broader process of sector recapitalisation and restructuring, which moved up a gear in June 2012 with the request for financial assistance from the EU. By year end, the financial institutions with the severest capital shortfalls, according to the stress tests run in summer 2012, had transferred impaired assets to the Asset Management Company for Assets Arising from Bank Restructuring (SAREB) for the amount of 51 billion euros (see exhibit 1). Of the capital shortfalls identified, summing 56 billion euros in the worst-case scenario, 39 billion correspond to state aid via the FROB's purchase of shares and subordinated debt.⁹

Spanish financial institutions in the thick of a restructuring process,...

Sector restructuring weighed on banks' income statements through 2012, as they provisioned heavily against impairment losses (on financial and, to a lesser extent, non-financial assets). The result was a sector-wide loss of almost 85 billion at the pre-tax profit line, despite minor improvement in gross operating income, up from 57 billion in 2011 to 59 billion at the 2012 close, and a two billion reduction in operating expenses to 27 billion euros. It seems likely, however, that sector income statements will now recover some of their lost form, with the system recapitalised and problematic assets taken off the balance sheets of ailing banks.

...characterised by hefty impairment losses on financial and non-financial assets ...

Lending to non-financial private sectors tailed off increasingly through the second half of 2012 and first months of 2013,¹⁰ with the January rate down to -5.3% year on year (-2.2% in January 2012). The finance reaching non-financial corporations shrank by 6.3%, while loans to households dropped by a lower 3.7%. In straight number terms, this equates to a 150 billion decrease in loans outstanding over full-year 2012. As regards the euro area, the latest data point to some contraction in consumer credit to business and households, albeit less so than in Spain, and some timid expansion in home purchase loans. Spanish non-financial corporations were again able to counter the dearth of bank finance by tapping capital markets, with a preference for fixed-income instruments. The result was year-on-year growth in outstanding debt securities of 13.5% to January 2013 (contrasting with an 8.5% decrease in bank credit).

...and a sharp decline in lending to business and households.

9 Remaining measures to make up the full amount of the shortfall, primarily those concerning the management of hybrid and subordinated debt instruments and private capital raising efforts, are set out in the IMF report Spain: *Financial Sector Reform – Second Progress Report*, of March 2013.

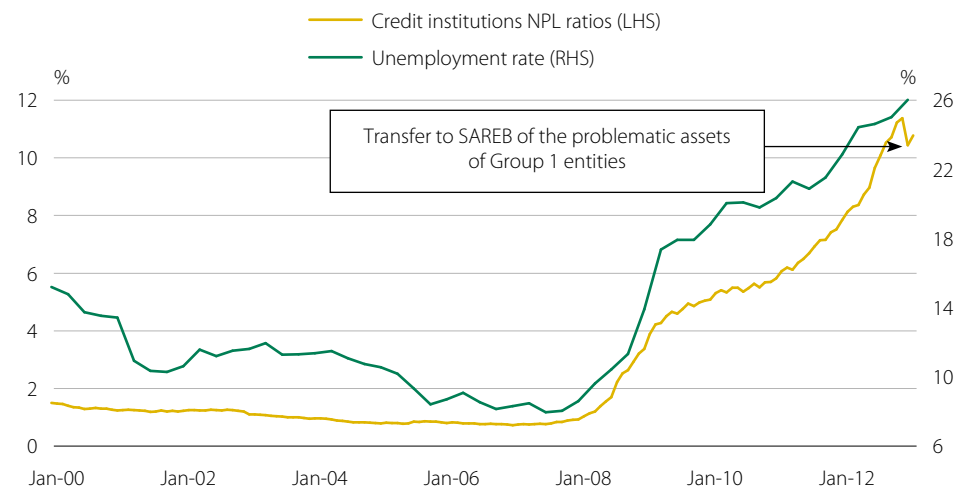
10 The figures referred to include loans transferred to the SAREB. This company's absorption of a large volume of private-sector loans make it a key actor in any analysis of the financing of the Spanish economy.

Financial sector NPL ratios fall 1% in December to 10.4% as problematic assets start being hived off to SAREB.

Credit institution NPL ratios rose 0.4 points in January to 10.8%. This followed a December dip on the first round of asset transfers to SAREB (see figure 9), with the ratio retreating one full point from its November peak of 11.4% (the highest level of the available historical series). Delinquent loans were again strongly linked to real estate and construction, with year-end ratios of 29.6% and 24.5% respectively, after a 1-2 point fall in the closing quarter reflecting their high profile in the SAREB transfer. Meantime, the NPL ratio of remaining productive activities rose 1.2 points in the same period to 8.7%. Non-performance in the household sector advanced to 4.9% in December 2012 (4.4% in September), with unsecured loans as the main locus (6.8% in September rising to 8.1% in December) ahead of mortgage loans (up by 0.3 points in the fourth quarter to 4.3%).

Credit institution NPL ratios and the unemployment rate¹

FIGURE 9

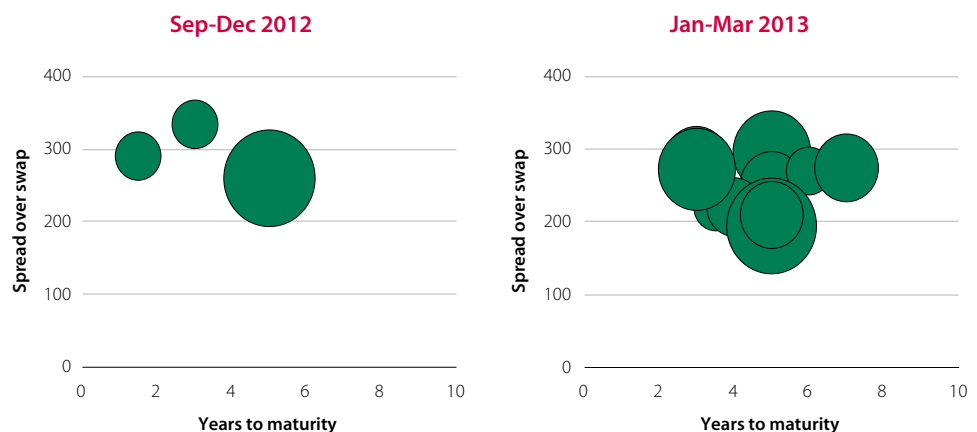


Source: Banco de España and INE. NPL ratios to January 2013, unemployment rate to December 2012.

¹ % of the active population.

Debt issuance by Spanish financial institutions¹

FIGURE 10



Source: Dealogic.

¹ Senior bonds and mortgage covered bonds. Floating-rate issues. The size of the bubble is proportional to the size of the issue.

Credit institution financing conditions were adversely impacted by financial market tensions over the first half of 2012. Banks, however, were able to cover their needs in reasonable comfort by taking up government guarantees for sector debt financing and stepping up their recourse to Eurosystem funding. Also, international debt markets have tentatively reopened for the entities in best repair, allowing in a significantly higher number and volume of unsecured issues at longer maturities and a lower cost.

Deposit-taking entities remain heavily dependent on Eurosystem funding, despite easier financing conditions.

The aggregate profits of non-financial listed companies dropped 45.4% in 2012 as far as 12.65 billion euros (see table 4), on the sluggish state of domestic activity. Much of this decline was down to retail and service companies, whose aggregate profits crashed by 51% to 4.63 billion euros, and the deepening losses of construction and real estate firms, which summed over 5.10 billion in the full-year period. The best performers in relative terms were energy companies, whose profits slipped by a bare 3%, while the aggregate profits of the industry sector dropped from 2.77 billion euros in 2011 to 2.47 billion in 2012.

The aggregate profits of non-financial listed corporations shrink by 45% in 2012...

Earnings by sector:¹ non-financial listed companies

TABLE 4

Million euros	EBITDA ²		EBIT ³		Net profit	
	2H11	2H12	2H11	2H12	2H11	2H12
Energy	26,643	27,949	17,144	17,588	10,741	10,421
Industry	6,716	7,237	4,455	4,845	2,767	2,467
Retail and services	29,557	28,924	15,500	14,176	9,453	4,632
Construction and real estate	5,095	5,079	2,207	1,579	-166	-5,108
Adjustments	231	63	354	197	353	234
AGGREGATE TOTAL	68,242	69,252	39,660	38,385	23,148	12,646

Source: CNMV.

1 Year to date.

2 Earnings before interest, taxes, depreciation and amortisation.

3 Earnings before interest and taxes.

The aggregate debt levels of non-financial listed companies decreased by 4.1% to 296.30 billion euros, of which 60% was lodged with construction and real estate operators and a further 37% with energy sector firms (see table 5). Aggregate leverage, meantime, edged down in the year from 1.44 to 1.40, with the reduction extending to all sectors except construction and real estate. Companies' debt coverage ratio, measuring the years needed to repay existing debt assuming constant EBITDA, held more or less flat at 4.3, while their interest cover (EBIT/interest expenses) worsened slightly between 2011 and 2012. The latter indicator deteriorated in all the sectors followed with the exception of industry, although ratios were at their lowest in construction and real estate.

...while their debt levels fall by 4.1% to 296 billion euros.

Gross debt by sector: listed companies

TABLE 5

Million euros		2008	2009	2010	2011	2012
Energy	Debt	82,608	100,572	98,283	95,853	91,233
	Debt/ Equity	0.89	1.08	0.95	0.92	0.85
	Debt/ EBITDA ¹	2.82	3.46	2.81	3.27	3.26
	EBIT ² / Interest expenses	3.67	3.38	4.15	3.30	3.14
Industry	Debt	15,645	15,953	14,948	17,586	16,836
	Debt/ Equity	0.69	0.69	0.58	0.63	0.62
	Debt/ EBITDA	2.71	3.05	2.11	2.54	2.33
	EBIT/ Interest expenses	3.41	3.15	5.00	3.90	3.98
Construction and real estate	Debt	119,788	104,762	99,917	83,716	76,213
	Debt/ Equity	3.77	4.08	3.42	2.98	3.50
	Debt/ EBITDA	31.87	22.48	11.18	15.00	15.01
	EBIT/ Interest expenses	0.01	0.31	0.98	0.52	0.33
Retail and services	Debt	112,322	108,579	115,413	113,142	113,466
	Debt/ Equity	2.14	1.78	1.60	2.01	1.99
	Debt/ EBITDA	3.58	3.70	3.38	3.78	3.92
	EBIT/ Interest expenses	2.86	3.28	3.94	2.45	2.06
Adjustments ³	Debt	-20,802	-1,908	-1,792	-1,404	-1,378
AGGREGATE TOTAL	Debt	309,561	327,958	326,769	308,893	296,320
	Debt/ Equity	1.63	1.63	1.43	1.44	1.40
	Debt/ EBITDA	4.63	4.82	3.84	4.29	4.28
	EBIT/ Interest expenses	2.01	2.42	3.12	2.30	2.09

Source: CNMV.

1 Earnings before interest, taxes, depreciation and amortisation.

2 Earnings before interest and taxes.

3 In drawing up this table, we eliminated the debt of issuers consolidating accounts with some other Spanish listed group. The figures in the adjustments row correspond to eliminations from subsidiary companies with their parent in another sector.

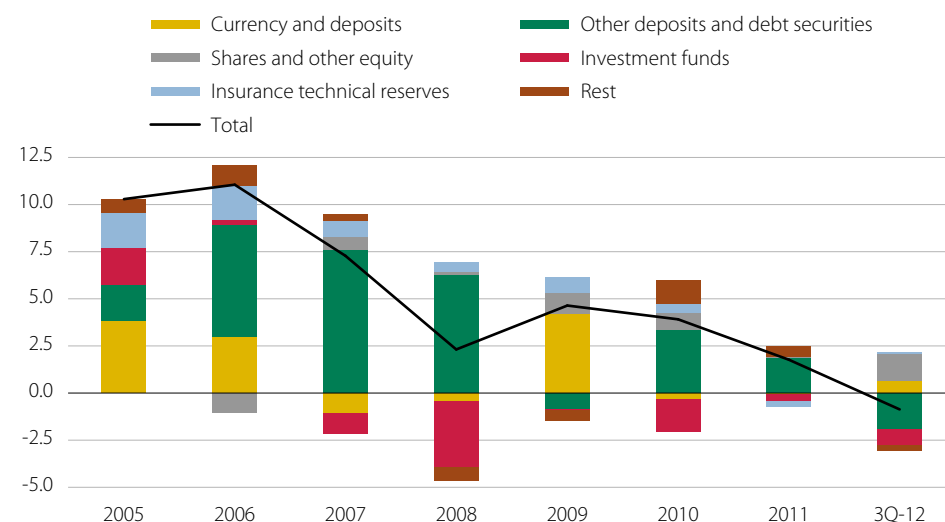
Households stabilise their debt but go on losing financial wealth. Last year's large outflows from deposits, debt instruments and investment funds have begun to level off.

Indicators for the third quarter of 2012 locate the indebtedness and financial burden of households at just over 120% and 15% respectively of disposable income. These essentially flat ratios are because household borrowings and income have fallen by a similar margin. Households' net financial wealth, meantime, continued in decline due to depreciating real estate. As regards investment decisions, the salient development has been the gathering tide of financial divestments, as far as 0.9% of GDP in the third-quarter period,¹¹ with the biggest disposals corresponding to time deposits, fixed-income instruments and investment funds. This trend, which marked a break with the investing customs of Spanish households (see figure below), has seemingly remitted in the closing months of 2012, to judge by the recovery in bank deposits.

11 Cumulative four-quarter data.

Households: financial asset acquisitions (% GDP)

FIGURE 11



Source: Banco de España, *Cuentas financieras*. Cumulative four-quarter data.

2.3 Outlook

In its latest forecasts, published in January, the IMF augurs global growth of 3.5% this year and 4.1% in 2014, back to more or less the rate of 2011. The advanced economies, it projects, will expand 1.4% this year, on a par with 2012, and 2.2% in 2014, while the emerging economies will manage a 5.5% advance in 2013 followed by 6% in 2014, just short of the 6.3% attained in 2011.

The main risks for these projections remain tilted to the downside, despite the more robust state of international financial markets. In Europe, it would be premature to say that the sovereign debt crisis has been laid to rest, making it all the more necessary to complete the restructuring of the region's financial system and move ahead with integration projects like the banking and fiscal union. Fiscal consolidation is still a major near- and mid-term challenge that affects not only Europe but other advanced economies like Japan and the United States. The risks facing the emerging economies are of a different nature, though here too the task in hand for most countries is to adopt economic policies that rebalance growth and make them more resilient to possible domestic imbalances and global demand shocks.

The IMF's July projections for the Spanish economy point to a slowdown in domestic activity extending to 1.5% in 2013, and a return to positive growth in 2014 of 0.8%. These estimates mark a minor revise-down over its previous forecasts of October 2012. Despite improved conditions on domestic financial markets in these past few months, the macro scenario remains hedged by uncertainty, given the state of the Spanish labour market and the need to let adjustment processes run their course (real estate sector, financial sector, deleveraging, etc.). In general, however, the reform and restructuring of the domestic banking system, and the government's deployment of less contractionary measures, without losing sight of fiscal targets, could alleviate the downside risks.

The IMF is forecasting world growth of 3.5% in 2013 and 4.1% in 2014...

...amid fears of renewed sovereign debt market tensions and with leading economies striving to fight back to fiscal health.

Activity in Spain will likely stay subdued in the coming quarters amid intense fiscal adjustment and bank sector restructuring.

Exhibit 2: “The shadow banking system: latest FSB recommendations”

Shadow banking has been defined as financial intermediation involving entities and activities outside the regular banking system. Such intermediation can be good for the economy in providing agents with a wider choice of investment and financing vehicles. But experience from the recent crisis has demonstrated the capacity of some non-bank entities and transactions to operate on a large scale in ways that create bank-like risks to financial stability. The increase in system risk associated with shadow banking lies not only in its direct but also indirect activity, through its web of connections with the banking sector. Yet shadow banking has never been the prime focus of prudential regulation, so has stayed unconstrained by the controls and conditions operating on entities and transactions in the regular banking sphere.

Further to the requests made by the G-20 at its summits in Seoul (2010) and Cannes (2011), the Financial Stability Board is working with other international bodies to draft a set of recommendations for the regulation and oversight of this activity in order to avoid and/or minimise latent risks. In the process, the FSB has pinpointed five areas where it believes policies are needed to mitigate the potential systemic risks associated with shadow banking:

- i. To mitigate the spill-over effect between the regular banking system and the shadow banking system.
- ii. To reduce the susceptibility of money market funds (MMFs) to “runs”, i.e., a spate of investor withdrawals.
- iii. To assess and mitigate systemic risks posed by entities other than money market funds working within the shadow banking system.
- iv. To assess and align the incentives associated with securitisation.
- v. To dampen risks and pro-cyclical incentives associated with secured financing contracts such as repos and securities lending.

Diverse institutions have analysed these five target areas and come up with their reports. On 18 November 2012, the FSB published two consultative documents¹ with a series of recommendations on regulating the entities that make up the shadow banking system (point iii) and repos and securities lending (point v). IOSCO, meantime, brought out recommendations last October and November relating to money market funds (point ii) and securitisation² (point IV) respectively, while the Basel Committee for Banking Supervision (BCBS) is working on its own recommendations addressing point i, which are due to be published this mid-year.

In its securitisation report, IOSCO issues a series of recommendations, drawn from its consultation with industry organizations, aimed at aligning incentives between stakeholders, building confidence in this kind of market and removing, where possible, impediments to cross-border activity. To this end, it proposes risk retention by the originator, already obligatory in some jurisdictions, as a central tenet of industry operation, and recommends enlarging and improving disclo-

sure through, for instance, the conduct of regular stress tests on underlying assets, and a move towards the standardisation of securitisation products, along the lines initiated by the industry itself.

IOSCO has also published recommendations to improve the working of money market funds, in the light, particularly, of the massive outflows these funds have suffered in recent years. The first point it makes is that MMFs should be explicitly defined within the collective investment scheme universe, and in the corresponding regulations. The competent authorities are also urged to ensure that MMFs value their assets according to current market prices (rather than amortised cost) and maintain a minimum amount of liquid assets, with which they can face redemptions and thereby prevent fire sales.

In its section on the entities other than MMFs engaged in shadow banking, the FSB proposes classifying them by reference to five predefined economic functions (rather than their legal forms or names), so the competent authorities can set and enforce rules according to whether they belong to one or other group. All policies applied should, if necessary, be reformulated to provide international consistency in assessing their risks.

The FSB has also examined the risks posed by the securities lending and repo markets, and has drafted recommendations in their regard. In essence, these propose enhanced transparency, with reporting requirements binding on all agents; regulatory changes in respect of haircuts on transactions, which should be based on long-run risk, and the possibility of introducing floors on haircuts where there is material procyclicality risk; and structural market changes, including increased use of central counterparties and the reform of the bankruptcy law treatment of these transactions, in view of its difficult enforcement.

According to the timeline envisaged by the FSB, a full report containing final recommendations on the five target areas should be ready by September of this year.

- 1 *A Policy Framework for Strengthening Oversight and Regulation of Shadow Banking Entities* (http://www.financialstabilityboard.org/publications/r_121118a.pdf) and *Policy Recommendations to Address Shadow Banking Risks in Securities Lending and Repos* (http://www.financialstabilityboard.org/publications/r_121118b.pdf).
- 2 *Policy Recommendations for Money Market Funds* (<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD392.pdf>) and *Global Developments in Securitisation Regulation* (<http://www.iosco.org/library/pubdocs/pdf/IOSCOPD394.pdf>).

3 Spanish markets

3.1 Equity markets

Domestic equity markets have enjoyed a bull run since the end of July 2012 and the ECB's announcement of new measures to preserve the financial stability of the euro area, which cushioned them in part from the potentially adverse impact of the reform and restructuring of the Spanish financial system. Prices, moreover, have continued rising through the first quarter of 2013, though more haltingly at times of

Share prices rally as of end-July 2012 in a climate of improved liquidity and lesser volatility, but trading volumes remain thin.

political uncertainty, especially in Italy. The year also started off with a robust improvement in market liquidity conditions and reduced levels of volatility, albeit with the persistence of the thin trading volumes that have dominated since the start of the crisis. The easing of financial market tensions also permitted the removal, on 1 February, of the short-selling ban in force since 23 July 2012.¹²

Rises have persisted through the first quarter of 2013 in most domestic stock indices ...

The Ibex 35 advanced 5.5% in the first quarter of this year on the heels of the vigorous rally of August-December. These second-half gains, however, failed to offset the price slide of the opening months, leaving the index 4.7% in negative territory over full-year 2012 (see table 6). After ending last year with opposing fortunes, small and medium cap indices moved higher in the opening months, with the small cap index in the lead (gains of 11.9% and 5.7% in 2013 to date against -24.4% and 13.8 respectively in full-year 2012). Finally, the indices tracking the Latin American companies traded on domestic platforms performed unevenly in the first quarter, with the 2% fall in the FTSE Latibex All-Share contrasting with the 4.6% rise of the FTSE Latibex Top (-10.7% and -2.6% respectively in 2012).

...and sectors.

The first-quarter advance was headed by consumer services (17.5% after a 12.7% gain in 2012), followed by technology and telecommunications (11.5% after -18.3% in 2012), oil and energy (6.7% after -16%), basic materials, industry and construction and financial and real estate services (3.6% in both cases after -8% and -4.7% in 2012). Consumer goods was the only sector to lose ground in the opening quarter, slipping back 0.2% after the strong surge of 2012 (55.6%). Closer analysis shows that the sub-sectors performing most strongly in the first months of 2013 were transport and distribution (within consumer services), insurance (financial and real estate services), pharmaceutical products and biotechnology (consumer goods), telecommunications and others (technology and telecommunications) and oil (oil and energy), with gains ranging from 11% to 41%. Other sub-sectors too held in positive terrain, the exceptions being food and drink and clothing and footwear (consumer goods), real estate and others (financial and real estate services) and minerals, metals and metal processing (basic materials, industry and construction) albeit with falls in no case exceeding 5%.

The P/E of the Ibex 35 increases more slowly in the first months of 2013.

The price-earnings ratio¹³ (P/E) of the Ibex 35 lost some of its momentum after advancing steadily through the second half of 2012, supported by the price rally of the third quarter and, in lesser measure, the fall in expected earnings. The more modest increase of the opening months was repeated on other advanced economy indices, conserving the Spanish index the midway slot in the international P/E ranking which it has occupied since the third quarter of 2012. By March, specifically, the Ibex 35 multiple was at 12.1 times, compared to the 11.7 of last year's close and the 9.2 of year-end 2011.

¹² For more information, see www.cnmv.es

¹³ On one-year forward earnings.

Performance of Spanish stock market indices and sector

TABLE 6

%							1Q 13 (to 15 March)		
	2009	2010	2011	2012	3Q 12 ¹	4Q 12 ¹	% prior qt.	% Dec	% y/y
Index									
Ibex 35	29.8	-17.4	-13.1	-4.7	8.5	6.0	5.5	5.5	2.3
Madrid	27.2	-19.2	-14.6	-3.8	8.2	6.1	5.7	5.7	2.7
Ibex Medium Cap	13.8	-5.6	-20.7	13.8	4.0	12.6	5.7	5.7	10.1
Ibex Small Cap	17.6	-18.3	-25.1	-24.4	11.0	-6.0	11.9	11.9	-10.7
FTSE Latibex All-Share	97.2	9.0	-23.3	-10.7	2.6	-6.7	-2.0	-2.0	-21.1
FTSE Latibex Top	79.3	9.7	-17.1	-2.6	-1.2	-2.9	4.6	4.6	-11.6
Sector²									
Financial and real estate services	47.3	-31.7	-18.9	-4.7	11.5	5.4	3.6	3.6	-2.1
Banks	50.0	-33.1	-20.3	-4.8	11.2	5.0	3.3	3.3	-2.5
Insurance	18.9	-26.4	12.5	-2.0	27.8	8.5	17.9	17.9	10.3
Real estate and others	-31.8	-53.3	-47.5	-14.4	36.5	31.7	-3.0	-3.0	0.3
Oil and energy	-2.7	-8.6	-2.7	-16.0	5.8	10.6	6.7	6.7	-0.3
Oil	12.4	10.2	14.9	-35.4	19.4	1.6	11.9	11.9	-10.5
Electricity and gas	-8.4	-14.2	-10.8	-5.4	0.1	15.2	4.5	4.5	4.0
Basic materials, industry and construction	22.5	-15.2	-14.3	-8.0	4.6	8.8	3.6	3.6	-2.9
Construction	17.7	-14.9	-6.9	-9.3	4.0	14.6	3.0	3.0	-1.6
Manufacture and assembly of capital goods	9.9	-29.2	-12.2	-8.8	4.7	6.7	2.1	2.1	-0.4
Minerals, metals and metal processing	36.4	-9.1	-33.7	-8.7	-0.6	3.2	-2.7	-2.7	-18.8
Engineering and others	92.7	-0.1	-29.0	3.8	14.5	-4.8	5.2	5.2	2.1
Technology and telecommunications	22.8	-12.8	-20.9	-18.3	1.1	-0.3	11.5	11.5	-5.7
Telecommunications and others	23.3	-12.8	-20.8	-23.0	0.1	-1.5	12.4	12.4	-9.1
Electronics and software	3.0	-12.0	-21.3	39.4	7.7	7.9	6.0	6.0	29.6
Consumer goods	26.3	17.0	5.7	55.6	16.5	9.1	-0.2	-0.2	40.3
Textiles, clothing and footwear	38.3	28.6	12.7	66.2	18.5	9.1	-3.0	-3.0	45.4
Food and drink	7.0	25.3	-6.3	25.0	7.0	12.2	-4.1	-4.1	12.6
Pharmaceutical products and biotechnology	14.5	-22.2	-7.3	68.3	23.1	4.4	14.8	14.8	60.6
Consumer services	32.3	-0.1	-24.2	12.7	2.4	13.0	17.5	17.5	19.0
Motorways and car parks	36.2	-10.1	-3.7	5.7	7.6	8.5	8.0	8.0	8.8
Transport and distribution	3.8	55.3	-34.9	29.7	-4.9	20.2	40.2	40.2	49.8

Source: BME and Thomson Datastream.

1 Change vs. previous quarter.

2 IGBM sectors. Under each sector, data are provided for the most representative sub-sectors.

The earnings yield gap, which reflects the return premium required to be invested in equity versus long-term government bonds, has held more or less flat since the last quarter of 2012, after narrowing sharply in the third quarter on an escalating P/E ratio and the steeply falling yields of the long-term Spanish bond. The result was a mid-March gap of 3.4, ahead of the 3.3 of the 2012 close but well below the 5.2 of June that year, and not far off its historical average since 1999 (3.2).

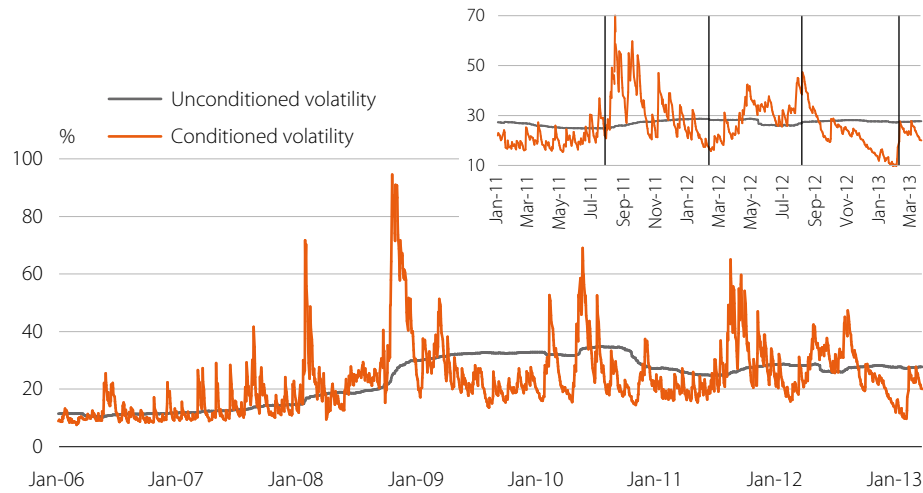
The earnings yield gap stabilises after a third-quarter fall.

Market volatility retreats from the highs of mid-2012...

Ibex 35 volatility was choppier in the first months of 2013 after last year's descent from the highs of late July (when it was testing 50%), but remained low by historical standards at just over 20%.

Historical volatility of the Ibex 35

FIGURE 12



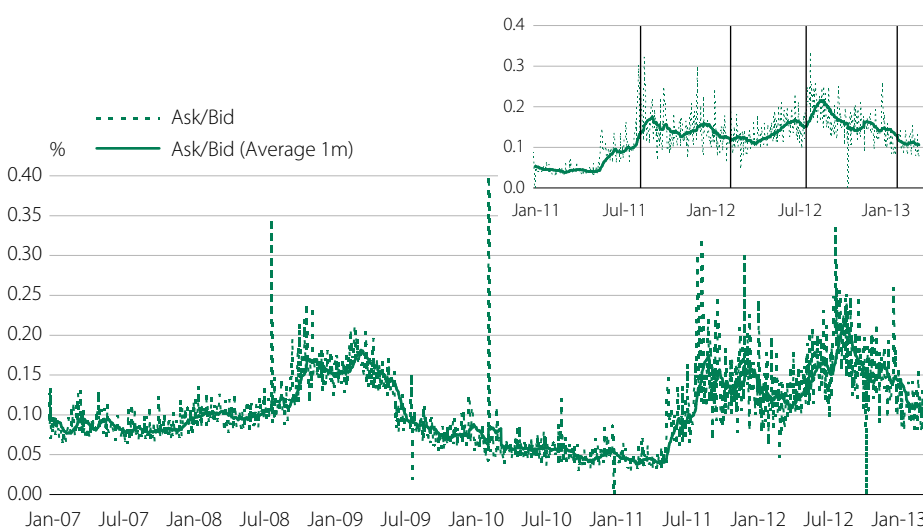
Source: Thomson Datastream and CNMV. Data to 15 March. The vertical lines in the enlarged figure refer respectively to the introduction and lifting of the previous short-selling ban on 11 August 2011 and 16 February 2012 respectively, and the new ban starting on 23 July 2012 and ending on 1 February 2013.

...and liquidity conditions pick up strongly.

The liquidity conditions of the Ibex 35 (measured through the bid/ask spread) resumed the improvement path of last September-October, after the interruption of the closing months (see figure 13). The year's more settled mood was reflected in a March spread of 0.11%, in line with the average recorded since the series was begun in 2003, and comfortably below both the 0.15% of end-2012 and the 0.21% of August that year.

Ibex 35 liquidity. Bid-ask spread

FIGURE 13



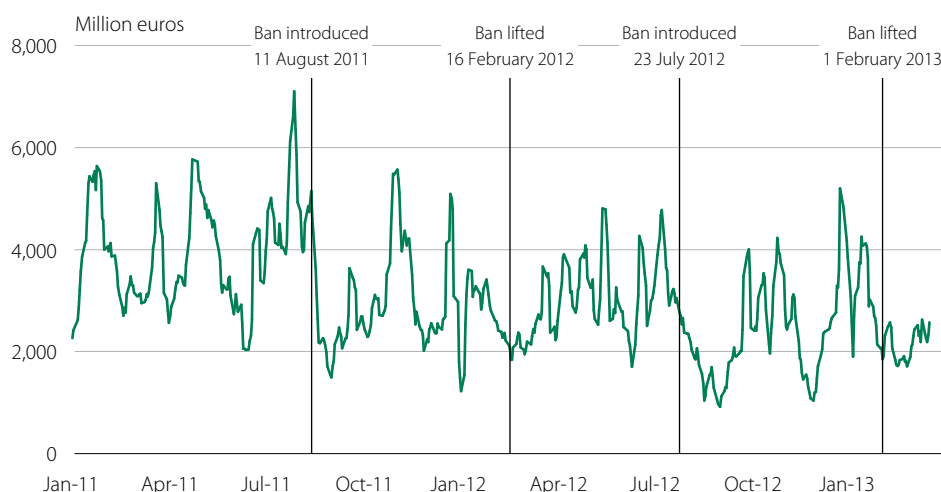
Source: Thomson Datastream and CNMV. Data to 15 March. The vertical lines in the enlarged figure refer respectively to the introduction and lifting of the previous short-selling ban on 11 August 2011 and 16 February 2012 respectively, and the new ban starting on 23 July 2012 and ending on 1 February 2013.

The Spanish stock market registered a trading volume of 138.67 billion euros in the first three months of 2013 (to 15 March), 4.3% less than in the same period last year (see table 7). Average daily volume, at 2.62 billion, was higher than last year's second-half average (2.26 billion) but lower than in the first six months (2.96 billion). As we can see from figure 14, market trading volumes shrank for a period of around twenty trading days following the entry of the short-selling ban, and rebounded in the seven sessions after it was lifted.¹⁴ Overall, however, trading volumes on Spanish stock markets reached their lowest point since the onset of the crisis.¹⁵

Trading on Spanish stock markets remains thin by historical standards.

Daily trading on the Spanish stock market¹

FIGURE 14



Source: CNMV. Data to 15 March 2013.

¹ Moving average of five trading days.

Equity issuance on domestic markets surged by 57% to 4.99 billion euros compared to the first three months of 2012 (see table 8). Note, however, that the capital raised this year to date is inflated by the FROB's recapitalisation and subsequent sale of a credit institution, while last year's first-quarter figure included the merger by takeover of one entity by another (36% of the total), a capital increase by a medium-sized bank (28%) and a subscription offer of shares addressing the holders of certain preference shares and subordinated debt instruments issued by another medium-sized bank (27%).

Equity issuance expanded strongly in the first quarter of 2013 on transactions derived from the bank sector restructuring process.

14 For a fuller analysis of how the short-selling restrictions deployed since 2011 have affected euro-area stock markets, see the article by Carlos Aparicio Roqueiro "Empirical study on the bans on short selling in Europe in 2011 and 2012", in this Bulletin.

15 Taking average daily volumes in the year, the low point comes in 2012 (2.61 billion euros), compared to the higher levels of 2008 to 2011 (4.89 billion in 2008, 3.49 billion in 2009, 4.05 billion in 2010 and 3.62 billion in 2011).

Turnover on the Spanish stock market

TABLE 7

Million euros

	2009	2010	2011	2012	3Q 12	4Q 12	1Q 13 ¹
All exchanges	886,135	1,037,284	925,667	667,443	153,483	138,303	138,674
Electronic market	880,544	1,032,447	920,879	663,076	152,438	137,463	137,516
Open outcry	73	165	48	40	8	8	5
of which SICAVs ²	20	8	6	0	0	0	0
MAB ³	5,080	4,148	4,380	4,025	947	755	1,070
Second Market	3	3	2	0	0	0	0
Latibex	435	521	358	302	90	77	84
Pro memoria: non-resident trading (% all exchanges)							
	64.5	75.3	81.3	n.a.	n.a.	n.a.	n.a.

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

1 Cumulative data from 1 January to 15 March.

2 Open-end investment companies.

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

n.a.: Data not available at the closing date for this report.

Capital increases and public offerings¹

TABLE 8

	2009	2010	2011	2012	3Q 12	4Q 12	1Q 13 ²
CASH AMOUNTS³ (million euros)	11,391	16,017	17,146	21,142	5,695	6,962	4,988
Capital increases	11,389	15,407	17,019	19,911	5,291	6,186	4,988
Of which, through POS	17	959	6,239	2,457	75	0	0
National tranche	15	62	5,827	2,457	75	0	0
International tranche	2	897	412	0	0	0	0
Public offering of shares	2	610	127	1,231	405	776	0
National tranche	2	79	125	1,231	405	776	0
International tranche	0	530	2	0	0	0	0
NUMBER OF FILINGS⁴	53	69	92	105	27	30	26
Capital increases	53	67	91	103	26	29	26
Of which, through POS	2	12	8	7	1	0	0
Of which, bonus issues	11	15	22	22	10	4	9
Public offering of shares	1	3	2	3	1	1	0

Source: CNMV.

1 Incorporating issues admitted to trading without a prospectus being filed.

2 Data to 15 March.

3 Excluding amounts recorded in respect of cancelled transactions.

4 Including all transactions registered, whether or not they eventually went ahead.

Exhibit 3: “Amended legislation on prospectuses and transparency requirements for the issuers of securities”

Royal Decree 1698/2012 of 31 December amending the legislation on prospectuses and transparency requirements in relation to the issuance of securities rounds off the transposition of Directive 2010/73/EU, till now only partly written into Spanish law. As the legislator affirms in the preamble to this latest text, its purpose is to reduce the administrative burden involved in publishing an issue prospectus, while modernising and improving part of the applicable rules.

Main novelties are as follows:

- Revision of some of the thresholds determining when an offer is a public offer, with the result that a prospectus is no longer mandatory in the following cases:
 - a) When the denomination per unit of the securities or minimum amount per investor is at least 100,000 euros (previously 50,000 euros).
 - b) When the number of persons to whom the offer is addressed is no more than 150 (previously 100 persons).
 - c) When the offer’s total consideration is no more than five million euros (previously 2,500,000 euros) calculated over a twelve-month period.
- The resale of securities carried out through financial intermediaries will be exempt from the obligation to publish an additional prospectus, provided that a valid prospectus is already available to the public and the issuer or party responsible has consented in writing to its use.
- A prospectus will be valid from the date it is filed with the CNMV rather than the date it is published. Also, an electronic version must be made available on the issuer’s website.
- The concept of key information is given legal definition as the essential information, appropriately structured, that must be provided to investors so they understand the nature and risks of the issuer, the guarantor and the securities that are being offered or admitted to trading on a regulated market. Also, the definition of qualified investor is recast to align it with the definition of professional investor as per the Markets in Financial Instruments Directive (MiFID).
- A series of provisions affect the summary of the prospectus. First, this document is given a specific, harmonised format, and brought within the key information requirement set out above. Second, a summary can be dispensed with in the admission to trading of non-equity securities whose denomination per unit is higher than 100,000 euros. Finally, whoever applies for the securities to be admitted to trading on Spanish secondary markets must translate the summary into Spanish when the full prospectus is not in that language.

- Two new conditions refer to the final terms issued under a base prospectus. On the one hand, issuers must communicate the final terms of passported prospectuses to the competent authority of the host Member State. On the other, issuers of commercial paper with a maximum maturity of 12 months will not have to present final terms for each offering or admission to listing.

The reform of EU legislation on the prospectus for public offerings of securities and their admission to trading was also advanced by Commission Delegated Regulation 486/2012 of 30 March 2012 amending the Prospectus Regulation and in force since 1 July 2012. Among its innovations, we can single out the introduction of a proportionate disclosure schedule for certain operations, and a template for the “form of final terms”.

3.2 Fixed-income markets

Domestic debt market tensions abate in the closing months,...

The tensions rending domestic financial markets over the middle months of 2012 have abated since the third quarter on the ECB’s announcement of a new secondary market bond-buying programme,¹⁶ the headway made in recapitalising and restructuring Spain’s financial system, and the upkeep of the country’s fiscal consolidation drive. This calmer mood has permitted: (i) a run-down in yields of public and private debt securities, (ii) declining risk premiums in both sectors of the economy, (iii) an upswing in government bond turnover in secondary markets, and (iv) a sizeable increase in government debt holdings in non-resident hands. Another result has been the visible uncoupling between price movements in public sector financial instruments and those issued by the banks.

...permitting a run-down in public and private debt yields in both short...

Against this backdrop, short-term Treasury bill rates closed the year at 1.1%, 1.7% and 2.2% in three, six and twelve-months tenors respectively, then went on falling as far as March averages of 0.3%, 0.9% and 1.4% (see table 9). In contrast to the second half of 2012, when 12-month rates fell at a significantly greater speed, this first-quarter decline was more evenly paced across different maturities, in the range of 76 bp to 88 bp. Commercial paper yields, after holding relatively steady through the closing months of 2012, headed abruptly lower in 2013, with falls of between 138 bp in the three-month maturity and 190 bp at twelve months.

...and long maturities...

Long government bond yields have come down substantially after peaking last July above 7% at the height of market turbulence. As we can see from table 10, three, five and ten-year yields recorded March averages of 2.8%, 3.6% and 4.9% respectively, substantially below the equivalent levels at the 2010, 2011 and 2012 close. Long-term corporate bond yields traced a similar course as far as 3.2%, 4.1% and 6.8% respectively in March 2013, a good 270 bp away from their mid-2012 highs.

¹⁶ This programme, involving what are known as outright monetary transactions (OMTs), focuses on the shorter part of the yield curve, particularly maturities of between one and three years, and is predicated on an application from the government to the appropriate European financial assistance mechanism (see http://www.ecb.int/press/pr/date/2012/html/pr120906_1.en.html).

Short-term interest rates¹

TABLE 9

%	Dec 10	Dec 11	Dec 12	Sep 12	Dec 12	Mar 13 ³
Letras del Tesoro						
3 month	1.60	2.20	1.14	0.93	1.14	0.33
6 month	2.71	3.47	1.68	1.74	1.68	0.92
12 month	3.09	3.27	2.23	2.52	2.23	1.35
Commercial paper²						
3 month	1.37	2.74	2.83	2.85	2.83	1.45
6 month	2.52	3.52	3.58	3.56	3.58	1.75
12 month	3.04	3.77	3.80	3.69	3.80	1.90

Source: Thomson Datastream and CNMV.

1 Monthly average of daily data.

2 Interest rates at issue.

3 Data to 15 March.

Medium and long corporate bond yields¹

TABLE 10

%	Dec 10	Dec 11	Dec 12	Sep 12	Dec 12	Mar 13 ²
Government bonds						
3 year	3.87	4.01	3.40	3.88	3.40	2.78
5 year	4.65	4.65	4.22	4.84	4.22	3.60
10 year	5.38	5.50	5.33	5.92	5.33	4.90
Corporate bonds						
3 year	4.31	5.63	3.76	5.32	3.76	3.19
5 year	5.44	6.35	4.71	6.47	4.71	4.07
10 year	6.42	9.24	7.70	9.13	7.70	6.79

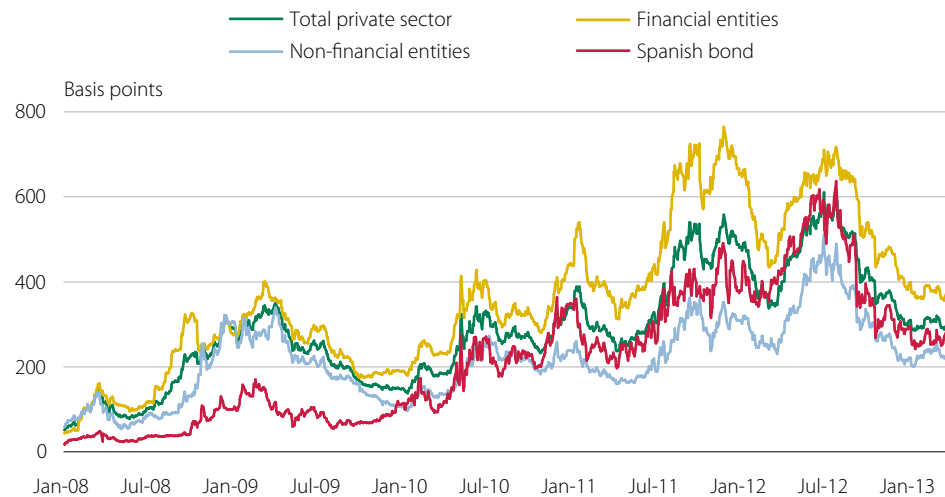
Source: Thomson Datastream, Reuters and CNMV.

1 Monthly average of daily data.

2 Data to 15 March.

On this performance, Spain's sovereign risk premium, as derived from 5-year CDS, pulled steadily back from its end-July peak of 640 bp to a year-end level of 300 bp and onto 270 bp in mid-March (see figure 15). Meantime, the ten-year Spanish/German spread narrowed from close to 635 bp in late July to 396 bp at end-December 2012 and 344 bp in mid-March 2013. This lesser perception of sovereign risk extended across Europe, accompanied by a notable downturn in indicators of credit risk contagion from more vulnerable to more solid economies (see figure 5).

...and taking much of the heat off sovereign risk premiums in a context of less contagion.



Source: Thomson Datastream and CNMV.

1 Simple average. Data to 15 March.

There is evidence too of some uncoupling between the price movements of Spanish government bonds and shares.

Private sector risk spreads tended to mirror the progress of their sovereign equivalents in 2012 and the first months of 2013, with a sharp ascent to the month of July giving way to a sustained easing movement. As figure 15 shows, the average CDS spreads of corporate issuers, which in normal market circumstances exceed those of public debt, held at comparable levels over the period of greatest tension due to the contemporaneous spike in bank sector risk premiums. Specifically, the CDS spreads of Spanish private-sector issuers retreated from end-July highs of over 600 bp to 300 bp in mid-March 2013. Between these same dates, the average CDS spreads of Spanish banks dropped from over 700 bp to approaching 370 bp, while those of financial corporations fell from around 500 bp to just over 220 bp. This decline in the credit spreads of the various sectors of the Spanish economy was accompanied from August onwards by a loosening correlation between the price movements of Spanish government bonds and shares (see figure 16).

Primary market activity also moved up a gear in the latter half of 2012,...

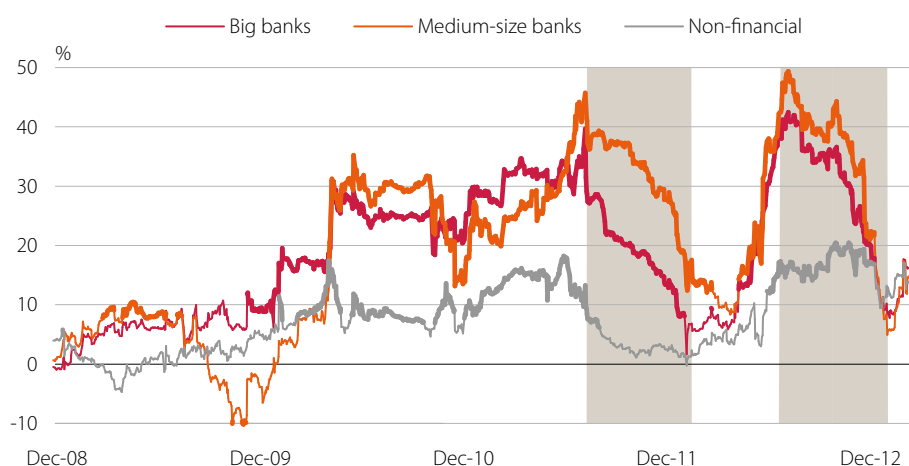
Spain's financial corporations, banks especially, have taken advantage of the second-half decline and subsequent stabilisation in market tensions to resume issuance of marketable debt securities and simultaneously scale down their net Eurosystem borrowings. The gross volume of fixed-income issues registered with the CNMV in 2012 came to 357.83 billion euros, 23.8% more than in 2011. This advance, which brought issuance close to 2009 levels, was driven by increased placements of government-backed non-convertible bonds, mortgage covered bonds and commercial paper, offsetting the decline in issuance of asset-backed securities.

...but has tapered off in the opening months of 2013, on more modest sales of commercial paper and mortgage covered bonds.

This year, however, the issuance spurt has been running out of steam, with gross sales in the first three months down 60% versus the year-ago period to 40.58 billion euros. Leading the year-on-year decline were commercial paper and mortgage covered bonds, down by 78% and 60% respectively to 9.03 and 8.19 billion euros (22% and 20% of the year-to-date total). The other big drop was in convertible bonds, down by 62% to 425 million euros, though their weight in the total is relatively small.

Correlation between returns on national government bonds and shares^{1,2,3}

FIGURE 16



Source: Thomson Datastream and CNMV.

- 1 Ordinary least square (OLS) estimates are run on each portfolio, in rolling six-month windows, where the left side of the equation is the return (log) of the share portfolio and the right side the return (log) of the Eurostoxx 300 and that of a portfolio long in national government bonds and short in German bonds (iboxx indices). The coefficient corresponding to the government bond portfolio is multiplied by the standard deviation of the return on this portfolio during the estimation period, and divided by the standard deviation in the same period of the return on the corresponding portfolio of shares.
- 2 The shaded area represents the period when the short-selling ban was in force in Spain.
- 3 The line of each correlation indicator alternates between thick and fine. A thick line means we cannot rule out that the regression coefficient for the variable representing the inverted spread was significantly different from zero to 10% over the period in question.

Sales of non-convertible bonds fell by a lower 42%, in year-on-year terms, to 15.56 billion euros, equivalent to 38% of the total amount (29% in the first quarter of 2012 and 24% in the full-year period). Almost all non-convertible issues in last year's closing quarter and the first quarter of 2013 comprised government-backed securities issued by "bad bank" SAREB against the receipt of assets from Group 1 and Group 2 entities. Government-backed bonds were also prominent in the issuance mix of 1Q 2012, except then their use was primarily as collateral in bank sector funding operations with the ECB.

Non-convertible bond sales are also down to a lesser extent, the majority carrying a state guarantee.

Asset-backed securities, meantime, raised 7.38 billion euros (18% of total issuance, against 7% in 2012). This was 20% less than one year ago, reflecting the still depressed state of securitisation markets. No issues were reported of either preference shares (repeating the zero issuance of 1Q 2011) or territorial covered bonds (2.50 billion in 1Q 2011).

Securitisation markets remain notably lethargic.

Foreign debt financing by domestic institutions dropped to just over 92 billion euros, 23.2% less than in 2011 (see table 11). This decline was entirely due to lower sales of short-term paper, whilst long-term issues remained notably dynamic (54.7% of total 2012 issuance against 42.8% one year before).

Foreign debt financing decreases in the year, with short-term instruments leading the decline.

Gross fixed-income issues

TABLE 11

	2009	2010	2011	2012	2012		2013
					3Q	4Q	1Q ²
filed¹ with the CNMV							
NUMBER OF ISSUES	512	349	353	334	48	69	53
Mortgage bonds	75	88	115	94	27	18	14
Territorial bonds	1	9	42	18	2	0	0
Non-convertible bonds and debentures	244	154	87	134	13	23	24
Convertible/exchangeable bonds and debentures	6	3	9	7	0	2	3
Asset-backed securities	76	36	45	35	1	17	10
Commercial paper facilities	73	59	53	46	5	9	2
Securitised	2	2	2	1	0	1	0
Other commercial paper	71	57	51	45	5	8	2
Other fixed-income issues	0	0	0	0	0	0	0
Preference shares	37	0	2	0	0	0	0
NOMINAL AMOUNT (million euros)	387,476	226,449	288,992	357,830	60,680	84,904	40,585
Mortgage bonds	35,574	34,378	67,227	102,170	29,800	13,020	8,195
Territorial bonds	500	5,900	22,334	8,974	1,674	0	0
Non-convertible bonds and debentures	62,249	24,356	20,192	86,442	91	39,815	15,562
Convertible/exchangeable bonds and debentures	3,200	968	7,126	3,563	0	843	425
Asset-backed securities	81,651	63,261	68,413	23,800	1,884	11,185	7,377
Domestic tranche	77,289	62,743	63,456	20,627	1,884	9,398	6,854
International tranche	4,362	518	4,957	3,173	0	1,788	523
Commercial paper ³	191,342	97,586	103,501	132,882	27,230	20,041	9,026
Securitised	4,758	5,057	2,366	1,821	275	300	180
Other commercial paper	186,583	92,529	101,135	131,061	26,955	19,741	8,846
Other fixed-income issues	0	0	0	0	0	0	0
Preference shares	12,960	0	200	0	0	0	0
Pro memoria:							
Subordinated issues	20,989	9,154	29,199	7,633	581	2,492	1,422
Covered issues	4,794	299	10	0	0	0	0
					2012		2013
abroad by Spanish issuers					3Q	4Q	1Q ⁴
NOMINAL AMOUNT (million euros)	149,686	127,731	120,043	92,083	17,330	20,100	8,800
Long-term	47,230	51,107	51,365	50,353	10,783	13,164	7,909
Preference shares	3,765	0	0	0	0	0	0
Subordinated debt	2,061	0	242	307	0	0	0
Bonds and debentures	41,404	50,807	51,123	50,046	10,783	13,164	7,909
Asset-backed securities	0	300	0	0	0	0	0
Short-term	102,456	76,624	68,677	41,730	6,547	6,936	891
Commercial paper	102,456	76,624	68,677	41,730	6,547	6,936	891
Securitised	108	248	322	11,590	2,756	1,695	-

Source: CNMV and Banco de España.

1 Incorporating issues admitted to trading without a prospectus being filed.

2 Data to 15 March.

3 Figures for commercial paper issuance correspond to the amount placed.

4 Data for the month of January. No data are available for foreign sales of securitised commercial paper in this month.

4 Market agents

4.1 Investment vehicles

Financial UCITS¹⁷

Assets under management in mutual funds dropped 6.3% in 2012 to just over 124 billion euros, their lowest level since the second half of the 1990s. This annual outflow, exceeding 8.30 billion euros, had its origin exclusively in unit-holder redemptions (11.50 billion in the year), while portfolio returns were a positive 5.5% (see table 13). Over 80% of the shrinkage, moreover, took place in the second quarter, as mounting financial market tensions provoked a flight of savings from the industry while eroding the value of portfolio investments. By category, the decline was steepest among fixed-income funds (6.28 billion euros), guaranteed equity funds (3.60 billion) and, in smaller measure, absolute return funds (1.39 billion). The only categories recording net inflows on any scale, and fitfully at that, were guaranteed fixed-income and passively managed funds.

Investment fund assets shrink by 6.3% to 124 billion euros as the redemption drain continues.

Net investment fund subscriptions

TABLE 12

Million euros	2010	2011	2012	2012			
				1Q	2Q	3Q	4Q
Total investment funds	-25,580.9	-10,839.0	-11,495.4	-1,652.3	-3,095.8	-3,176.6	-3,570.7
Fixed income ¹	-27,150.0	-10,427.7	-5,662.5	-726.9	-1,781.3	-1,880.9	-1,273.4
Balanced fixed income ²	-1,416.9	-1,925.7	-651.6	-237.9	-123.6	-173.6	-116.5
Balanced equity ³	-90.1	-320.5	-281.6	-134.0	-26.0	-68.3	-53.3
Euro equity ⁴	-696.9	152.0	-109.7	-151.5	67.8	-2.1	-23.9
International equity ⁵	1,151.9	-817.6	-370.2	-14.0	-113.8	-55.9	-186.5
Guaranteed fixed-income guaranteed	4,716.0	7,228.3	-334.5	584.1	-2.6	58.5	-974.5
Guaranteed equity ⁶	-2,500.1	-3,061.6	-3,353.1	-731.6	-700.6	-805.1	-1,115.8
Global funds	323.7	945.3	-7.8	157.9	-72.1	-101.1	7.5
Passively managed ⁷	-790.3	-274.5	572.1	29.3	114.6	67.8	360.4
Absolute return ⁷	871.8	-2,337.0	-1,296.5	-427.7	-458.2	-215.9	-194.7

Source: CNMV. Estimates only.

- 1 Includes: Euro and international fixed income and money market funds (as of 3Q 2011, money market funds encompass those engaging in money market and short-term money market investments, Circular 3/2011).
- 2 Includes: Euro and international balanced fixed income.
- 3 Includes: Euro and international balanced equity.
- 4 Includes: Euro equity.
- 5 Includes: International equity.
- 6 Includes: Guaranteed and partial protection equity funds.
- 7 New categories as of 2Q 09. Absolute return funds were previously classed as global funds.

Fund numbers continued to dwindle throughout 2012, which closed with 2,185 schemes in operation compared to 2,310 at end-2011. The reduction was greatest in those categories suffering the highest outflows, namely fixed income (54) and guaranteed equity (59), while growth was confined, by the same token, to guaranteed fixed income and passively managed funds.

Further decline too in the number of funds registered ...

17 Although this classification includes hedge funds and funds of hedge funds, we make no separate reference to them here, since they are the subject of their own sub-section further ahead.

Main investment fund variables*

TABLE 13

Number	2010	2011	2012	2012			
				1Q	2Q	3Q	4Q
Total investment funds	2,408	2,310	2,185	2,300	2,255	2,197	2,185
Fixed income ¹	537	508	454	491	479	459	454
Balanced fixed income ²	160	140	125	140	132	128	125
Balanced equity ³	138	128	117	130	122	119	117
Euro equity ⁴	172	148	127	143	135	129	127
International equity ⁵	232	220	211	222	220	214	211
Guaranteed fixed-income	276	351	398	375	385	393	398
Guaranteed equity ⁶	499	420	361	404	384	369	361
Global funds	192	203	192	200	198	194	192
Passively managed ⁷	61	59	85	64	75	75	85
Absolute return ⁷	141	133	115	131	125	117	115
Assets (million euros)							
Total investment funds	143,918.2	132,368.6	124,039.9	131,994.5	125,120.7	125,108.2	124,039.9
Fixed income ¹	56,614.6	46,945.5	40,664.6	45,101.8	42,837.8	41,512.2	40,664.6
Balanced fixed income ²	7,319.0	5,253.6	5,500.9	5,686.9	5,430.9	5,512.9	5,500.9
Balanced equity ³	3,470.5	2,906.1	3,179.9	3,234.2	3,040.3	3,116.2	3,179.9
Euro equity ⁴	5,356.8	4,829.2	5,270.2	4,815.6	4,516.5	4,891.7	5,270.2
International equity ⁵	8,037.3	6,281.2	6,615.0	6,813.2	6,373.7	6,663.2	6,615.0
Guaranteed fixed-income	26,180.2	35,058.0	36,445.0	36,677.0	35,421.7	36,489.9	36,445.0
Guaranteed equity ⁶	22,046.5	18,014.5	14,412.7	17,408.5	15,943.0	15,383.0	14,412.7
Global funds	4,440.3	5,104.7	4,358.6	4,545.5	4,272.1	4,288.4	4,358.6
Passively managed ⁷	2,104.8	1,986.2	2,991.2	2,053.9	2,190.9	2,456.2	2,991.2
Absolute return ⁷	8,348.1	5,989.7	4,601.9	5,657.8	5,093.9	4,794.4	4,601.9
Unit-holders							
Total investment funds	5,160,889	4,835,193	4,410,741	4,759,243	4,634,772	4,531,940	4,410,741
Fixed income ¹	1,622,664	1,384,946	1,261,634	1,362,443	1,326,504	1,297,686	1,261,634
Balanced fixed income ²	270,341	206,938	188,574	204,653	195,137	193,992	188,574
Balanced equity ³	171,336	145,150	138,096	145,472	141,784	140,387	138,096
Euro equity ⁴	266,395	237,815	220,433	224,886	225,774	220,342	220,433
International equity ⁵	501,138	448,539	398,664	442,753	432,816	417,276	398,664
Guaranteed fixed-income	790,081	1,042,658	1,075,852	1,071,544	1,070,002	1,082,897	1,075,852
Guaranteed equity ⁶	1,065,426	912,298	727,867	874,249	832,332	783,203	727,867
Global funds	105,720	127,336	101,321	113,396	105,966	105,824	101,321
Passively managed ⁷	90,343	100,416	125,003	101,901	108,166	110,678	125,003
Absolute return ⁷	277,445	229,097	173,297	217,946	196,291	179,655	173,297
Return⁸ (%)							
Total investment funds	0.35	-0.08	5.50	2.41	-1.75	2.72	2.08
Fixed income ¹	0.11	1.56	3.54	1.51	-0.47	1.35	1.12
Balanced fixed income ²	-0.54	-1.34	4.95	2.3	-1.55	2.41	1.75
Balanced equity ³	-0.98	-5.64	7.83	3.25	-2.9	4.12	3.3
Euro equity ⁴	-2.94	-11.71	12.31	3.34	-6.34	8.16	7.28
International equity ⁵	14.22	-10.83	13.05	8.91	-3.63	5.27	2.32
Guaranteed fixed-income	-0.67	3.28	4.85	2.48	-2.32	2.42	2.27
Guaranteed equity ⁶	-1.79	0.14	5.07	1.63	-2.43	3.89	1.99
Global funds	3.22	-4.64	7.44	3.56	-1.23	2.95	2.03
Passively managed ⁷	-2.36	-7.33	7.1	1.97	-4.31	5.50	4.04
Absolute return ⁷	1.53	-1.87	3.84	1.68	-1.04	1.81	1.36

Source: CNMV.

* Data for funds have filed financial statements (i.e., not including those in the process of winding-up or liquidation).

1 Includes: Euro and international fixed income and money market funds (as of 3Q 2011, money-market funds encompass those engaging in money market and short-term money market investments, Circular 3/2011).

2 Includes: Euro and international balanced fixed income.

3 Includes: Euro and international balanced equity.

4 Includes: Euro equity

5 Includes: International equity.

6 Includes: Guaranteed equity and partial protection equity funds.

7 New categories as of 2Q09. All absolute return funds were previously classed as global funds.

8 Annual return for 2009, 2010 and 2011. Quarterly data comprise non-annualised quarterly returns.

Unit-holder numbers closed the year at 4,410,000, 424,000 fewer than at end-2011. The decline was relatively steady throughout the year and hit mainly at guaranteed equity (184,000) and fixed-income funds (123,000).

... and unit-holder numbers,...

Preliminary data for January 2013 indicate a certain reversal of all these trends. According to the figures, investment funds assets would have increased 2% in the space of the month to 126.5 billion euros, on portfolio gains (1.1%) and net fund subscriptions (exceeding one billion euros). The recent cap imposed on bank deposit interests has presumably redirected funds into the industry's most deposit-like category, essentially fixed-income schemes (guaranteed or otherwise), though subscription volumes were also up in passively managed funds.

... though both trends have partially corrected in the early months of 2013.

The liquidity conditions of fund fixed-income portfolios continued to improve from mid-year on in absolute and relative terms. As we can see from table 14, the amount of less-liquid assets fell by over one billion euros between June and December, from 6.45 to 5.39 billion (-16.4%). On this showing, the ratio of less-liquid assets dropped from 5.2% of total fund assets in June 2012 to 4.3% at the annual close. As regards the composition of these less-liquid holdings, we can point to the growing share of financial institution debt instruments rated below AA (up from 69% to 76%) and a parallel decline in the weight of asset-backed securities (from 21% to 14%).

The liquidity conditions of private fixed-income portfolios continue to improve.

Estimated liquidity of investment fund assets

TABLE 14

Type of asset	Less-liquid investments					
	Million euros			% total portfolio		
	Jun 12	Sep 12	Dec 12	Jun 12	Sep 12	Dec 12
Financial fixed income rated AAA/AA	466	425	348	24	27	23
Financial fixed income rated below AAA/AA	4,443	4,514	4,120	19	20	19
Non-financial fixed income	165	132	148	6	4	5
Securitisations	1,374	966	774	50	41	42
AAA-rated securitisations	65	53	44	95	96	97
Other securitisations	1,309	912	730	49	40	40
Total	6,448	6,037	5,390	21	20	20
% of investment fund assets	5.2	4.8	4.3			

Source: CNMV.

Real estate schemes

The downturn in Spanish construction and real estate continued to make life hard for this category of funds, whose returns deteriorated further in 2012. By the end of the year, a total of six funds remained in operation, the same number as at end-2011, though only five were truly operative, with a sixth being wound up as we write. The number of real estate investment companies, meantime, was unchanged at eight.

The real estate and construction crunch continue to complicate life for real estate investment schemes in 2012.

On the fund side, main variables performed on a par with the previous years, though with declines smoothing slightly (except in returns). Hence fund assets decreased by 6.5% to 4.20 billion euros, while unit-holder numbers closed 4,517

Real estate funds lost 6.5% of their assets while returns sank to -6.0%.

lower at 25,218. Aggregate fund returns were negative in every quarter, summing a full-year loss of 5.96% (see table 15). Note also that a majority of these schemes' assets are in the hands of investors belonging to the management company's financial group.

Main real estate scheme variables

TABLE 15

	2009	2010	2011	2012				
				2012	1Q	2Q	3Q	4Q
FUNDS								
Number ¹	8	7	6	6	6	6	6	6
Unit-holders	83,583	75,280	29,735	25,218	29,754	27,716	27,587	25,218
Assets (million euros)	6,465	6,116	4,495	4,202	4,447	4,386	4,314	4,202
Return (%)	-8.31	-4.74	-3.23	-5.96	-0.86	-1.23	-1.83	-2.17
COMPANIES								
Number	8	8	8	8	8	8	8	8
Shareholders	928	943	943	937	939	939	935	937
Assets (million euros)	309	322	313	284.1	310.8	305.1	294.7	284.1

Source: CNMV.

1 Funds filing financial statements.

Assets under management in real estate investment companies down 9.2%.

Finally, assets under management in real estate investment companies dropped by 9.2% in 2012 to 284 million euros, while their shareholder numbers slipped from 943 to 937.

Hedge funds

Another divergent performance from the hedge fund industry ...

The hedge fund landscape was again defined by the slump in fund of hedge fund business, profoundly affected by the crisis, and a pure hedge fund segment in steady expansion by the measure of both assets and investor numbers. In both types of scheme, a significant number of funds are in the process of liquidation.

...with fund of fund assets down 4.7% to 546 million euros,...

As we can see from table 16, funds of hedge funds lost 4.7% of their assets between December 2011 and November 2012, as far as 546 million euros, while unit-holder numbers reduced by 420 to 3,385. Redemptions outstripped subscriptions in every quarter of the year (except the last, for which no data were available at the closing date for this report).

...compared to a 15% advance in pure hedge fund assets to 838 million euros.

Conversely, pure hedge funds increased their assets by 15.1% between December 2011 and November 2012, to over 838 million euros, and enlarged their unit-holder roll from 2,047 to 2,304. Asset growth drew on year-long fund subscriptions but also owed a lot to portfolio gains, except for a brief dip in the second quarter of 2012 with market tensions at their height.

	2009	2010	2011	2012			
				1Q	2Q	3Q	4Q ²
FUNDS OF HEDGE FUNDS							
Number ¹	38	28	27	27	28	26	24
Unit-holders	5,321	4,404	3,805	3,592	3,607	3,513	3,385
Assets (million euros)	810.2	694.9	573.0	568.0	561.4	561.3	545.8
Return (%)	7.85	3.15	-1.70	1.15	-2.21	1.36	
HEDGE FUNDS							
Number ¹	29	33	36	36	36	36	36
Unit-holders	1,917	1,852	2,047	2,077	2,169	2,305	2,304
Assets (million euros)	652.0	646.2	728.1	775.3	774.5	828.7	838.1
Return (%)	14.94	5.37	-2.60	3.66	-2.42	2.72	1.29

Source: CNMV.

1 Funds filing financial statements.

2 Data to November 2012.

Exhibit 4: “ESMA guidelines on remuneration policies under the Alternative Investment Fund Managers Directive (AIFMD)”

Directive 2011/61/EU of 8 June 2011 on alternative investment fund managers (AIFMD) calls on the European Securities and Markets Authority (ESMA) to develop guidelines on sound remuneration policies in accordance with the Directive’s Annex II. The AIFMD requires the managers of the funds within its scope (non-UCITS schemes such as hedge funds, venture capital funds, and real estate funds in Spain) to implement sound, prudent remuneration policies and structures in order to strengthen investor protection and prevent conflicts of interest which could lead to excessive risk taking. It was to comply with this assignment that ESMA approved the corresponding guidelines on 29 January 2013, to apply as of 22 July 2013.

The main issues these guidelines address are: 1) which remuneration items are covered, 2) the identified staff subject to their contents, 3) the application of proportionality, 4) corporate governance in remuneration matters, 5) standards for aligning interest and risk and 6) transparency. Each of these points is dealt with briefly in the paragraphs that follow.

For the purpose of the guidelines, remuneration consists of all forms of compensation paid by the manager, any amount paid by the fund itself, including carried interest, and any transfer of units or shares in respect of professional services rendered. Remuneration can comprise both a fixed and a variable component (depending on performance or other contractual criteria) and may include monetary payments or benefits (such as cash, shares, options or pension contributions) or non-monetary benefits (discounts, car allowance, mobile phone, etc.).

The staff within the scope of the guidelines (identified staff) are all those whose professional activities have a material impact on the risk profile of the manager or the funds it manages, along with the staff of any entity to whom the manager has delegated risk management or investment management functions. The manager is obliged to identify all such groups of staff.

The diverse risk profiles and characteristics of managers, as regards their own size and that of the funds they manage, their internal organisation and the nature, scope and complexity of their activities, justifies a proportional approach to compliance with these guidelines, allowing certain requirements to be adapted to each manager's particular circumstances (setup of a remuneration committee, variable remuneration in instruments, establishment of a deferral period for payment in kind, among others).

The guidelines approach the governance of remuneration by reference primarily to the supervisory function and the remuneration committee. Proportionality operates in both cases, to the extent that having a remuneration committee may be optional for certain AIFMs. The supervisory function is responsible for evaluating and reviewing the manager's procedures on a regular basis. It is accordingly in charge of approving and maintaining the remuneration policy of the AIFM and overseeing its implementation, and should also approve any subsequent material exemptions or changes and carefully consider and monitor their effects. The remuneration committee, where one exists, should be made up of non-executive members of the supervisory function, the majority of whom qualify as independent. Among its main responsibilities is to support and advise the supervisory function in designing remuneration policies and to ensure that such policies are in line with the objectives and interests of the AIFM, the AIFs it manages and the investors of such AIFs.

The guidelines include a series of measures to promote the better alignment of interests and risk. These are of binding application to the remuneration packages of identified staff, though managers are urged to consider their AIFM-wide application. Their first requirement is that managers should implement a fully flexible policy of variable remuneration, which should be exclusively associated to the achievement of objectives by identified staff. Fixed remuneration, by the same token, should be sufficiently high to remunerate the professional services rendered, in line with level of education, degree of seniority, level of expertise required, etc.

Variable remuneration is the key element in any remuneration system that seeks an optimal alignment of interests and risk. For ESMA, a fully flexible policy means that this remuneration component should be performance-based and risk-adjusted, such that incentives to take risks are constrained by incentives to manage risk in an effective manner. To this end, the guidelines specify three phases or subprocesses for the calculation and implementation of variable remuneration.

The first phase (performance and risk measurement process) concerns the accrual period during which the right to receive variable remuneration is earned, and the measurement of the risk-adjusted performance that serves as its calculation base (although it also contemplates adjusting performance measures for risk

at a later stage). Performance assessment can make use of both quantitative and qualitative criteria, including judgmental measures, as long as they are properly documented. Regarding the length of the accrual period, the text specifies a minimum of one year, while pointing out that multiyear periods allow for greater certainty, given the longer time horizon of most managed funds.

The second phase, the award process, and the third, the pay-out process, refer respectively to the process of determining individual awards, and the form and timing of variable payment. In the second phase, the manager must translate its risk-adjusted performance assessment into a variable remuneration component for each staff member. The main difficulty here is in determining how individuals have contributed to carry risk, given that some risks may materialise in future, and adjusting accordingly. In the pay-out phase, managers have the opportunity to adjust variable payments through contractual arrangement known as clawbacks, when the staff member agrees to return ownership, or maluses, when payment is reduced or cancelled on evidence of misconduct, such that remuneration reflects actual risk outcomes and the real achievement of objectives. To facilitate such ex-post adjustments in variable remuneration, 40% to 60% of payment should be deferred for a period of between three and five years. Likewise, for the purpose of better aligning the interests of managers and clients, the guidelines state that at least 50% of variable remuneration, including both the upfront and deferred part, should be paid in financial instruments issued by or bearing a close link to managed vehicles (for instance, shares or share-related instruments), specifying a retention period during which they cannot be sold.

Finally, a set of guidelines deal with managers' obligations regarding the internal and external disclosure of remuneration information, primarily information of a qualitative nature. Disclosure reports should be published annually at least and set out the decision-making process used to determine remuneration payments, how pay and performance are linked, a description of the main performance metrics used, and how they take into account current and future risks, in a way that is clear and easily understandable to the reader.

Foreign UCITS marketed in Spain

Investment in foreign UCITS expanded by 26.8% after the contraction of the previous year, to close at 38 billion euros. This level of investment, surpassing the figure for 2010, owed to the higher volumes captured by investment companies, while funds reported some erosion across all key variables. The number of investors and schemes also rose in the year by 7.2% to 816,417 and by 2% to 754.

Investment in foreign UCITS climbs 26.8% to almost 38 billion euros.

Outlook

The collective investment industry has suffered more than most from the consequences of the crisis, with unit-holder redemptions escalating to all-time highs. These persistent outflows, aggravated at times of stress by a slump in investor confidence, are also the result of fierce competition from low-risk investment products marketed by the banks, primarily deposits and, more recently, commercial paper,

The redemption flood of recent years, which has left industry assets at an all-time low,...

whose attractive conditions marked an attempt by deposit-taking entities to draw in customer funds at a time of scarce liquidity.

...may be stemmed in the coming months, as competition from other investment products slackens off.

In the short term, we can see both good and bad portents for the investment fund industry. On the one hand, the ongoing recapitalisation and restructuring of the Spanish banking system will facilitate banks' access to alternative funding sources (the markets, for instance), and this, along with the recently imposed interest rate caps on bank deposits, could boost investment fund inflows over coming months. On the other, the savings constraints faced by households coping with lower disposable income could limit the industry upside. Also, a new wave of sector reorganisation could be just around the corner, given the numerous schemes operating in losses and the prospect of further management company mergers or acquisitions as bank restructuring continues its course.

4.2 Investment firms

Investment firm business suffers a historical setback in 2012.

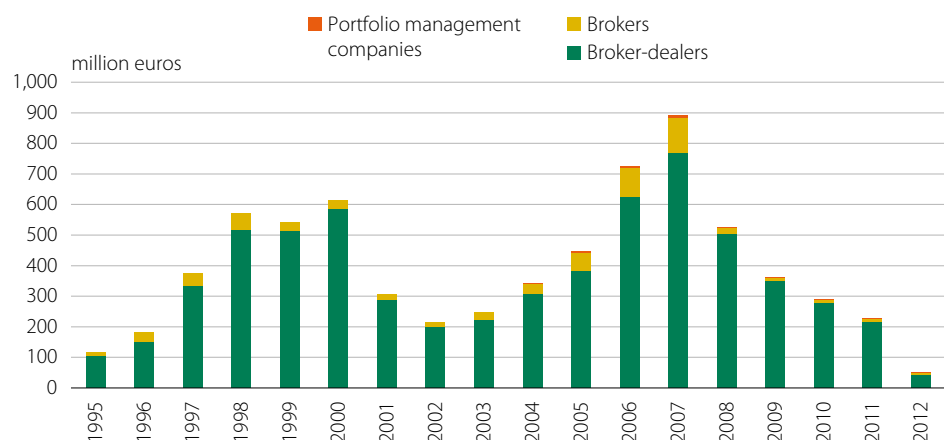
For the fifth year running, investment firms had to struggle with the fallout from domestic market turmoil, which has driven down revenues across all main business lines. In this complex landscape, the number of loss-making firms was unchanged with respect to 2011, but the volume of their losses was substantially higher. Sector capital adequacy remained in the safety zone, albeit with some narrowing of margins.

Broker-dealer pre-tax profits fall 81% on a slump in income from financial investments and investment service fees ...

The aggregate pre-tax profits of broker-dealers plunged by 81% in 2012 to 42 million euros, with the fall tracing mainly to financial investments and investment service fee income (see table 17). Closer examination of this last item shows that income on order processing and execution decreased by 34% to 348 million euros, in line with the trading contraction on domestic financial markets. Other captions suffering a reverse were investment advisory services (down by 91% to 5.1 million) and UCITS marketing (down 24% to 45 million euros). The 71% advance under the "others" caption to 149 million euros and lower exchange rate losses failed to offset the decline under remaining income heads, driving gross income down to 448 million, 32% less than in 2011.

Investment firm pre-tax profits^{1,2}

FIGURE 17



Source: CNMV.

1 Except IAFs.

2 2012 earnings on an annual basis.

Aggregate income statement (2012)

TABLE 17

Thousand euros	Broker-dealers			Brokers			Portfolio managers		
	Dec 11	Dec 12	% var.	Dec 11	Dec 12	% var.	Dec 11	Dec 12	% var.
1. Net interest income	91,542	56,185	-38.6	2,481	1,910	-23.0	682	732	7.3
2. Net fee income	490,517	410,729	-16.3	97,886	93,235	-4.8	7,988	7,879	-1.4
2.1. Fee income	776,641	588,890	-24.2	112,351	108,187	-3.7	18,477	17,887	-3.2
2.1.1. Order processing and execution	529,711	348,273	-34.3	36,354	38,111	4.8	-	-	-
2.1.2. Issue placement and underwriting	7,446	6,869	-7.8	2,870	3,128	9.0	-	-	-
2.1.3. Securities custody and administration	21,060	19,775	-6.1	441	588	33.3	-	-	-
2.1.4. Portfolio management	16,186	14,882	-8.1	12,352	14,454	17.0	16,582	16,307	-1.7
2.1.5. Investment advising	55,025	5,138	-90.7	5,349	3,092	-42.2	1,894	1,579	-16.6
2.1.6. Search and placement	485	50	-89.7	61	88	44.3	-	-	-
2.1.7. Margin trading	8	8	0.0	42	30	-28.6	-	-	-
2.1.8. UCITS marketing	59,588	45,050	-24.4	21,381	25,949	21.4	0	0	-
2.1.9. Others	87,133	148,846	70.8	33,500	22,745	-32.1	0	0	-
2.2. Fee expense	286,124	178,160	-37.7	14,465	14,952	3.4	10,489	10,008	-4.6
3. Result of financial investments	271,956	9,403	-96.5	622	1,254	101.6	186	4	-97.9
4. Net exchange income	-198,307	-37,362	81.2	78	-106	-	29	-30	-
5. Other operating income and expense	3,952	8,841	123.7	-1,617	-1,356	16.1	-40	29	-
GROSS INCOME	659,659	447,796	-32.1	99,450	94,938	-4.5	8,845	8,615	-2.6
6. Operating expenses	426,672	375,782	-11.9	89,736	87,624	-2.4	7,210	7,122	-1.2
7. Depreciation and other charges	21,532	23,556	9.4	1,944	2,781	43.1	109	87	-20.2
8. Impairment losses	4,076	12,904	216.6	12	-12	-	0	0	-
NET OPERATING INCOME	207,379	35,555	-82.9	7,758	4,545	-41.4	1,526	1,406	-7.9
9. Other profit and loss	9,861	6,450	-34.6	412	2,371	475.5	0	5	-
PROFITS BEFORE TAXES	217,240	42,005	-80.7	8,170	6,916	-15.4	1,526	1,411	-7.5
10. Corporate income tax	68,687	53,786	-21.7	2,681	3,383	26.2	484	458	-5.4
PROFITS FROM ONGOING ACTIVITIES	148,553	-11,782	-	5,489	3,533	-35.6	1,042	952	-8.6
11. Profits from discontinued activities	0	0	-	0	0	-	0	0	-
NET PROFIT FOR THE YEAR	148,553	-11,782	-	5,489	3,533	-35.6	1,042	952	-8.6

Source: CNMV.

Although broker-dealers managed a 12% reduction in operating expenses, their elevated levels (376 million euros), combined with deepening impairment losses, made further inroads into net operating income, which closed 83% down on year-ago levels at 35.5 million euros. It bears mention, however, that the sub-sector's aggregate profit figure was significantly distorted by the performance of one sector operator, without whom the overall decline in profits lessens to 18%.

...despite positive progress in operating cost contention.

Brokers, meantime, recorded pre-tax profits of 6.9 million euros, 15.4% less than in 2011 (8.2 million). Net fee income, which contributes over 98% of their total gross income, dropped by 4.8% in 2012 to 93.2 million euros. The story, however, varied significantly from one line to the next, with higher inflows from order processing and execution fees (up 4.8% to 38 million euros), UCITS marketing (up 21.4% to 26 million euros) and portfolio management (up 17% to 14.4 million euros), countered

Broker profits fall by 15% in 2012, in spite of rising revenues in traditional business lines,...

by a sizeable decline in fees from other services (down by 32.1% to 22.7 million euros). The result was a 4.5% fall in gross income to 94.9 million euros. Here too, companies made some headway in operating cost contention (down 2.4% to 87.6 million), but not enough to annul their dampening effect below the gross income line.

...while portfolio managers see their profits slide by 7.5%.

Finally, the aggregate pre-tax profits of portfolio management companies fell by 7.5% in the full-year period to 1.4 million euros. Aggregate gross income slipped by 2.6% to 8.6 million euros, due mainly to the decrease in net fee income (-1.4% to 17.9 million euros), its largest component. Operating expenses, meantime, were 1.2% lower at 7.1 million euros.

Sector ROE sinks from 15% to 11.6% on the first-half earnings stall.

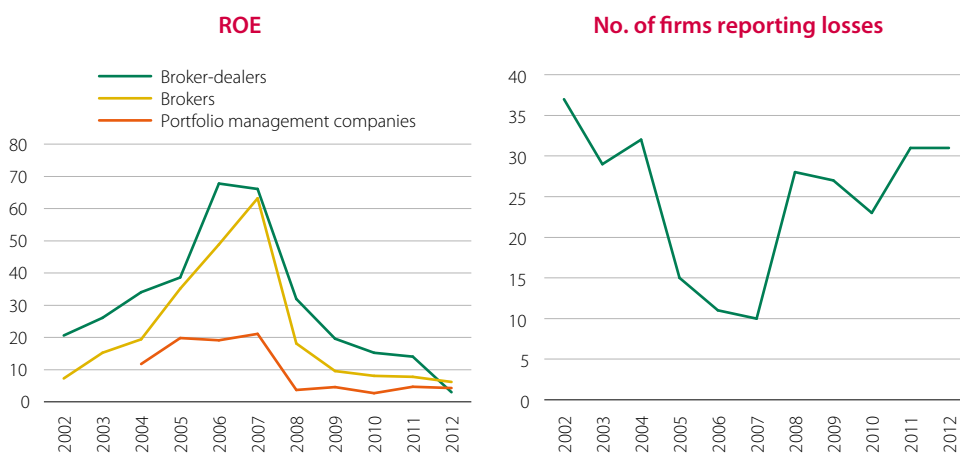
Sector-wide return on equity (ROE) sank from 11.8% in 2011 to 3% in 2012, in line with the year-long slide in investment firm earnings. By sub-sector, the ROE of broker-dealers took the biggest punishment, with a fall of over eleven points to 3%. Other intermediaries got off more lightly, with declines of over one point, to 6.2%, in the case of brokers, and less than 0.5 points, to 4.2%, in that of portfolio management companies (see figure 18, left-hand panel).

The number of loss-making firms is unchanged, but the size of their losses is six times greater.

Against this sector-wide backdrop of income and earnings decline, 31 firms reported pre-tax losses, the same number as in 2011, although the scale of these losses was considerably greater. Also the numbers are deceptive in that eight firms that ceased trading in the year. Of the total of loss-making firms in operation at the 2012 close, 14 were broker-dealers (13 in 2011), 15 were brokers (17 in 2011) and two were portfolio management companies (one in 2011). Their combined attributable losses in the period stood at 154.5 million euros, almost six times more than the 27 million of the previous year, and triple the sector's aggregate pre-tax profits for 2012.

Pre-tax ROE of investment firms and loss-making entities

FIGURE 18



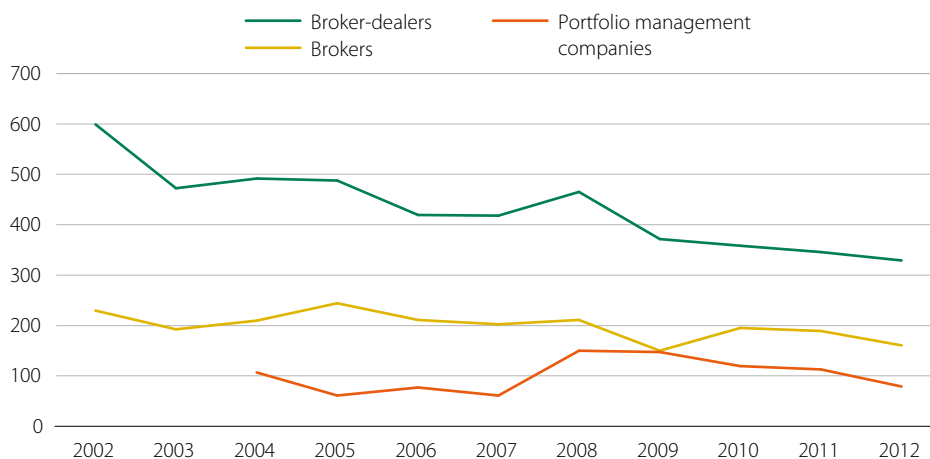
Source: CNMV.

Sector capital ratios remain comfortably clear of minimum requirements.

Investment firms remained comfortably compliant with capital standards, though it bears mention that their surpluses have narrowed by 30% since the advent of new, stricter capital standards in June 2009. The aggregate capital adequacy ratios of the investment firm sector contracted slightly to end-2012, as far as 3.3 times the minimum requirement in the case of broker-dealers (3.5 in 2011), 1.6 times for the broker group (1.9 in 2011) and 0.8 times for portfolio managers (1.1 in 2011).

Investment firm capital adequacy
(surplus of qualifying equity to the minimum requirement, %)

FIGURE 19



Source: CNMV.

The onward march of investment advisory firms (IAFs) showed signs of faltering in 2012. The number of these firms, which began operating in Spain in 2009 with the transposition of the MiFID, rose from 82 in 2011 to 101 in 2012, but this time business volumes failed to accompany in either assets under advice (down by 8.3% to 14.70 billion euros) or financial advisory contracts outstanding (down 5.7% to 3,468). The bulk of assets under advice (78% of the total) again corresponded to the professional clients segment, with the remaining 22% drawn from retail clients. Sector fee income fell by 18.4% to 25.3 million euros, while aggregate profits, at 3.6 million, were 52.5% less than in 2011 (see table 18).

IAF expansion threatens to run out of steam.

The outlook for investment firms is far from clear, in view of the grave erosion of traditional revenue streams like order processing and securities placements, and the deterioration suffered by the collective investment industry. One exception in this scenario is companies' growing income from corporate intelligence services, once marginal to their main business. To date, bank sector restructuring has had little impact on sector organisation, accounting for just two of last year's eight closures, with one more likely in 2013. However, the growing scale of some firms' losses could prompt additional moves to reorganise the sector via mergers and/or closures.

The heavy losses of the investment services sector suggest a degree of reorganisation may be in the wings.

Main investment advisory firm variables

TABLE 18

Thousand euros	2010	2011	2012	2012		% semi-annual change	% annual change
				1H	2H		
NO. OF FIRMS	52	82	101	97	101	4.1	23.2
ASSETS UNDER ADVICE¹	15,802,743	16,033,109	14,708,739	14,663,856	14,708,739	0.3	-8.3
Retail customers	1,715,084	2,181,943	3,201,927	2,415,002	3,201,927	32.6	46.8
Professional customers	13,995,206	13,831,973	11,452,681	12,205,216	11,452,681	-6.2	-17.2
Others	92,453	19,193	54,132	43,638	54,132	24.1	182.0
NO. OF CONTRACTS	2,431	3,677	3,468	3,279	3,468	5.8	-5.7
Retail customers	2,345	3,542	3,265	3,099	3,265	5.4	-7.8
Professional customers	79	126	185	164	185	12.8	46.8
Others	7	9	18	16	18	12.5	100.0
FEE INCOME²	20,745	31,052	25,347	13,940	25,347	81.8	-18.4
Fees received	20,629	30,844	25,171	13,855	25,171	81.7	-18.4
From customers	17,132	26,037	20,525	11,668	20,525	75.9	-21.2
From other entities	3,497	4,807	4,646	2,186	4,646	112.5	-3.4
Other income	116	209	175	85	175	105.9	-16.3
EQUITY	10,057	12,320	15,123	13,098	15,123	15.5	22.8
Share capital	3,014	3,895	4,448	4,328	4,448	2.8	14.2
Reserves and retained earnings	242	950	7,125	5,904	7,125	20.7	650.0
Profit/loss for the year ²	6,801	7,474	3,550	2,866	3,550	23.9	-52.5

1 Period-end data at market value.

2 Cumulative data for the period.

Exhibit 5: “CNMV’s adoption of the ESMA guidelines on suitability”

On 25 June 2012, ESMA published a set of guidelines whose aim was to clarify certain aspects of the MiFID suitability requirements in order to ensure their common, uniform and consistent application.¹

National authorities must expressly notify ESMA of the adoption of these guidelines, which the CNMV has duly done while issuing a communication on the subject.

The guidelines came into force on 21 December, 2012 and, as such, have been incorporated into the Commission’s supervisory practices. It bears mention, however, that the CNMV was already applying many of their key tenets (see communication of 19 October) and had published a guide on the subject in 2010.²

Set out below are the main points covered by the guidelines:

1. Who:

These guidelines apply to investment firms, including credit institutions that provide investment services, UCITS management companies, and competent authorities.

2. What:

Suitability requirements apply in relation to the provision of investment advice and portfolio management services, as stipulated in article 19.4 of the MiFID and articles 35 and 37 of its Implementing Directive 2006/73/EC. Although they mainly address situations where services are provided to retail clients, they should also be considered as applicable, where relevant, to the services rendered to professional clients

3. Steps to be taken by service providers:

- Improve the information given to clients about suitability testing. Investment firms should inform clients of the reasons for assessing suitability, thereby encouraging them to provide full and accurate responses. At no stage should investment firms or UCITS managers create any ambiguity or confusion about their own responsibilities in the process.
- Establish and implement policies and procedures that enable them to understand the essential facts about their clients and the characteristics of the financial investments available to them. Among the essential facts to be gathered are the client's age, marital status, family situation, employment situation and need for liquidity.
- Ensure that staff involved in material aspects of the suitability process have an adequate level of knowledge and expertise, and, to this end, provide point-of-sale staff with the appropriate training.
- Determine which information is necessary and relevant in relation to a client's knowledge and experience, financial situation and investment objectives by reference to the complexity of the products and services at stake. This proportionality test is of capital importance in two situations: (i) illiquid financial instruments, when the information gathered must include the length of time for which the client is prepared to hold the investment, as specified by the client and checked exhaustively by the provider, and (ii) the difference between investment advice and portfolio management services – what matters in the first case is that the client is able to understand the risks and nature of each financial instrument that the firm plans to recommend, and, in the second, that the client understands the overall risk of his or her portfolio.
- Take steps to ensure that the information collected is consistent and not overly reliant on clients' self-assessment.
- Keep information fully updated when a service is being provided on an ongoing basis.
- Establish criteria to determine who should be subject to the suitability assessment when the client is a legal person or a group of two or more natural persons, or where one or more natural persons are represented by another. Make a record of any agreement concluded to this effect.

- Ensure the suitability of the investment, such that assessments consistently take into account (i) all relevant information about the client (including their current portfolio of investments); (ii) the match between this information and the recommendations made, with particular regard to risk diversification, costs, time horizon and conflicts of interest; and (iii) whether the client has an adequate understanding of the relationship between risk and return.
- Maintain adequate records regarding the suitability assessment, including any investment advice provided and all investments (or divestments) made, in such a way as to enable the detection of failures.

1 *Guidelines on certain aspects of the MiFID suitability requirements.* Available at <http://www.esma.europa.eu/system/files/2012-387.pdf>

2 *Guía de actuación para el análisis de la conveniencia y la idoneidad.* Available at <http://www.cnmv.es/portal/verDoc.axd?t={56cad31c-e05c-4edd-9d07-a4f84e3cd116}>

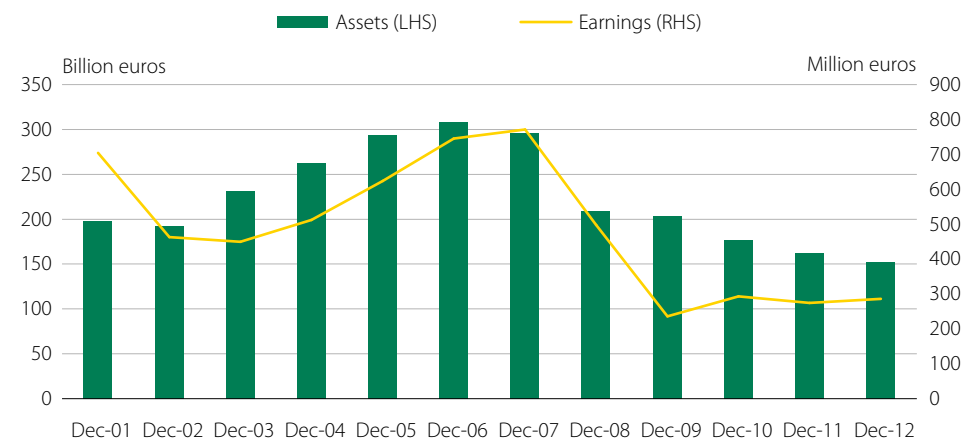
4.3 UCITS management companies

Despite a 5.5% drop in assets to 152.6 billion euros,...

Assets under management in UCITS management companies fell by 5.5% in 2012 to 152.60 billion euros. Though 94% of the difference corresponded to securities investment funds, real estate funds and investment companies also suffered to some extent. The sector's asset volumes have been declining since the crisis broke, though the rate did slow a little in 2012 (see figure 20).

UCITS management companies: assets under management and pre-tax profits

FIGURE 20



Source: CNMV.

...UCITS managers are able to grow their profits 4.1%.

Management companies were able, nonetheless, to grow their pre-tax profits by 4.1% in 2012 as far as 286 million euros, with a sharp decrease in fees paid (96% in respect of fund marketing) and higher inflows from portfolio management offsetting a 4.3% fall in fund management fees to 1.42 billion euros (see table 19). Average UCITS management fees inched up from 0.90% to 0.93%, reflecting a shift in the fund mix towards riskier categories that tend to carry higher fees. Sector-wide

return on equity (ROE) climbed from 20.7% in 2011 to 23.1%, while the number of loss-making entities dropped back from 32 to 28, generating combined red numbers of 10.2 million euros (11.3 million in 2011).

Management companies' ongoing effort to rationalise their fund offering by means of multiple product mergers was accompanied once more by some timid advances in sector reorganisation, with one new entrant versus ten retirals thinning their ranks to 105 at the 2012 close. Of the ten closures, seven were an offshoot of the broader restructuring of Spanish banks.

Fund mergers are accompanied by some weeding-out of management companies.

UCITS management companies: assets under management, management fees and fee ratio

TABLE 19

Million euros

	Assets under management	UCITS management fee income	Average UCITS management fee (%)	Fee ratio (%) ¹
2003	231,458	2,304	1.00	73.8
2004	262,132	2,670	1.02	73.6
2005	293,973	2,976	1.01	72.2
2006	308,476	3,281	1.06	71.5
2007	295,922	3,194	1.08	70.5
2008	209,014	2,302	1.10	70.8
2009	203,730	1,702	0.84	68.6
2010	177,055	1,622	0.91	68.1
2011	161,481	1,479	0.90	66.6
2012	152,644	1,416	0.93	64.6

Source: CNMV.

1 Ratio of fee expenses for fund marketing to fee income from UCITS management.

4.4 Other intermediaries: venture capital

The number of venture capital entities (VCEs) increased slightly over full-year 2012, from 336 to 340 (see table 20). Of this total, 139 were venture capital companies (VCCs), 119 venture capital funds (VCFs) and 82 VCE management companies. Twenty-two entities joined the register during the year (ten VCCs, eight VCFs and four VCE managers) compared to 18 retirals, the majority of them (14) VCCs. Points to note were that most new entrants (83%) continued to sign up for the simplified regime, and that the public sector has downsized its industry presence to just two VCCs.

The number of venture capital entities rises slightly in 2012

According to preliminary data furnished by industry association Asociación Española de Entidades de Capital Riesgo (ASCRI), venture capital investment in Spain receded 22.5% in 2012 as far as 2.52 billion euros. As much as 94% of the total, significantly, corresponded to transactions of less than five million euros. This evidences the scale of the investment effort being made in Spanish SMEs, with early-stage companies, in particular, featuring in 38% of the year's transactions. Leveraged buyouts, meantime, accounted for 54% of total investment but only 1.7% of

According to ASCRI, sector investment receded 22.5% in 2012...

transaction numbers. International funds were again prominent, as the source of 60% of annual investment. The sectors attracting most investment were “other services” (26%), products and services (14.5%), medicine and health (13.6%) and communications (10.8%), while IT ventures headed the transaction list (32%). Finally, the venture capital sector raised 2.17 billion euros for its investments, 9% less than in 2011. Of this total, 70% corresponded to international funds investing in Spain.

Movements in the VCE register in 2012

TABLE 20

	Situation at 31/12/2011	Entries	Retirals	Situation at 31/12/2012
Entities	336	22	18	340
Venture capital funds	114	8	3	119
Venture capital companies	143	10	14	139
Venture capital management companies	79	4	1	82

Source: CNMV.

...in what remains a challenging business landscape.

The short-term outlook for the venture capital sector remains hazy for a number of reasons. Foremost among them, the deterioration of domestic activity and the difficulty of obtaining bank finance, which appears likely to last until the end of the financial sector restructuring process. In this uncertain climate, the identification of growth opportunities will be paramount in future.

II Reports and analyses

Empirical study on the bans on short selling in Europe in 2011 and 2012

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1 Introduction

In 2011 and 2012, various European securities markets authorities placed a ban on creating or increasing covered short positions in shares listed on their markets (hereinafter, ban on short selling). The CNMV, together with French, Belgian and Italian authorities, established this restriction in 2011 for shares of financial companies and lifted it in February 2012. The escalation in financial tensions in Italy and Spain led those countries to apply this measure again in July 2012, with the CNMV extending the restriction to non-financial securities. In September, the Italian CONSOB allowed this type of trading once again, while the CNMV authorised it on 31 January 2013.

Short selling is positive for market efficiency as it incorporates the opinions of the most pessimistic investors. Banning short selling therefore decreases the liquidity of the shares and increases volatility. However, in circumstances of high volatility, uncertainty and systemic risk, the possibility of taking short positions may prove an incentive to spurious price movements in securities markets. Accordingly, dissemination of incorrect signals in those situations is more likely to affect prices in the secondary market and even the fundamental value of companies. Furthermore, due to the presence of systemic risk, it may reduce the ability of other public and private issuers to raise finance. In this regard, the ban on short selling could be positive if applied as a temporary measure whilst the problems generating the high volatility are being solved.

This document describes the circumstances in which the bans on short selling were adopted in Europe, both the ban in 2011 and the ban in 2012, and how markets evolved while the bans were in force. The document then goes on to analyse the behaviour of the share prices of the Eurostoxx 300, their volatility, their trading and their liquidity over the time they were subject to a ban on short selling.¹

The article is structured as follows. Section 2 summarises the literature on short selling. It also indicates the conditions under which short selling may create multiple equilibriums and generate inefficient results and, finally, it describes the empirical contributions and limitations of this document. Section 3 offers information on the situation during the periods over which the measure was applied, specifically analysing the correlation between share prices and public debt, which is the variable believed to approximate systemic risk. Section 4 describes the behaviour of the prices and implied volatility of the European shares which were subject to the ban on short selling. Section 5 analyses the variations in trading and liquidity associated with the bans on short selling and includes a specific study of the evolution of the Spanish stock market during the ban which began in 2012. The conclusions are presented at the end.

1 Unless another period is explicitly mentioned, this document uses data for the period from 04/01/2010 to 04/03/2013.

2 Academic literature and empirical limitations

2.1 Academic literature

2.1.1 Short selling and the functioning of securities markets

One of the first studies on the effect of short positions is that of Diamond and Verrecchia,² in which the authors model stock market trading in the presence of constraints on short selling. Banning short selling reduces the trading of the investors who are most pessimistic about the fundamental value of the company. The market price, which is ideally a function of individual forecasts, will therefore suffer upward bias and its informational efficiency will be reduced.

Beber and Pagano³ explained that the deterioration of the price discovery process generated by the ban on short selling has an ambiguous effect on share liquidity. Firstly, the reduction in the informational quality of the price will lead to greater uncertainty, which in turn leads to a fall in liquidity. However, on the other hand, if the investors who could have conducted short selling are mostly investors with superior information, the ban reduces their ability to operate and allows market-makers to reduce their spreads.

The above authors performed a study on the application of the ban and its effects during 2008-2009 for 30 countries, exploiting cross-country variations in legislation and the variations generated because these measures were applied at different moments in time. Their results indicate that the aforementioned bans on short selling are negative for market liquidity and reduce the efficiency of the price discovery process. Furthermore, they consider that the ban on short selling had no discernible effect on the level of share prices, which the authors believe was the reason for the bans. An interesting result is that information transparency on short positions has a positive effect on liquidity. This transparency measure was adopted by the CNMV in 2008.

Arce and Mayordomo⁴ analyse the ban on short selling applied in 2011 in Spain and other European countries and find that it led to a reduction in liquidity, trading volume and the efficiency of price discovery. These results are particularly noticeable in medium-sized banks, which were the most affected by the uncertainty.

In addition to this worsening of market functioning, it is also important to remember that the ban on short selling limits the possibilities which investors have for portfolio design, which may reduce the appeal of other shares. For example, an investor may wish to purchase shares of a Spanish company, but avoid the general country risk. To do this, the investor would buy shares of the company they are interested in and create a short position in other Spanish shares. As the ban limits this type of trading, it may in the end discourage investment in the first company.

2 D. Diamond and R. Verrecchia (1987), "Constraints on short-selling and asset price adjustment to private information", in *Journal of Financial Economics*, vol. 18, pp. 277-311.

3 A. Beber and M. Pagano (2013), "Short-Selling Bans around the World: Evidence from the 2007-09 Crisis", in *Journal of Finance*, vol. 68, pp. 343-381, February.

4 Ó. Arce and S. Mayordomo (2012), *Short-sales Constraints and Financial Stability: Evidence from the Spanish 2011 Ban*, available at <http://papers.ssrn.com>

2.1.2 Short selling in situations of financial instability

In general, investors will want to take a short position when the market price is higher than their estimate of the fundamental value of a company. Given that the price is based on the average expectations of different investors, and that these individual expectations are, by definition, much more varied at times of high uncertainty, it will be specifically at these times when there are more short positions. It is therefore important to remember that, in general, it is uncertainty that causes the appearance of short positions and not the reverse.

However, establishing short positions generates an incentive to attempt to achieve a fall in the prices of the affected assets. This debate is reproduced by Krugman⁵ for Hong Kong in the Asian crisis. At that time, hedge funds established short positions in Hong Kong shares and long positions in assets denominated in US dollars, expecting to benefit from a possible devaluation of the currency or, otherwise, from a defensive increase in the interest rate which would reduce share values. However, according to Hong Kong officials, “the hedge funds weren’t just betting on these events [...] the sales of Hong Kong dollars were ostentatious, carried out in large blocks [...] so as to make sure everyone in the market noticed. [...] the hedge funds paid reporters and editors to run stories suggesting that the Hong Kong dollar or the Chinese renminbi, or both, were on the verge of devaluation. In other words, they were deliberately trying to start a run on the currency”.

The fact that there are investors who will benefit from a specific evolution in prices, either upwards or downwards, and have incentives to attempt to manipulate prices is common in securities markets. Supervisors prevent and pursue this behaviour without requiring extraordinary measures such as the ban on short selling. What is different about the current situation is the grave uncertainty which exists both from a microeconomic and a macroeconomic point of view. This grave financial uncertainty or instability means that manipulating prices downwards may be relatively easy and can cause greater damage.

For the ban on short selling to produce positive effects, it must simultaneously meet the following conditions, which are more likely in these situations of high uncertainty.

The first condition is that it must be possible to influence the price in the secondary market. In situations of high volatility, the price is more sensitive to information which reaches the market both through news and rumours, and through the flows traded in the market. Therefore, strategic dissemination of negative information not based on the fundamentals of the company may lead to a greater temporary impact on the price.

However, as this strategy is not based on fundamental information, it would have a merely temporary effect on the share price, which would disappear when the informational confusion disappears, with relatively little damage. The only permanent effect which it might cause is that described by Shkilko, Van Ness and Van Ness:⁶

5 P. Krugman (1999), *The return of depression economics*, W. W. Norton.

6 A. Shkilko, B. Van Ness and R. Van Ness (2008), *Aggressive Short Selling and Price Reversals*, AFA 2008 New Orleans Meetings Paper, available at: <http://ssrn.com>

that the perceived increase in volatility discourages some investors from entering the market, generating a persistent decrease in the price.

The second condition is that the secondary market price may affect the fundamental value. If, due to the grave uncertainty, it is possible to alter the short-term market price, as described above, there is also the possibility in extreme cases of generating permanent effects on the fundamental value of the affected company. There is therefore a permanent deterioration in the value, which, in addition, benefits whoever has altered said value if they have previously established short positions.

The route whereby the phenomenon outlined above occurs has been described by Goldstein and Guembel,⁷ including the possible benefit which the price manipulator would obtain as a result of generating a self-fulfilling prophecy. Liu⁸ specifies this for banks, which are the most sensitive companies to this phenomenon as a large part of their liabilities are very liquid. In situations of extreme volatility and uncertainty, it cannot be ruled out that sudden adjustments in the share price of the company may lead to a worsening of its financing conditions in primary securities markets, in its borrowing through loans or, in the case of banks, in the costs to retain and attract depositors. This is due to the fact that the stock market is one of the most liquid and visible markets and therefore a sharp fall in the price in the secondary market may be interpreted by those providing finance to the company as an indication of a worsening of the company's economic situation which they are unaware of.

The increase in the issuer's cost of financing has a negative effect on the company's fundamental value. Consequently, a spurious movement in the secondary market may end up generating a self-fulfilling prophecy i.e. the dissemination of negative information without an economic basis may in itself generate a worsening in said economic basis. Furthermore, as Venter⁹ explains, the generation of this negative equilibrium does not require the existence of a person who manipulates the share price, but it may arise as an uncoordinated equilibrium between different agents who aim to protect themselves from what other agents may do.

Liu (2010) believes that only those with short positions in a company may benefit from generating self-fulfilling prophecies through price manipulation, since they are the only ones who can benefit from an increase in the perceived risk associated with the issuer. This explains how a ban on this type of trading may be particularly useful.

The third condition is that the aforementioned phenomena may affect other issuers. Accordingly, a context of high systemic risk would act as a catalyst able to strengthen the aforementioned reaction. A strong dependence between different issuers may make it easier to achieve the objectives, due to the greater confusion and difficulty in valuing assets which are highly correlated with each other, and, in turn, increase possible profits.

7 I. Goldstein and A. Guembel (2002), *Manipulation, the Allocational Role of Prices and Production Externalities*, AFA 2003 Washington, DC Meetings; 5th Annual Texas Finance Festival; EFA 2002 Berlin Meetings Presented Paper, available at: <http://ssrn.com>

8 X. Liu (2010), *Predatory Short-Selling and Self-fulfilling Crises: When Morris-Shin Meets Diamond-Dybvig*, available at: <http://ssrn.com>

9 G. Venter (2011), *Short-sale constraints and creditor runs*, Job Market Paper.

For example, the banking crisis in Spain has led to a worsening in the perception of the financial situation of the State due to the costs of a public bailout. However, this worsening of the perception of the public issuer has also generated a worsening of the perceived value of bank assets.

The literature on short trading and its effects on systemic stability is very limited, but we should highlight the aforementioned article by Arce and Mayordomo (2012), which focused on measuring the effect of the ban on short selling in Spain in 2011. They believe that the ban weakened the contagion effect coming from sovereign risk which affected medium-sized banks and helped stabilise the probability of default of those banks. These effects were not detected in larger Spanish banks or in Spanish non-financial companies, with regard to which there were fewer doubts. Furthermore, these authors highlight that following the ban on short selling for financial companies in 2011, this trading was transferred to non-financial Spanish companies.

In conclusion, the ban on short selling may be justified in extreme situations of high uncertainty and systemic risk. However, this ban is not able to reduce the underlying problems, but acts as a passive safety device which reduces the possibility of additional damage resulting from the possible existence of multiple equilibriums.

2.2 Limitations and contributions of this article

The title of this article, “empirical study”, explains its main limitation. This document describes the evolution of indicators on the functioning of the market during the ban on short selling without speaking about the existence of causal effects. The main reason lies in the simultaneous nature of the factors which have most likely also had a significant impact on market evolution and which are not independent from the ban on short selling.

Clear examples of these factors which may disrupt the analysis are as follows:

- both the ban adopted in 2011 and the ban adopted in 2012 took place at the same time as measures by the European Central Bank or declarations by the Bank’s president¹⁰ which were interpreted positively by the market and which undoubtedly had an impact on the perception of systemic risk and on market behaviour.
- the bans are not applied at random, but in situations and in countries with grave economic uncertainty, which in turn do not disappear as a result of simply applying the ban. Therefore, the bans will be statistically correlated with indicators which reflect this uncertainty, such as falls in liquidity, without us being able to deduce causality.

10 On 26 July 2012 (three days after the ban on short selling), Mario Draghi, President of the ECB, declared that the Bank would do whatever it took to safeguard the euro. A similar problem can be found for the study of the 2011 ban, since on 5 August (six days before the ban), the ECB President declared his commitment to actively apply a Securities Market Programme.

In addition to these limitations, it is important to point out that this article is not a cost-benefit analysis of this measure. Performing a well-founded analysis would require a counterfactual scenario. However, as often occurs with macroeconomic studies of infrequent events, it is impossible to establish a solid counterfactual scenario.

The contributions of this document are as follows: i) it is one of the first analyses of the ban on short selling which includes those started in 2011 and 2012, and ii) the document models the behaviour of variables, such as trading and implied volatility, which are not usually included in analyses on bans on short selling.

3 General evolution of financial markets and short positions in Spain

3.1 General evolution of financial markets

This section collects general indicators of the situation and evolution of financial markets so as to provide a context to the decisions taken by the CNMV on short positions. The reference data will be the data from France, Italy, Germany and Spain, the largest financial markets in the Eurozone.

Panels A and B of figure 1 show the variations in prices and implied volatility of the main Eurozone indexes. As can be seen, the first ban (August 2011) took place at a time of sharp falls in prices and high perceived risk, and it was not lifted until these tensions were mitigated. The ban applied in July 2012 was also preceded by falls and increases in volatility in Italy and Spain.

Panels C and D show the credit risk of public and bank debt, approximated by the CDS price. As we can see, sovereign risk and bank risk follow a similar course over the period, although at different levels, which is a symptom of a strong correlation between the risks. Prior to the ban which began in 2011, as well as the ban which began in 2012, the CDS on banks of the countries which applied the bans had risen notably. In fact, the ban which started in 2011 was not withdrawn until the price of these credit default swaps fell significantly.

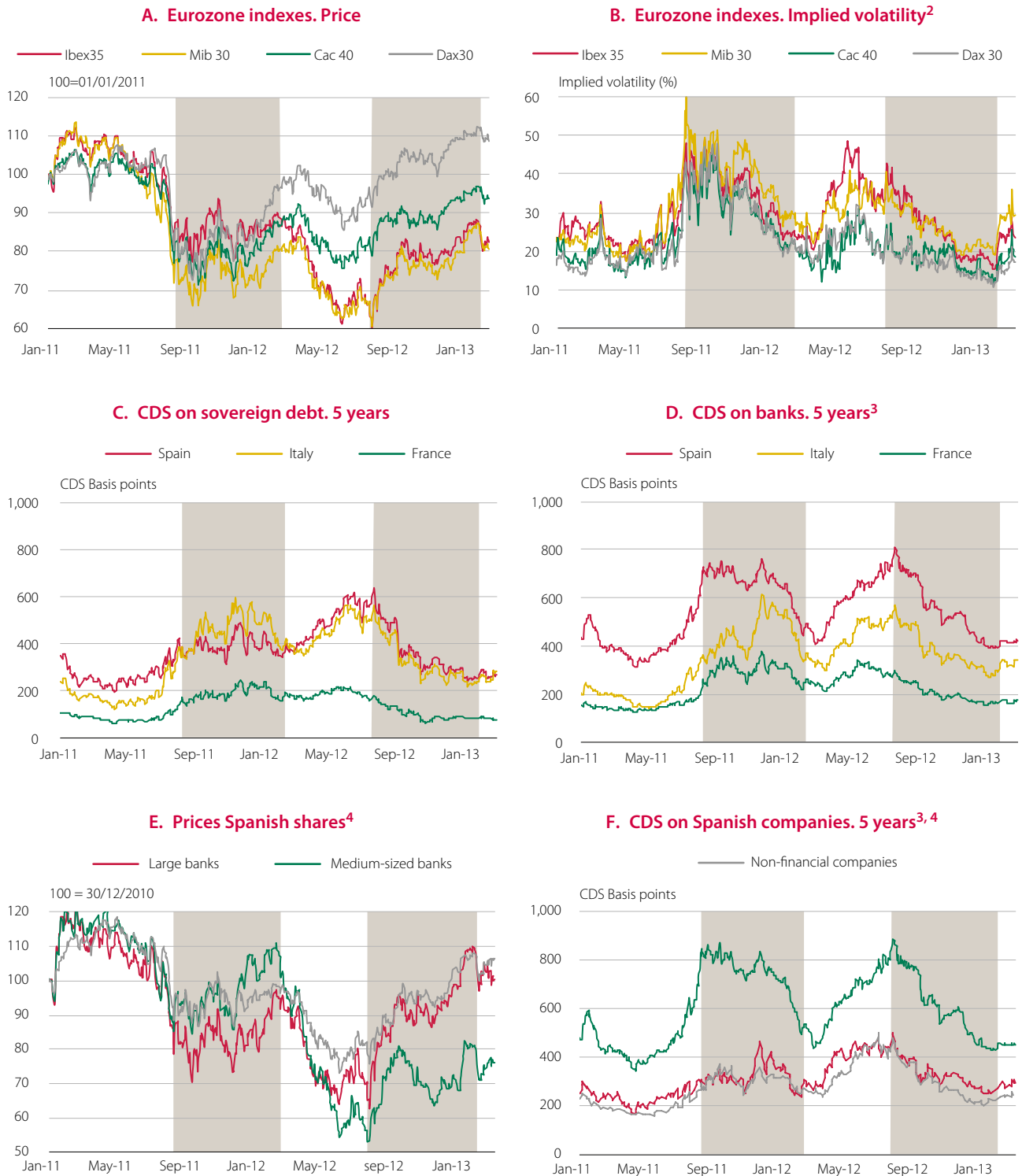
Panels E and F show the case of Spanish companies in more detail. As can be seen, the companies with the greatest problems over the period were medium-sized banks, which were those subject to the greatest uncertainty.

3.2 The correlation between sovereign debt and share prices

As mentioned in section 2.1, a strong correlation between the prices of the liabilities of different issuers is a symptom of the existence of systemic risks which may act as a catalyst for increasing the probability and the damage of spurious movements in share prices. This section shows the evolution of this correlation between the shares of private issuers of Italy, France and Spain, the countries which imposed the ban on short selling in 2011 or 2012, and their risk premium.

General evolution of financial markets¹

FIGURE 1



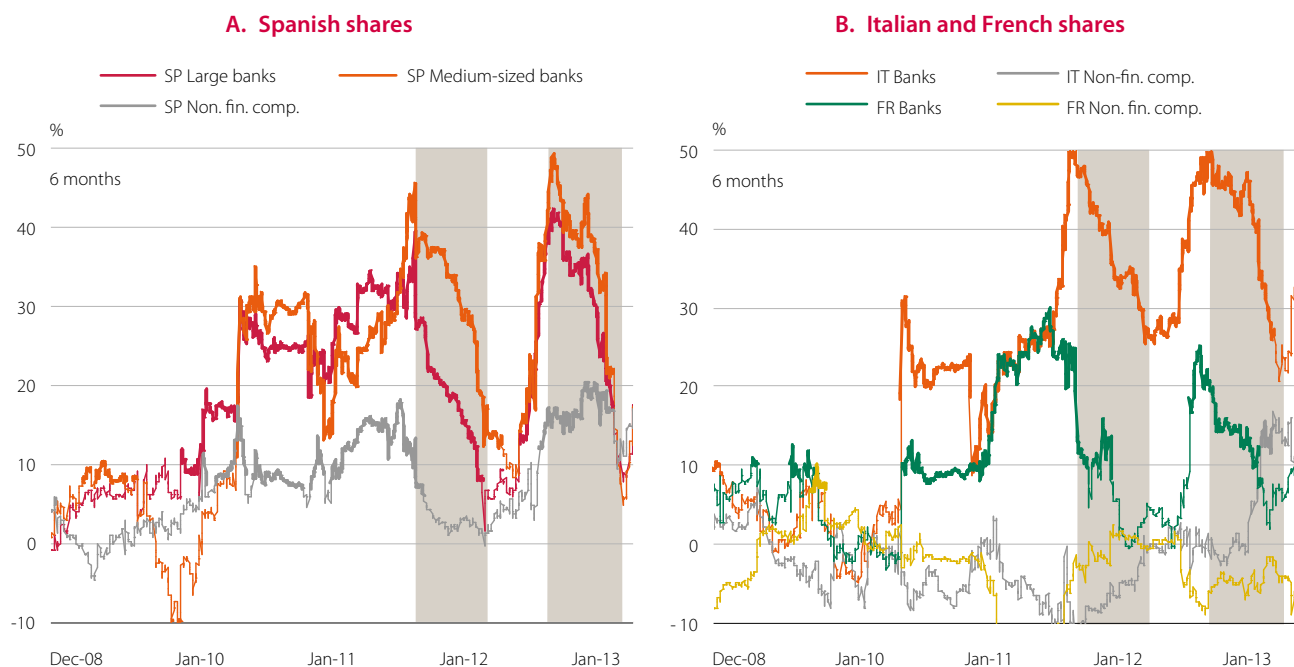
Source: Thomson Datastream and CNMV. (1) The shaded areas indicate the periods in which a ban on short selling was in force in Spain. (2) The implied volatility is that calculated for the Datastream European continuous call option over each index or share, with strike price closest to the value of the underlying. (3) Arithmetic mean of the price of the five-year CDS on national issuers with shares admitted to trading on a regulated market. For Spain, the average of the medium-sized banks includes the CDS on unlisted savings banks. (4) For Ibex 35 companies. The price is calculated as the equally weighted average. Large banks are the two largest Spanish banks and medium-sized banks are the rest. The price is calculated with reinvestment of dividends according to the RI (return index) concept of Datastream.

For this purpose, an APT model has been calculated, with six-month rolling estimation windows, on returns on equally weighted portfolios of shares of the aforementioned countries. The variables on the right-hand side of the equation include the evolution of the Eurostoxx 300 in order to control for factors which are common to all equity in the Eurozone. In order to control for the evolution of sovereign risk, a variable has been introduced which represents the inverse of the sovereign risk premium. Therefore, if there is a systemic correlation, the sign of the coefficient is expected to be positive and significantly different from zero.

It is important to remember that this is not a causal analysis but simply a measure of the correlation between two types of assets. In this regard, it is not possible to determine from this model whether a fall in the value of public debt has led to a fall in the value of shares, if the effect has been in the opposite direction, or whether both effects are happening simultaneously.

Correlation between the return on national public debt and the return on shares^{1, 2 and 3}

FIGURE 2



Source: Thomson Datastream and CNMV. (1) The shares are of companies included in the Eurostoxx 300 in September 2012. Equally weighted portfolios are composed containing shares of financial and non-financial companies with prices which take into account recapitalisation of dividends. For each portfolio we performed an OLS estimation, in six-month rolling windows, where the variable on the left-hand side of the equation is the return (log) of the share portfolio and on the right-hand side the return (log) of the Eurostoxx 300 and the return of a portfolio long in domestic debts and short in German debt. The coefficient corresponding to the public debt portfolio is multiplied by the standard deviation of the return of the public debt portfolio in the period and divided by the standard deviation of the return of the share portfolio in the same period. (2) The shaded area indicates the period that the bans on short selling were in force in Spain. The line which appears below "6 months" is an indicator of the timescale which indicates the dimension of the sub-samples used for each estimation. (3) For each correlation indicator the line is shown as thick or thin. If the line is thick it means that for the estimation for said period, it cannot be rejected that the regression coefficient for the variable which represents the inverse of the risk premium is significantly different from zero at 10%.

Panels A and B of figure 2 show this correlation measure for various share portfolios in Spain, Italy and France. We can therefore see that prior to the current financial crisis, that correlation between risk premium and share prices did not exist. However, since 2009, the correlation between the public debt of these countries and the

prices of their banking sectors become significant and, in some cases, notable. On some occasions, even the shares of non-financial companies seem to be affected, as in Spain prior to the ban in 2012.

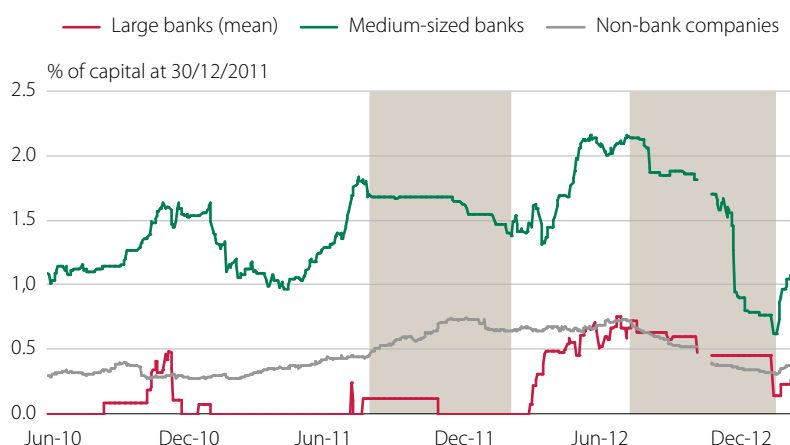
As has been observed for other risk and uncertainty indicators, the securities markets authorities of these countries seem to have acted by banning short selling at the times when the correlation reached maximum levels. The ban that was initiated in 2011 was only withdrawn when the correlation had notably fallen. The 2012 ban in Italy and Spain was also preceded by that sharp increase in correlation, and the ban in Spain was not lifted until the situation had returned to normal.

3.3 Evolution of short selling in the Spanish market

The CNMV has information on the short positions of investors which are equal to or greater than 0.2% of the share capital of the affected listed company. Every two weeks, the CNMV offers information on its website on the short positions accumulated in each issuer.¹¹ Figure 3 shows the aggregate evolution of the short positions of Ibx 35 companies. It shows a cut-off point on 31 October 2012 - the change to the new European legislation for banning short selling.

Reported short positions. Ibx 35^{1, 2 and 3}

FIGURE 3



Source: CNMV. (1) The shaded area indicates the periods that the ban was in force in Spain. (2) The indicators are calculated with data on shares making up the Ibx 35 at 30/12/2011. For each share, a percentage of the share capital over which short positions have been reported is obtained. The aggregate data are weighted by the market value of the shares at a fixed date (30/12/2011) so as to avoid variations in the indicator due to price variations. (3) The cut-off point represents the change in domestic legislation to harmonised European Union legislation.

During the analysis period, from June 2010 to March 2013, the companies over which reported short positions were most significant were medium-sized banks. Given the fact that economic uncertainty was concentrated in those banks, this is in line with the theory presented. Short positions on non-financial companies and ma-

11 In addition, when the short position of a single investor exceeds 0.5% of the share capital, the identity of the investor is disclosed to the market.

for banks were smaller. In any event, this aggregate figure simplifies a reality in which there were issuers over which there were no reported short positions and others which concentrated a large proportion of reported short positions.

During the ban which began in July 2012, the short positions reported on the three groups of issuers fell slowly during the first few months of the ban, from August to October. But the fall was even more abrupt in November 2012, when the capital increase of one of the medium-sized banks led to a dilution in the value of the short positions.

Following the lifting of the ban on short selling on 31 January 2013, there were increases in these positions, although from levels which were much lower than those which existed prior to the ban.

4 Price and volatility of the shares affected by the ban

This section includes an analysis of the evolution of the price and volatility of the shares affected by the ban. The population to be analysed will be the shares making up the Eurostoxx 300 index in September 2012. This population makes it possible to analyse relatively liquid shares and, therefore, with suitable statistical behaviour and, in turn, with sufficient diversity by country, sector and size. The price of all the shares is denominated in euros and therefore the currency market is not an additional factor to be controlled.

4.1 Evolution of the price of the companies affected by the ban

The expected effect of the ban is that it will worsen the informational quality of the market as it prevents the most pessimistic opinions reaching the market, thus creating an upward bias in the price. Furthermore, if it is true that multiple equilibriums are possible, the ban may also lead to an increase in the market price as it reduces the probability of the worst equilibriums. Under either of the two assumptions, it could be expected that the higher the uncertainty about the company, the greater the effect that the ban will have on the price of its shares.

In order to analyse the possible existence of an effect on share prices of the ban on short selling, an individual APT model has been estimated for each one of the shares of the Eurostoxx 300 and the Ibex 35 affected by the bans on short selling during 2011 and 2012. The evolution of the Eurostoxx 300 index and the inverse of the national risk premium have been used as explanatory variables of the return. In addition, dummy variables have been introduced which include the validity of the ban on establishing short positions.

Table 1 shows the descriptive statistics for the statistics of the coefficients of the dummy variables which reflect the validity of the ban for different periods and samples. A coefficient of this variable which is positive and significantly different from zero, approximately 1.65, would imply that the price of a share has had a positive return during the ban period that cannot be explained by other factors, which would indicate a possible bias in prices as a result of the ban.

Return of the shares during the ban

TABLE 1

Individual estimates of the return by GARCH. Descriptive statistics of the t-statistic¹ of the coefficient of the dummy ban variable

Period	# Shares ³	Ban variable ⁴	Descriptive statistics of the t-stat of the coefficient of the ban variable ²					
			Minimum	1st quartile	Median	Mean	3rd quartile	Maximum
01/01/11 - 31/12/12	48	The whole period	-2.20	0.08	1.02	0.97	1.85	4.59
01/03/2011 - 31/12/2011	21	The whole period	-1.66	0.12	0.72	0.53	1.20	2.24
01/03/2012 - 31/12/12	44	The whole period	-1.48	0.09	1.11	1.10	1.92	4.34
01/01/11 - 31/12/12	48	First month	-6.07	-0.75	0.63	0.65	1.54	9.27
		Rest of the ban	-2.16	-0.16	0.81	0.80	1.55	5.21
01/03/2011 - 31/12/2011	21	First month	-0.84	-0.21	0.26	0.47	1.17	2.15
		Rest of the ban	-1.61	-0.74	0.74	0.49	1.31	2.65
01/03/2012 - 31/12/12	44	First month	-2.72	-0.26	0.74	0.84	1.94	5.26
		Rest of the ban	-1.32	0.28	0.80	0.71	1.28	2.71

Source: Thomson Datastream and CNMV. (1) For Ibex 35 shares (Spain) and Eurostoxx 300 shares (France and Italy) which were affected by the ban on short selling. An ARCH equation (1) has been estimated for each share in the period 01/03/2012 to 31/12/2012, or alternatively in the periods 01/03/11 to 31/12/11 and 01/03/12 to 31/12/12 to analyse both bans separately. The variable on the left-hand side of the equation is the return (log) of the share and the right-hand side includes a constant, the return (log) of the Eurostoxx 300 and of the debt portfolio, which simulates the inverse of the Spanish risk premium. In addition, dummy variables are included which reflect the validity of the ban. (2) This offers the t-statistic obtained from the estimate for the coefficients of the variables which represent the ban. (3) The number of shares depends on the period analysed. For the 2011 ban, Spanish non-financial companies are not included and for the 2012 ban, French companies are not included. (4) The dummy variable which represents the ban. "The whole period" indicates that its value is 1 for the whole period in which the ban is in force. "First month" is a dummy variable which only takes the value 1 in the first month that the ban is in force and 0 for the rest of the time the ban is in force. "Rest of the ban" is the complementary variable to "First month".

For the different periods and specifications of the dummy variable which represents the ban, we can see that the median is below 1.65. This indicates that there were no abnormal increases in prices during the ban for at least half of the shares under consideration. Separating the ban period in two, the first month and the rest, we still cannot see notably different results. It therefore does not seem possible to state that there was an extraordinary short-term return in the affected shares.

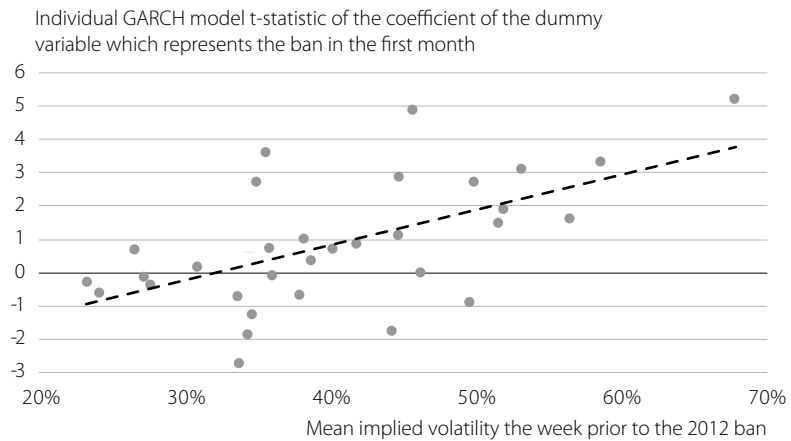
If we analyse the third quartile of the t-statistics, we can see cases in which more than 25% of the analysed shares show abnormally positive returns. For example, in the case of the 2012 ban, we can see that this third quartile takes a value of 1.94 during the first month that the ban was in force. More specifically, 13 of the 44 shares which were affected by the ban had an abnormally positive return during the first month the ban was in force.

According to the point indicated in section 2.1, we can expect that the ban on short selling will introduce a greater upward bias, the higher the level of uncertainty existing about said share. Figure 4 puts forward the possible existence of this effect for

Spanish companies affected by the 2012 ban. The mean of the implied volatility for each share in the week prior to the ban has been taken as an approximation of the uncertainty. As we can see, there appears to be a certain graphic relationship between the volatility prior to the ban and the excess return during the ban. However, the results are not sufficiently robust statistically to state this with confidence.

Abnormal returns in the first month of the ban and prior volatility

FIGURE 4



Source: Reuters, Datastream and CNMV. The horizontal axis shows the average implied volatility of each share the week before the 2012 ban in Spain. The vertical axis shows the t-statistic of the regression coefficient, explained previously, for the dummy variable which reflects the validity of the ban during the first month.

4.2 Volatility of the shares affected by the ban

The ban on short selling reduces the efficiency of market price discovery and, therefore, we can expect a share affected by said constraint to be subject to greater volatility. The opposite effect would take place if the ban on short selling is considered to protect the company from spurious movements in its prices.

In order to analyse the behaviour of the volatility of shares subject to the ban on short selling, a panel data analysis has been used¹² which includes all the shares of the Eurostoxx 300 for the period 2010-2013.¹³ The variable on the left-hand side of the equation is the implied volatility of each share. Using this variable reduces the need to make assumptions about the statistical distribution of the volatility and, in theory, said variable immediately incorporates all the information available in the market, unlike estimated volatilities. At the same time, it introduces a component of subjectivity as this indicator reflects the estimates of the participants in the options market about the expected volatility of a share, which may or may not coincide with the volatility eventually displayed by the share.

12 Following Y. Croissant and G. Millo (2008), *Panel Data Econometrics in R: The plm Package*, available at <http://cran.r-project.org>

13 Annexes I and II of this document contain a description of the structure of the data used and the main variables analysed. Annex III contains the graphic information on the distribution of the different variables analysed which are conditional on the validity or not of a ban on short selling.

One possible bias of the estimate is that the bans are usually established for whole groups of shares in a specific country. As has been seen, the evolution of share prices and volatility depends on the perceived macroeconomic risk of the issuer's country. If this bias is not controlled for and the ban coincides with a period of relaxation (worsening) of macroeconomic conditions, an incorrect conclusion might be reached that share volatility fell (increased) during the ban. Consequently, and in order to control for that macroeconomic effect, the CDS of the sovereign bond of the home country of the share has been introduced as a control variable. However, it is not the case for all companies that the CDS of their home country has a similar relationship with the volatility of the shares. Therefore, the estimate has been made allowing the coefficients which relate the implied volatility of each share with the CDS of its country to be variable and only the relationships which are significant to 10% are maintained in the final estimate.

The results are shown in table 2. For all the estimates obtained, the implied volatility increases when the ban is introduced. Accordingly, in estimation 4, we can see that the value of the coefficient of the prohibition dummy is 0.013, which implies that the ban is associated with a 1.3% increase in implied volatility or the volatility expected by market agents. By sub-period, in estimation 6 we can see that the 2012 ban was associated with a growth in implied volatility, while for the 2011 ban we cannot statistically reject that there was no increase.

Changes in the implied volatility (log) of the shares of the Eurostoxx 300, associated with the ban on short selling¹

TABLE 2

Panel data estimation

Estimation	1	2	3	4	5	6
Estimation period	Jan 10 Mar 13	Jan 10 Mar 13	Jan 10 Mar 13	Jan 10 Mar 13	Mar 11 Dec 11	Mar 12 Dec 12
Individual fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Time fixed effects	No	Yes	Yes	Yes	Yes	Yes
Ban	0.213***	0.117***	0.016***	0.013***	0.002	0.029***
t-statistic²	68.25	40.79	11.75	9.85	0.63	8.38
CDS (log)				Variable ³	Variable ³	Variable ³
t-statistic²				Variable ³	Variable ³	Variable ³
Volatility (-1) (log)			0.870***	0.864***	0.820***	0.784***
t-statistic²			112.20	106.87	42.90	42.24

Source: Thomson Datastream and CNMV. Data from 04/01/2010 to 04/03/2013. (1) The variable on the left-hand side of the equation is the implied volatility (log) of the shares of the Eurostoxx 300 obtained from the options market. It does not include Portugal as there are no implied data available on Portuguese shares. The observations in which the implied volatility was in the last percentile have been eliminated so as to avoid possible outliers. The right-hand side of the equation includes: i) constants for each share in the sample, ii) a time constant for each session included in the panel data, iii) a dummy variable which takes the value 1 when there is a ban in force on short selling on the share, iv) the price of the CDS of the sovereign debt of the home country of the company which has issued the share and v) the volatility delayed one session. (2) The t-statistic is estimated by using White's diagonal variance-covariance matrix. (3) For estimations 4 to 6, variable coefficients have been used to analyse the relationship between implied volatility and the national CDS. In order to avoid excessively reducing the degrees of freedom, individual estimations have been made of the model, subsequently including the control of CDS in the panel data estimation only for those shares for which the existence of a correlation has been demonstrated, all of them with their own coefficient. Subsequently, the process has been iterated so as to eliminate those variables for which the coefficient was not significant. For estimation 4, the mean coefficient obtained in this manner was 0.018, the median of the coefficient was 0.022, and the median of the t-statistic was 5.524.

As a robustness analysis, Annex IV contains similar estimations for the observed, instead of implied, variance. For this variable, the ban is also associated with an increase in volatility, which is understood as the square of the error of an individual APT model for each share. Accordingly, the observed volatility would have increased on average by 13.7% for the companies affected by the ban, after controlling for other explanatory factors of the volatility.

5 Functioning of the market during the bans on short selling

As mentioned above, a ban on short selling is likely to worsen efficiency in the price discovery process. One possible consequence of this will be a fall in liquidity in these markets. In addition, this restriction is likely to reduce the trading volumes in these markets. This section analyses how the bans affected trading in shares and their liquidity. The final point of the section includes a specific analysis of the Spanish equity market.

5.1 Trading in European markets

A panel data estimation has been made in order to measure the behaviour of trading. The results are shown in table 3. The variable on the left-hand side of the equation is the number of shares of a particular stock traded in all European markets according to the Bloomberg composite, divided by the number of shares admitted to trading i.e. the daily turnover. The right-hand side of the equation includes a variable which indicates the validity of a ban on short selling for that share. In addition, the implied volatility of the share in the previous session is used as a control variable. Finally, the effect of the ban will be estimated using the period immediately prior to and subsequent to three significant events: i) the entry into force of the ban in 2011, ii) the lifting of said ban, iii) the entry into force of the ban in 2012.

Changes in the turnover (log) of the shares of the Eurostoxx 300, associated with the ban on short selling¹

TABLE 3

Panel data estimation

Estimation	1	2	3	4	5	6
Estimation period	Jan-10 Mar-13	Jan-10 Mar-13	Jan-10 Mar-13	10/07/2011 12/09/2011	16/01/2012 16/03/2012	22/06/2012 24/08/2012
Individual fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Time fixed effects	No	Yes	Yes	Yes	Yes	Yes
Ban	-0.241***	-0.188***	-0.216***	-0.592***	-0.134***	-0.318***
t-statistic²	-28.53	-23.37	-25.50	-18.95	-6.44	-8.99
Volatility (-1) (log)			0.293***	0.140***	0.008*	0.016
t-statistic²			32.69	3.20	1.92	0.33

Source: Bloomberg, Thomson Datastream and CNMV. The data under consideration go from 04/01/2010 to 04/03/2013. (1) The variable on the left-hand side of the equation is the turnover (log) of the shares, calculated as the number of shares traded on all European markets (Bloomberg EU Composite) divided by the total number of shares issued. The delayed volatility (log) of each share is included as a control variable. The turnover observations of 100th percentile have been eliminated so as to avoid the effect of extreme values. (2) The t-statistic is estimated by using White's diagonal variance-covariance matrix.

As can be seen in estimation number 3, the 2011 and 2012 bans appear to be associated with falls in turnover of 20.2% for all the affected shares, even after controlling for the general activity in all the markets in the Eurozone, the ordinary turnover of the affected shares and the delayed volatility.

Estimations 4 to 6 contain the event analysis. The ban is found to be associated with a fall in the turnover of the affected shares in the three cases.

5.2 Liquidity of the shares in Eurozone markets

The Amihud illiquidity ratio¹⁴ has been used to make comparisons between different countries in the Eurozone. This is calculated by dividing the absolute value of the daily return¹⁵ by the percentage of shares traded on that day with regard to the total number issued.¹⁶ Accordingly, for a share i on day t , the Amihud ratio is calculated as

$$AR_{it} = 100.000 \cdot \frac{\text{abs}\left(\frac{P_{it}}{P_{it-1}} - 1\right)}{\frac{V_{it}}{NOSH_{it}}}$$

where P_{it} and P_{it-1} are the prices of share i on day t and the previous day, respectively, V_{it} is the number of shares of that company traded on that day and $NOSH_{it}$ is the number of shares of the company admitted to trading.

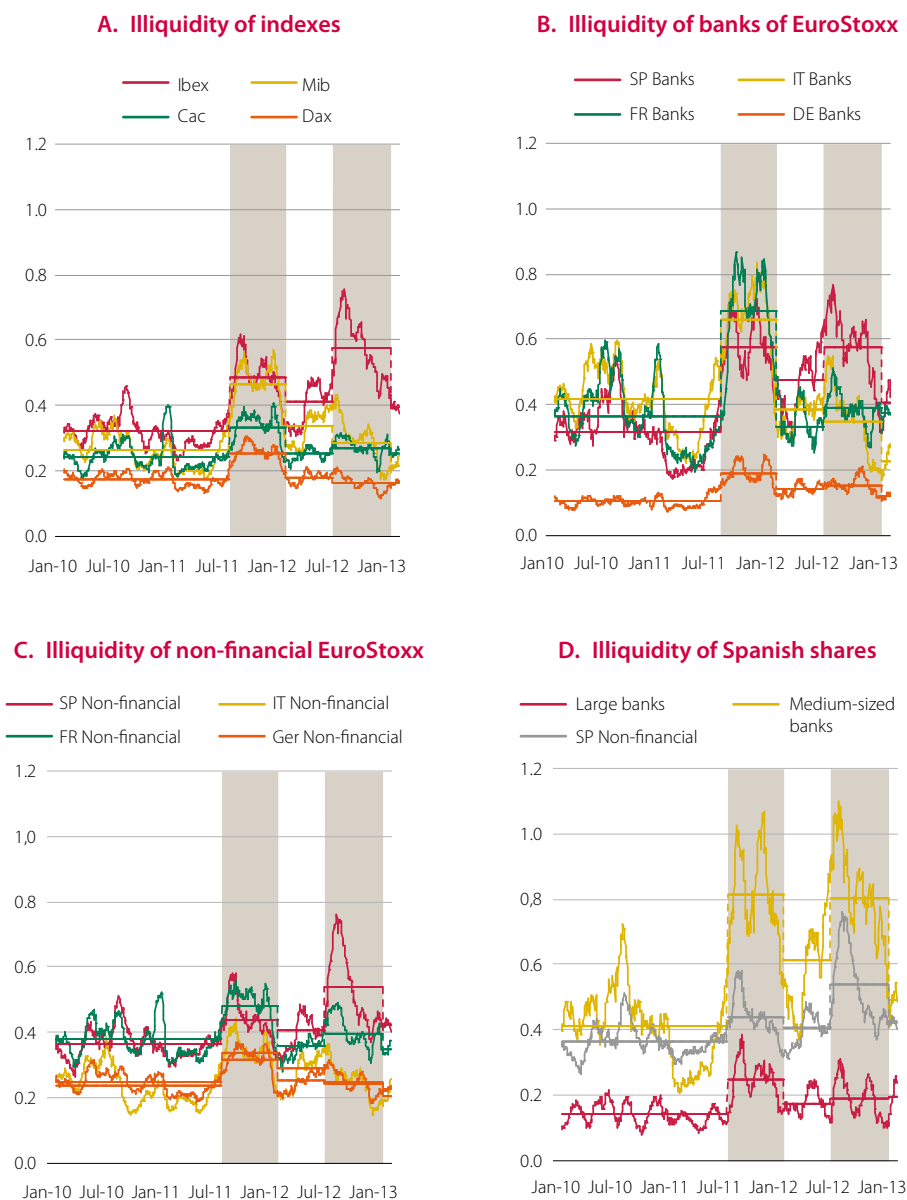
This ratio may be interpreted as the effect on the price (in absolute terms) of a 1% increase in trading. Given that the most liquid shares allow such increases in trading with a lesser impact on the price, a higher Amihud ratio will show greater illiquidity i.e. worse functioning of the market.

Figure 5 contains the evolution of the Amihud liquidity ratio in various Eurozone countries, calculated as a moving average of 22 sessions for the components of various indexes. We can see that the ban which started in 2011 was accompanied by an increase in illiquidity of the shares of the Eurozone, whether or not they were affected by the ban. In this regard, Panel C, made up of non-financial shares, is very informative as it shows how shares not subject to the ban suffered an increase in their illiquidity.

14 Y. Amihud (2002), *Illiquidity and stock returns: Cross-section and time-series effects*, in *Journal of Financial Markets*, January.

15 The "Total return index" calculated by Thomson Datastream will be used to calculate the return as this avoids the possible spurious effect of dividend payments.

16 For this study, we will use this measure modified with respect to the original proposed by Amihud in order to facilitate comparisons between companies by applying a denominator without a monetary scale as is the case with the numerator.



Source: Bloomberg, Thomson Datastream and CNMV. (1) Aggregate Amihud ratio calculated as the simple moving average of 22 sessions for the daily individual Amihud ratios. The individual Amihud ratio for each company and each session is calculated as the ratio between the absolute value of the daily return and the percentage of shares issued by the company traded on all European stock markets according to the Bloomberg composite, all multiplied by 100,000. Those individual observations for each day and company from the 100th percentile have been eliminated from the sample as they are considered outliers. For each series, the average ratio for the relevant period is offered as a dotted line.

The 2012 ban is more difficult to interpret graphically. Following its application in Spain and Italy, there were increases in illiquidity, which later dropped until the end of the year. In the case of Italy, this may be explained by the lifting of the ban at the end of September, but in Spain this fall still occurred with the restriction in force. This fall, therefore, could also be explained by other, non-stock market factors which reduced uncertainty as regards these securities. In any event, the illiquidity of the Spanish market was greater during the period than in the other markets analysed.

Given that the interpretation of these graphs is ambiguous, we have analysed the evolution of liquidity using panel data, following the work performed by Beber and Pagano (2012). The estimation period is from 2010 to 2013 for Eurostoxx 300 shares. The variable on the left-hand side of the equation will be the daily Amihud illiquidity ratio for each share of the Eurostoxx 300. As control variables, dummies will be introduced for each share and session, the delayed illiquidity ratio and the implied volatility of each share at the close of the previous session, which will make it possible to control for the level of volatility, which may be correlated to the decision to ban short selling and the illiquidity itself. Finally, a dummy is included which takes the value 1 when there is a ban in force on short selling of a security in particular. In addition, this estimation will be made for different sub-samples, according to company size, the country which applies the ban and different estimation periods.

Changes in illiquidity (Amihud ratio) associated with the ban on short selling¹

TABLE 4

Panel data estimation

Description of the estimation				Coefficients of the estimation							
Estimation	Estimation period		Population under consideration	Fixed effects			Ban	Amihud (-1)		Volatility (-1)	
				Individual	Time	Coef.	t-stat	Coef.	t-stat	Coef.	t-stat
1	01/05/2010	04/03/2013	Eurostoxx300	Yes	No	0.242***	32.68				
2	01/05/2010	04/03/2013	Eurostoxx300	Yes	Yes	0.191***	25.58				
3	01/05/2010	04/03/2013	Eurostoxx300	Yes	Yes	0.158***	23.01	0.139***	32.44		
4	01/05/2010	04/03/2013	Eurostoxx300	Yes	Yes	0.152***	21.45	0.135***	27.10	0.050***	5.49
5	01/03/2011	31/12/2011	Eurostoxx300	Yes	Yes	0.237***	16.93	0.065***	7.03	0.014	0.51
6	01/03/2012	31/12/2012	Eurostoxx300	Yes	Yes	0.130***	11.21	0.081***	8.98	0.034*	1.73
7	01/05/2010	04/03/2013	Spain	Yes	Yes	0.145***	6.63	0.128***	8.16	0.178***	3.37
8	01/05/2010	04/03/2013	Italy	Yes	Yes	0.091***	6.52	0.245***	16.12	0.015**	2.31
9	01/05/2010	04/03/2013	France	Yes	Yes	0.186***	10.93	0.103***	12.55	-0.012***	-0.43
10	01/05/2010	04/03/2013	Financial	Yes	Yes	0.096***	7.81	0.168***	18.14	0.033	1.05
11	01/03/2012	04/03/2013	Small Cap. ²	Yes	Yes	0.086***	7.28	0.132***	21.51	-0.046	-1.47
12	01/03/2012	04/03/2013	Medium Cap. ²	Yes	Yes	0.167***	18.80	0.107***	25.00	0.076***	3.94
13	01/03/2012	04/03/2013	Large Cap. ²	Yes	Yes	0.264***	23.12	0.155***	32.47	0.029**	2.45
14	01/03/2012	04/03/2013	Very large Cap. ²	Yes	Yes	0.100***	14.06	0.151***	38.23	0.167***	8.27

Source: Bloomberg, Thomson Datastream and CNMV. (1) Panel data estimation for the period 01/01/2010 to 04/03/2013 of shares making up the Eurostoxx 300 in September 2012 for which there is information on implied volatility in the options market. The t-statistics of the coefficients have been estimated with a White diagonal matrix. The data where the ratio was in the top 1% of the whole sample have been eliminated so as to avoid the presence of outliers. In addition, the data for Greece have not been considered as the ban was in force throughout the period. Neither have the data for Bankia been used as it is difficult to statistically model. (2) The classification by size is derived from the mean of the market value during the estimation period. The group of small companies are those with a mean value lower than 2.5 billion euros, the group of medium-sized companies are those with a mean value from 2.5 billion euros to 5 billion euros, large companies are those between 5 billion euros and 10 billion euros, and very large companies are those with a mean value above 10 billion euros.

According to the results from table 4, the imposition of a ban on short selling is clearly statistically associated with greater illiquidity of the affected shares. In estimation number 4, after controlling for factors such as implied volatility and the general illiquidity in European markets, we can see that the ban leads to an average increase in the Amihud ratio of 0.152. If we analyse the 2011 and 2012 bans separately (estimations 5 and 6), we can see that the former was associated with higher

individual worsening of illiquidity than the latter. If the estimation is made by country (estimations 7 to 9) and by company size (estimations 10 to 14), we can also see the aforementioned significant effect.

5.3 Analysis of the Spanish equity market during the 2012 ban

As has been seen above, the ban on short selling appears to be statistically associated with falls in trading and the liquidity of the affected shares, whilst at the same time leading to increases in volatility. This section will study some specific aspects of the Spanish equity market during the period of the ban on short selling which began in July 2012.

The average daily value traded fell notably during the second ban, especially in the period August-October 2013. However, not all of this fall can be attributed to the ban on short selling, as it could have been simultaneously due to the fall in the price of the traded shares or even a seasonal effect.

The nominal trading has been deflated using the evolution of the IGBM¹⁷ in order to eliminate the above effects. Subsequently, the seasonally adjusted series has been calculated using the Tramo-Seats programme. Standardised data are offered in table 5 in such a way that 100 is the average, seasonally-adjusted and deflated trading in 2012.

Deflated and seasonally-adjusted trading in shares of the IGBM in BME

TABLE 5

100= Average deflated and seasonally adjusted trading in 2012

Month/year	2006	2007	2008	2009	2010	2011	2012
January	93.6	92.4	134.9	83.8	88.9	111.9	93.4
February	99.1	106.4	107.1	104.7	109.8	95.2	80.0
March	85.0	132.8	104.3	104.2	76.0	101.0	101.5
April	87.1	102.3	93.4	105.9	111.7	99.9	117.9
May	89.8	104.2	84.1	104.6	146.3	91.0	120.6
June	92.4	137.4	98.0	92.4	100.1	87.8	117.9
July	91.3	102.4	101.5	97.1	103.7	118.5	112.9
August	86.3	126.2	104.1	93.5	91.5	143.9	80.6
September	111.6	108.2	123.4	80.4	86.5	106.2	99.3
October	91.7	116.1	126.5	85.9	116.6	104.7	97.3
November	103.5	116.2	111.1	94.0	143.4	108.2	71.9
December	108.2	107.7	96.5	98.1	97.7	97.1	106.6

Source: CNMV and author. The total daily value traded in BME on shares of the IGBM has been deflated by using this last index and its monthly average has been calculated for the period 1998-2012. This deflated monthly average trading has been seasonally adjusted using the Tramo-Seats programme. In order to facilitate the analysis, the data obtained have been standardised by dividing by the average in 2012.

17 In any event, this adjustment is not perfect as the weightings of the IGBM depend on the capitalisation of the companies and not on the relative importance of the trading of the shares, although it is used because it is appropriately correlated.

As can be seen, even after performing these adjustments, the months of August and November 2012 have two of the lowest activities of the whole period under analysis (80.6 and 71.9, respectively). However, other months in which the ban on short selling was in force show normal stock market activities, especially December, which is above the average. The conclusion is that the ban seems to be associated with falls in activity, but smaller falls than seemingly indicated by the data on value traded.

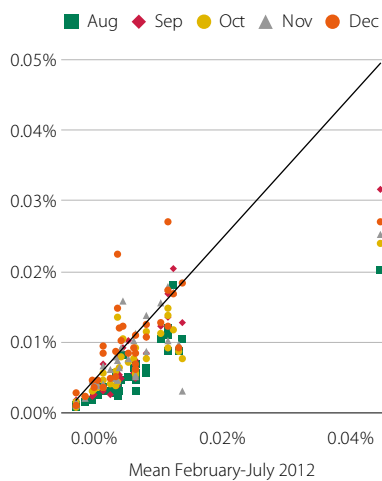
In order to analyse the liquidity of the Spanish stock market, we will use another liquidity measure known as Kyle's Lambda,¹⁸ estimated by the Sociedad de Bolsas. For each share, a calculation is made of the monetary value of the transaction which makes it possible to buy and sell said shares affecting the price as a maximum by +/-1%. The more liquid the share, the higher this monetary value will be i.e. the higher the capacity of investors to conduct large volume transactions without the market price changing against them.

For each Ibx 35 company, figure 6.A shows said standardised liquidity measure according to the market value of the company so that this measure may be interpreted as the percentage of shares of the company which may be acquired whilst altering their price by a maximum of +/-1%. The horizontal axis presents said value for the period between February and July 2012, a period with hardly any restrictions on short selling.¹⁹ The vertical axis offers the same data for the months of August to December, with the ban in force, accompanied by the bisector.

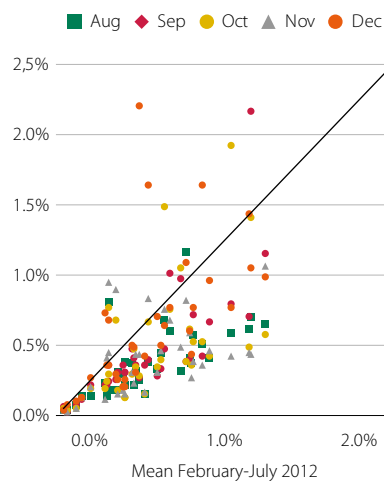
Liquidity in Ibx 35 shares. 2012 ban

FIGURE 6

A. Kyle's Lambda – ex-ante¹ liquidity



B. Turnover – ex-post² liquidity



Source: Sociedad de Bolsas, Thomson Datastream and CNMV. (1) In its monthly bulletin, the Sociedad de Bolsas offers the average value in euros necessary to alter the price of the share by +/-1%. A higher value implies higher liquidity as the foreseeable impact of the purchase will be lower. Said quantity has been standardised for the market value of the company at the close of the analysis period. (2) Turnover is calculated for each day as the number of shares traded divided by the number of shares issued; its monthly average is then calculated.

18 See the explanatory annex of the Monthly Report of the Sociedad de Bolsas.

19 During this period some type of restriction on short selling was in force during the first half of February and the last week of July.

In said graph, a point below the bisector implies a worsening of the liquidity with regard to the average of the period February-July 2012. As can be seen, in general ex-ante liquidity of the shares of the Ibox 35 companies fell over the month in which the ban was in force.

An analysis is then made of the ex-post liquidity, measured as the average daily number of shares traded of each Ibox 35 company divided by the total number of shares admitted (the turnover). The period February-July of this year is used as a period of comparison (horizontal axis of figure 6.B). The vertical axis shows said value for August and September 2012, together with the bisector. The results also show a fall in liquidity and are in line with those seen in figure 6.A.

6 Conclusions

The CNMV established bans on establishing or increasing short positions in 2011 and 2012 due to the fact “that European securities markets are going through a period of extreme volatility which might cause their disorderly functioning and affect the normal development of financial activity”.

A large part of the academic literature has a favourable opinion on short selling as it believes that this type of trading improves the efficiency of the price discovery process. However, some authors have also highlighted that in circumstances of grave uncertainty, short selling has the capacity to provide an incentive to transactions which generate spurious movements in the market price and, in extreme cases, permanently alter the fundamental value of the companies affected. These effects would be exacerbated in situations of systemic risk in which not only the directly affected issuer is harmed, but also other public or private issuers.

The securities market authorities that have applied these bans on short selling have done so precisely in those exceptional circumstances in which securities markets operated in conditions of high volatility, uncertainty and systemic risk. When these circumstances have eased, these authorities have withdrawn the restrictions as they are aware that they reduce the efficiency of securities markets.

This document has measured, for this period, the changes in the functioning of the market associated with the application of the bans on short selling. The word “associated” has been deliberately chosen because, due to empirical problems, this document does not aim to measure the causal effect of this ban on the functioning of the market and the author is aware that, in some cases, the changes may be associated with other market events which are correlated with the application of the ban on short selling.

The estimate of these changes associated with the bans on short selling has been made for the set of shares of the Eurostoxx 300 during the period 2010-2013. The conclusions are as follows:

- The ban is not associated with abnormal returns for most of the affected shares.

- When this price effect does exist, it appears in the short term and is more likely in companies regarding which there had previously been uncertainty.
- The ban is empirically associated with increases in the implied and observed volatility of the affected shares.
- The ban is empirically associated with falls in trading of the affected shares.
- The ban is empirically associated with falls in the liquidity of the shares, measured by the Amihud ratio. This worsening of liquidity is robust to the introduction of controls, such as the implied volatility of the shares and the delayed Amihud ratio. It is also robust to analysis by different sub-samples, countries, company sizes and periods.

The ban on short selling therefore seems to be empirically associated with securities markets functioning worse, which would be the explicit cost of this measure. However, its possible benefit, should it exist, is implicit and cannot be calculated, because to do so would require knowledge of the counterfactual scenario i.e. what would have happened if the measure had not been taken.

Annexes

Structure of the database used on the Eurostoxx 300

ANNEX I

Country	End	No. companies	2011 ban		2012 ban		No. of observations	
			Start	End	Start	End	Without ban	With ban
Austria	Yes	4	-	-	-	-	3,308	0
Austria	No	5	-	-	-	-	4,135	0
Belgium	Yes	6	12/08/2011	13/02/2012	-	-	4,164	798
Belgium	No	8	-	-	-	-	6,616	0
Germany	Yes	9	-	-	-	-	7,109	0
Germany	No	58	-	-	-	-	47,851	0
Spain	Yes	7	12/08/2011	15/02/2012	23/07/2012	31/01/2013	3,871	1,918
Spain	No	20	-	-	23/07/2012	31/01/2013	13,284	2,780
Finland	Yes	2	-	-	-	-	1,654	0
Finland	No	17	-	-	-	-	14,059	0
France	Yes	14	12/08/2011	13/02/2012	-	-	9,716	1,862
France	No	67	-	-	-	-	55,280	0
Ireland	Yes	1	-	-	-	-	827	0
Ireland	No	7	-	-	-	-	5,789	0
Italy	Yes	11	12/08/2011	24/02/2012	23/07/2012	14/09/2012	7,095	2,002
Italy	No	17	-	-	-	-	13,581	0
Luxembourg	No	3	-	-	-	-	2,481	0
Netherlands	Yes	6	-	-	-	-	4,962	0
Netherlands	No	27	-	-	-	-	20,501	0
Portugal	Yes	1	-	-	-	-	827	0
Portugal	No	4	-	-	-	-	3,308	0
Total	Yes	61	N.A.	N.A.	N.A.	N.A.	43,533	6,580
Total	No	233	N.A.	N.A.	N.A.	N.A.	186,885	2,780
Total		294	N.A.	N.A.	N.A.	N.A.	230,418	9,360

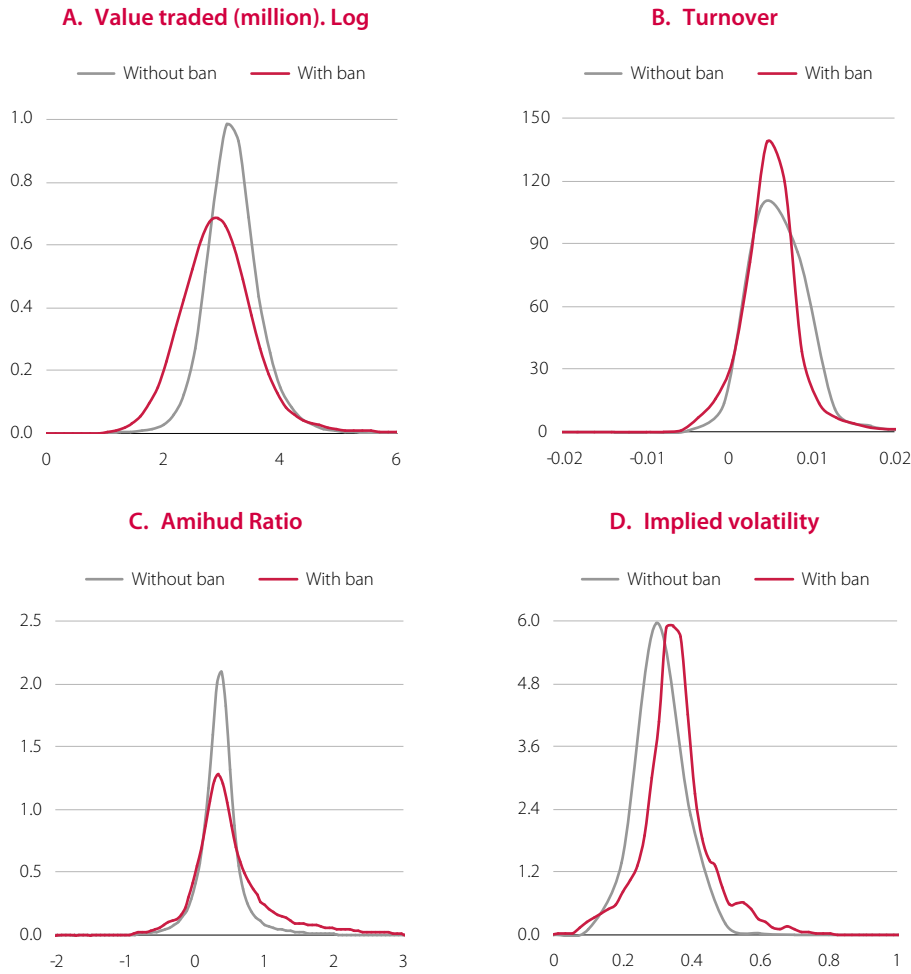
Source: Reuters Datastream, European securities commissions and CNMV. The companies of Greece have been excluded from the analysis because the ban was in force throughout the period. In addition, Bankia has been excluded from the analysis due to its statistically erratic behaviour. Data from 04/01/2010 to 04/03/2013.

Descriptive statistics of the variables used

ANNEX II

Variable	Ban	Minimum	1st quartile	Median	Mean	3rd quartile	Maximum
Value traded (million euro)	No	0.00	9.35	23.09	82.24	69.83	18,400
	Yes	0.00	6.05	13.38	76.98	66.32	4,120
Turnover	No	0.0000	0.0025	0.0046	0.0062	0.0077	0.4046
	Yes	0.0000	0.0016	0.0033	0.0057	0.0065	0.1768
Amihud	No	0.0000	0.0985	0.2215	0.3690	0.4407	4.0000
	Yes	0.0000	0.1467	0.3811	0.6617	0.8671	4.0000
Implied volatility	No	0.0014	0.2286	0.2841	0.3050	0.3570	9.0860
	Yes	0.1050	0.3030	0.3797	0.4344	0.5348	2.3310

Source: Reuters Datastream, Bloomberg and CNMV. The companies of Greece have been excluded from the analysis because the ban was in force throughout the period. In addition, Bankia has been excluded from the analysis due to its statistically erratic behaviour. Data from 04/01/2010 to 04/03/2013. The Bloomberg EU Composite, which aggregates the trading of a share for all markets in the European Union is used to measure the total trading volume. The value traded is estimated as the product of the trading and the closing price. The Amihud ratio is estimated as has been explained in the text. The implied volatility data are calculated by Datastream for European call options with the strike price close to the price of the underlying.



Source: Datastream-Reuters, Bloomberg and CNMV. For each observation, the variable is adjusted by subtracting the individual average, the average of the day for all shares and adding the unconditioned average. A Kernel is estimated on this data with an Epanechnikov function for the observations in which a ban on short selling is in force and for the observations for which no ban is in force. The companies of Greece have been excluded from the analysis because the ban was in force throughout the period. In addition, Bankia has been excluded from the analysis due to its statistically erratic behaviour. Data from 04/01/2010 to 04/03/2013. The Bloomberg EU Composite, which aggregates the trading of a share for all markets in the European Union, is used to measure the total trading volume. The value traded is estimated as the product of the trading and the closing price. The Amihud ratio is estimated as has been explained in the text. The implied volatility data are calculated by Datastream for European call options with the strike price close to the price of the underlying, called "continuous call".

Changes in the observed variance (log) of the shares of the Eurostoxx 300, associated with the ban on short selling

ANNEX IV

Panel data estimation. The left-hand side of the equation introduces the logarithm of the square of the estimation error for each share for each day of an APT model

Estimation	1	2	3	4	5	6
Estimation period	Jan 10	Jan 10	Jan 10	Jan 10	Mar 11	Mar 12
	Mar 13	Mar 13	Mar 13	Mar 13	Dec 11	Dec 12
Individual fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Time fixed effects	No	Yes	Yes	Yes	Yes	Yes
Ban	0.575***	0.428***	0.403***	0.292***	0.217***	0.028
<i>t</i> -statistic	20.23	15.04	14.16	9.71	3.65	0.47
log((error(-1)) ²)			0.050***	0.045***	0.039***	0.048***
<i>t</i> -statistic			24.41	19.88	8.84	11.38
Implied variance (-1) (log)				0.367***	0.206***	0.226***
<i>t</i> -statistic				27.78	7.54	7.45

Source: Thomson Datastream and CNMV.

Population: Eurostoxx 300 shares in September 2012. The issuers in Greece and Luxembourg, together with Bankia, have been removed. In addition, extreme observations of the square of the error, both the top 0.1% and the bottom 0.1%, have been removed.

Panel data estimation. Matrix of co-variances of the coefficients by White diagonal.

Variable of the left-hand side:

Napieran logarithm of the square of the estimation error of an individual APT model per share. For each share under consideration, an APT model is estimated for the period 04/01/2010 to 04/03/2013. The Eurostoxx 300 and national CDS of each share are introduced as variables on the right-hand side in the APT model in order to control for systemic risk. If the CDS coefficient is not significantly different from zero at 10%, a model with the Eurostoxx 300 as variable on the right-hand side is used. In the event that this is not significant either, the square of the daily return is used as the estimation error.

Variable of the right-hand side:

- i) constants for each share in the sample;
- ii) a time constant for each session included in the panel data;
- iii) a dummy variable which takes the value 1 when there is a ban in force on short selling the share;
- iv) the variable of the left-hand side, delayed by one session;
- v) the implied volatility delayed by one session.

An analysis of the design and impact of the financial transaction tax proposed by the European Commission

Ramiro Losada

1 Introduction

The current economic and financial crisis has had, and continues to have, serious repercussions on the economies of European countries and their public finances. There is consensus that the creation of real estate bubbles in various countries, such as the United States, Ireland, the United Kingdom and Spain played a key role in generating the crisis. There is also consensus that these bubbles were driven by a fast expansion in credit, accompanied by risk-taking and excessive leverage by financial institutions.

The intensity and persistence of the crisis can be largely explained by the fact that the financial sector was seriously affected by the real estate bubble in the main developed economies. A considerable number of financial institutions started to make losses and saw their solvency come under threat in various countries, forcing States to inject money into these institutions with the aim of containing the financial instability. In particular, the financial sector of the Eurozone has received substantial public aid as a consequence of the crisis, which has exacerbated public deficit problems generated by the loss of activity in the real economy.

The responsibility attributed to the financial sector in triggering the current crisis and the amount of public aid which this sector has received has led to an extensive debate both regarding the appropriateness of maintaining a system of public guarantees for this sector and regarding how to spread the load associated with the public aid given.¹ In this context, at its Pittsburgh Summit in 2009, the G-20 requested a report from the International Monetary Fund (IMF) on possible measures to ensure a fair and substantial contribution by financial institutions to government budgets.² The IMF proposed two alternatives. The first consisted of a fund paid for by financial institutions based on their potential risk for financial stability. The objective of the fund would be to meet the cost of any future bailout of financial institutions without having to resort to public aid. The second proposed option consisted of establishing a financial activities tax levied on the sum of the profits obtained by these institutions and the remuneration paid to their employees.

For its part, the European Commission (EC) has opted to develop a different alternative to those suggested by the IMF. Accordingly, on 28 September 2011, the European Commission presented a formal proposal for a Directive of the Council and of the European Parliament to establish a Financial Transaction Tax (FTT). This tax

1 With regard to the second issue, it should be pointed out that in most countries transactions performed through the financial sector are exempt from taxes, such as value-added tax (VAT) and other similar taxes, which are extensively levied on transactions of goods and services in other sectors.

2 International Monetary Fund (2010), *A fair and substantial contribution: A framework for taxation and resolution to improve financial stability*, Draft Report to the G-20.

would be levied on transactions in financial instruments in which financial institutions participate on secondary markets. As indicated in the EC proposal, the aim of this tax is not only to ensure a greater contribution from financial institutions to public budgets, but also to somewhat reduce the size of the financial economy, which, in its opinion, could be excessive compared with the real economy.

The proposal for a directive presented by the EC was discussed at the meetings in June and July 2012. In its meetings, the members of the EU did not reach an agreement to apply the FTT proposed by the EC. However, on 28 September 2012, the EC received a request from ten Member States asking to introduce an FTT in their jurisdictions through enhanced cooperation. Following authorisation from the Council, on 14 February 2013, the EC presented a new FTT proposal for the countries which finally sign up to the enhanced cooperation, which is almost fully based on the previous proposal for a directive. As shall be discussed in detail below, it only introduces one substantial new aspect: an extension of the taxpayer base.

It should be pointed out that the FTT proposal forms part of the European Union's comprehensive strategy to respond to the problems which have been identified as triggers of the current crisis. The European Union is currently immersed in an ambitious regulation programme for the financial services sector.³ This programme aims to make financial services safer by introducing incentives so that financial institutions do not return to practices which have proved to involve excessive risk. The EU's legislative reform of financial services is structured around four strategic objectives: better supervision of the financial sector; strengthening financial institutions and establishing a framework for their bailout, if necessary; an increase in the security and transparency of financial markets; and finally, greater protection for consumers of financial services.

The objective of reducing the size of the financial economy assumed in the EC proposal follows a line of thought within economic literature dealing with financial issues. A large part of this line of thought also affirms that excessive short-term dealing in secondary securities markets may be harmful to financial stability.

In 1972, James Tobin proposed introduction of a tax in currency markets to reduce the threat their volatility poses to financial stability. Prior to this proposal, John Maynard Keynes had proposed a transaction tax on equity trades which would make short-term trading in these assets more difficult.

However, whenever a new tax is introduced, it generates costs and benefits for society as a whole. As indicated below, the FTT is not an unknown in tax systems as several countries have, or had in the past, taxes levied on certain types of financial transaction, albeit in different forms. There is therefore a certain level of empirical evidence that can be used to analyse the effectiveness, with regard to its objectives, and the undesired costs associated with this type of tax.

3 See J. Rodríguez de Agüero (2012), "Recent initiatives in the regulation of securities markets in the European Union: the response to the financial crisis and the review of the main directives", in the CNMV fourth-quarter bulletin 2012, pp. 71-99.

In addition to describing in some detail the features of the FTT proposed by the EC, this article aims to analyse the main costs and benefits that would result from implementing the tax. The analysis is particularly based on the forecasts of the EC itself and the contributions from economics literature, including the contributions from empirical literature based on studies of the experiences in various countries that have applied taxes of this type.

The rest of the article is structured as follows. Section 2 describes the different FTT models which are, or which have been, in force in different countries. Section 3 describes and analyses the FTT proposed by the EC. Sections 4 and 5 focus, respectively, on the potential benefits and costs of the measure. We present our conclusions in Section 6. Finally, Annex I shows the possible redistributive effects of the FTT, and Annex II describes the assumptions and calculations made by the EC in the impact assessment which accompanies its FTT proposals.

2 Precedents in various countries

The proposals for establishing an FTT are often associated with the proposal put forward by the economist James Tobin in the 1970s, which is reflected in two well-known articles on the creation of a uniform international tax levied on spot currency transactions.⁴ In this proposal, Tobin argued that, given the increase in capital mobility, especially following the period in which the Bretton Woods system was in force, the tax could reduce volatility in this market, which would help economies to be more stable and their financing to be less expensive.

Financial transaction taxes have been used in some countries. In fact, various countries have had, or have, taxes of this type in force, although in most cases, the FTTs in force do not cover, as Tobin proposed, spot currency transactions. Within the European Union, countries such as Belgium, Poland, Ireland and the United Kingdom have been applying their own versions of the FTT for some time. In addition, although they do not currently have such a tax in force, Germany and Sweden have used this type of tax in the past. More recently, France, in August 2012, and Greece, in April 2011, unilaterally decided to establish their own versions of the FTT in their respective countries. Outside the European Union, the countries which maintain a tax of this type in force include Singapore, Switzerland and Taiwan.

The FTTs which are in force, or which have been in force, do not share the same design. In particular, in the context of the EU, although almost all the FTTs are levied, or have been levied, on spot share transactions, there are notable differences between them, which are summarised below.⁵

4 See J. Tobin (1974), *The new economics one decade older*, Princeton University Press and (1978), "A proposal for international monetary reform", in *Eastern Economic Journal*, vol. 4, pp. 153-159.

5 An FTT which is only levied on share transactions is called a "Securities Transaction Tax (STT)".

2.1 Belgium

In Belgium, the FTT which is currently in force is called “Tax on Stock Exchange Transactions”. This tax is applied to transactions in shares of listed companies, shares of investment companies, bonds and some types of derivatives. However, for a transaction with these financial instruments to be taxed, it must be executed on an organised Belgian market through Belgian intermediaries.

The tax rate applied varies depending on the type of transaction. Specifically, a rate of 0.07%, with a maximum of 500 euros per transaction, is applied for shares of investment companies and bonds of Belgian public debt or public debt of other States, and a rate of 0.17%, with a maximum of 500 euros per transaction, for any other type of financial instrument.

There are some important exemptions to payment of the tax, which include transactions for their own account made by financial institutions (banks, insurance companies, pension funds and mutual funds) and transactions for their own account made by non-resident taxpayers.

2.2 Poland

In Poland, the financial transaction tax forms part of a more general tax which is levied on any sale or exchange of property rights. The FTT is applied to transactions on any security or derivative product which generates legally recognised property rights. The tax is levied on transactions performed on organised markets, as well as on bonds and Polish Treasury bills. The tax rate applied to these transactions is 1% and must be paid by the buyer of the security or derivative.

2.3 Ireland

In Ireland, a tax is applied to the sale or transfer of shares of Irish companies and derivatives whose underlying is made up of shares of Irish companies. In this case, the taxpayer is the person who receives the shares or derivatives and the applicable tax rate is 1% of the instrument’s market value.

2.4 United Kingdom

In the United Kingdom, there are two taxes of these characteristics which are currently in force: Stamp Duty and Stamp Duty Reserve Tax. Those taxes are levied on sales and exchanges of shares. The first of these, Stamp Duty, is levied on transactions in which the transfer of shares is accredited by physical documents, for example traditional share certificates which must be presented or submitted upon settlement. However, when transactions affect shares represented by book entry, and which are settled electronically, the applicable tax is the Stamp Duty Reserve Tax.

In any event, for both taxes a rate of 0.5% of the value of the transaction is applied. The amount must be paid by the buyer, irrespective of whether the transaction has

been performed in the United Kingdom or whether either of the parties is resident in the United Kingdom.

2.5 Greece

In April 2011, Greece introduced a tax levied only on the sale of shares listed on organised markets, for trading conducted both on organised markets and on OTC markets. The tax rate applicable to these transactions was 0.2%. This tax is no longer applicable as from 1 January 2013.

2.6 France

As indicated above, the French version of the FTT was introduced in August 2012. The FTT levies a 0.1% tax on the buyer in purchases or swaps of shares of companies listed on organised markets with residence in France providing their capitalisation is greater than 1 billion euros. Both residents and non-residents in France are subject to this tax.

This FTT is also specifically levied on sales of shares through high-frequency trading by means of an additional 0.01% of the value of said transactions. In addition, this tax rate is also applied to credit default swaps (CDS) whose underlying is the debt of EU Member States. Unlike transactions involving the transfer of share ownership, the tax on CDS transactions is only applicable to residents in France.

2.7 Sweden

In 1984, Sweden introduced a 0.5% tax on the purchase or sale of shares and on the notional value of share options. The tax was applied to all sales made in the country which used local brokerage services. Both buyers and sellers were subject to the tax. The tax rate was revised in 1986 and increased to 1%.

Application of the tax was extended in January 1989 to include fixed-income securities. In this case, a lower tax rate of 0.002% was established for instruments with a maturity of 90 days or less, and of 0.03% for bonds with a maturity of five years or more.

The Swedish FTT on fixed-income securities was only in force until 15 April 1990, when it was repealed. For its part, the tax on transactions with shares and share options was also repealed at the end of 1991, after the tax rate was halved in January of the same year.

The Swedish tax was repealed for several reasons.⁶ Firstly, the revenues obtained from collecting the FTT were much lower than the forecasts. It was expected to raise

6 See S. R. Umlauf, S. R. (1993), "Transaction taxes and the behaviour of the Swedish stock market", in *Journal of Financial Economics*, vol. 33, pp. 227-240; G.W. Schwert and P.J. Seguin (1993), "Securities trans-

an annual amount of close to 1.5 billion Swedish kronor. However, the annual amount raised by this tax was only 50 million kronor. Furthermore, the authorities estimated that the introduction of the FTT led to a reduction in the amount raised through capital gains tax by a similar amount to that obtained by the new tax. Therefore, there was no increase in total tax raised in net terms. The fall in the amount raised by capital gains tax was the result of the fall in the price of assets, which was the result of the negative impact on their discounted present value of the expected tax levied on their future trading.

Secondly, a substantial displacement of trading was seen following introduction of the FTT. It is estimated that in 1990 over 50% of trading on Swedish equity had moved to London. Foreign investors in equity decided to avoid the tax by trading Swedish equity securities outside Sweden, while domestic investors reduced their trading volume.

The fall of fixed-income and derivative trading on the Swedish market was even sharper despite the tax rate being lower. During the first week of the FTT on bond trading, the volume of bond trading on the Swedish market fell by 85%. For its part, the introduction of the FTT in the derivatives market led to a 98% drop in futures trading and the disappearance of the options market. Following the repeal of the tax, trading volumes in equity, fixed-income and derivative assets recovered in a short period of time and grew substantially during the 1990s.

The experts that have analysed the impact of the Swedish FTT over the time that it was in force essentially identified two reasons why this tax brought more costs than benefits. Firstly, the tax was only applied to Swedish investment firms. Any transaction with Swedish securities made through intermediaries which were not Swedish avoided payment of the tax. Secondly, there was a wide range of financial products not subject to the tax and which could be considered as substitutes for the taxed financial assets, which facilitated tax arbitrage.

3 The financial transaction tax proposed by the European Commission

As indicated above, the proposal to establish a financial transaction tax, finally assumed by eleven Eurozone countries, has its origin in the general consensus that the financial sector should make a greater contribution to the costs generated by the crisis.⁷

The proposal for a directive presented on 28 September 2011 by the European Commission, which was initially aimed at establishing a common Financial Transaction

action taxes: an overview of costs, benefits and unresolved questions", in *Financial Analysts Journal*, vol. Sept-Oct, pp. 27-35; and J.Y. Campbell and K.A. Froot (1994), "International experiences with securities transaction taxes", in *The Internalization of Equity Markets*, pp. 227-308, University of Chicago Press.

7 See the Proposal for a Council Directive on a common system of financial transaction tax, amending Directive 2008/7/EC.

Tax (FTT) for all Member States of the EU, was also based on other arguments. In particular, the proposal highlighted the existence of advantageous tax treatment for the financial sector compared with other economic sectors. This advantage comes from the fact that most services in this sector are exempt from the payment of value added tax (VAT). Consequently, according to the European Commission, introducing a financial transaction tax (FTT) would contribute towards establishing a level playing field with other sectors.

This proposal for a Directive advocated an FTT levied on the value of certain transactions performed by financial institutions which act in their capacity as party to the transaction, with the tax applied before any netting off.⁸ For these purposes, the definition of financial institution was broad and included investment firms, credit institutions, organised markets, insurance and reinsurance undertakings, collective investment undertakings and their managers, pension funds and their managers, holding companies and financial leasing companies. Financial institutions also included, for these purposes, other natural or legal persons carrying on certain financial activities on a significant basis. However, central counterparties and central securities depositories were not considered as financial institutions for the purposes of the FTT.

The initiative proposed taxing transactions performed on secondary markets of financial instruments, specifically, instruments traded on capital markets, money-market instruments (with the exception of instruments of payment), units or shares in collective investment undertakings (which include UCITS and alternative investment funds) and derivatives agreements.⁹

The scope of the tax in the proposal was not limited to trading on organised markets, such as regulated markets or multilateral trading facilities, but also covered other types of trades, including over-the-counter trades. Neither was it limited to transactions involving the transfer of ownership of the instruments, but also to those transactions in which a financial institution assumes the risk implied by a given financial instrument (“purchase and sale”). In particular, this included securities lending between entities in the same group. Furthermore, where a derivatives agreement results in a supply of financial instruments, in addition to the taxable derivative agreement, the supply of financial instruments is also subject to tax, provided that all the conditions for taxation are fulfilled.

For the purposes of establishing a precise definition of the instruments whose purchase, sale or transfer were subject to the FTT, the Commission proposal referred to Annex 1 of Directive 2004/39/EC, known as MiFID. From the definitions established in this Directive, we can deduce that, in accordance with the Commission proposal,

8 The proposal for a Directive was supported by Article 113 of the Treaty on the Functioning of the European Union (TFEU). This article entrusts the Council, after consulting the European Parliament and the Economic and Social Committee, to adopt provisions for the harmonisation of legislation concerning indirect taxation in the EU to the extent that such harmonisation is necessary to ensure the establishment and functioning of the internal market and to avoid distortion of competition.

9 However, the proposal excluded transactions performed with the European Central Bank and national central banks from the scope of the tax so as to avoid any negative impact on the refinancing possibilities of financial institutions or on monetary policies in general.

all spot transactions with financial instruments would be subject to taxation, except transactions in currency markets.¹⁰ In the case of derivatives, the tax would be levied on currency derivatives, as well as on commodity derivatives.

It is important to highlight that, according to the Commission proposal, transactions which are performed on the primary market would not be subject to the FTT so as to avoid an increase in the cost of financing for non-financial sectors using capital markets, with the consequent negative impact on economic growth. Furthermore, taxing primary market transactions would enter into conflict with Council Directive 2008/7/EC concerning indirect taxes on the raising of capital, which does not allow additional taxes to be established on raising capital by issuing bonds or shares.

With regard to the territorial application of the FTT, the initial Commission proposal suggested using the residence principal. This means that for a financial transaction to be taxed, one of the parties must be established in the territory of a Member State. In this case, payment of the tax would take place in the Member State where the financial institution intervening in the transaction is established and would be independent from the location of the market (inside or outside the EU) where the transaction took place.¹¹

An important aspect in the design of any tax is the manner of determining the taxable amount on which the tax rate will be applied. This FTT proposal includes two ways of calculating the taxable amount, depending on whether they are spot or derivative transactions. In the first case, a price is usually set and, therefore, a total amount for the sale or transfer, which will constitute the taxable amount for the FTT. However, to avoid market distortions, when the transaction is made at a price lower than the market price or for transactions taking place between group entities, the taxable amount is to be the market price determined at arm's length at the time the FTT becomes chargeable. In the case of derivative agreements, the taxable amount shall be the notional amount of the underlying at the time the derivative agreement is purchased/sold or transferred.

With regard to the rates which will be applied to spot transactions, the proposal puts forward a rate of 0.1% for each one of the parties in transactions with shares and bonds. The tax rate for derivative agreements would be 0.01% for each one of the parties.

10 It was assumed in the proposals that a tax on currency transactions affecting the official currencies of Member States of the EU would breach Article 63 of the Treaty on the Functioning of the European Union, which prohibits restrictions on capital movements between Member States. With regard to transactions in currencies of countries which do not belong to the EU, Article 64.3 of the TFEU would allow adoption of a tax of this nature, although it could be interpreted by third countries as a protectionist measure.

11 When both parties to a transaction are resident in a territory of a State which is not a member of the Union, the Commission proposal did not consider the transaction as subject to the FTT unless one of the parties in the transaction performs part of its activity in a Member State of the EU. In this case, the financial institution of a third country should be considered for this purpose as an institution resident in the Member State in question, and the transaction would be subject to the tax in that State. Where transactions are carried out on trade venues outside the EU, they would be subject to the tax if at least one of the establishments carrying out or intervening in the transaction is located in the EU.

The European Commission proposal for a directive was discussed at the Ecofin Council meetings held in June and July 2012 without an agreement being reached to introduce a common FTT for all EU Member States. However, on 28 September 2012, the EC received a request from ten Member States asking it to submit a proposal for a Council Decision to authorise implementation of the FTT in their territories by means of an “enhanced cooperation” procedure.¹² On 23 October 2012, the EC proposed to the Council authorisation of the procedure, which was ratified on 22 January 2013.¹³

On 14 February 2013, the EC presented the new FTT proposal which will be implemented in the eleven countries which have so far signed up to the enhanced cooperation. This proposal is largely based on the criteria and principles of the proposal for a Directive made by the EC in 2011.

The new proposal only contains one significant amendment, which affects the determination of the parties liable for the tax. Specifically, in addition to the residence principal, now limited to the countries which implement the enhanced cooperation, a criterion has been added based on the place where the instruments are issued. This means that, in addition to taxing any financial transaction made by a resident of any of the countries implementing enhanced cooperation, transactions between non-residents trading in assets issued in said States will also be taxed.

In any event, it is important that the FTT which is eventually implemented through the enhanced cooperation should take into account the experiences with this type of tax, especially those, such as the Swedish one, which may be considered as failures.

A first step to be taken when deciding on the design of the future tax must be to establish the financial instruments and markets which it will be applied to. With regard to the financial instruments, the main objective of the design is to limit as far as possible the likelihood that the tax may be avoided by using highly substitutable financial products which enjoy different tax treatment. On this point, the initial EC proposal addressed the problem by requiring that the tax be applied to trading with shares, fixed-income instruments and any type of derivative. The only transactions not subject to the tax were spot currency transactions.¹⁴ Essentially, the catalogue of instruments considered by the EC includes the financial instruments listed in section C of Annex I of the MiFID, plus currency derivatives.

With regard to the markets whose transactions would be subject to tax, the EC proposal indicated that transactions both on regulated markets and on OTC markets would be taxed. Transactions on the primary share and bond markets would be exempt as this would breach EU legislation, as indicated above. The aim of applying

12 The countries which requested the enhanced cooperation were Austria, Belgium, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia and Spain.

13 “Enhanced cooperation” is a procedure whereby a minimum of nine Member States are allowed to adopt a legislative initiative proposed by the EC when it is not possible to reach an agreement to adopt it in all Member States of the EU. The conditions under which “enhanced cooperation” may be conducted are regulated in Article 20 of the Treaty on European Union and Articles 326 to 334 of the Treaty on the Functioning of the European Union.

14 See footnote number 10.

the tax both to organised markets and OTC markets is to avoid arbitrage between markets for tax reasons, with the consequent loss of competitiveness of the market whose trading is subject to the tax.

An important aspect in the design of the tax is to suitably define when the tax becomes chargeable for the parties to a transaction. There are three main options: when transfer of ownership takes place, when the agreement enters into force and when payment of the economic consideration is made by the buyer to the party which transfers the instrument.

A decision on this aspect should take into account both the incentives which may be generated as well as the features of the financial instruments and trading and post-trading processes. For example, the third option could generate incentives to defer payments over time for the parties to a transaction. That is the reason why the EC opted in its proposal to set the chargeability in spot transactions at the time ownership is transferred. However, this same criterion may not be applied to derivative agreements as transfer of ownership of the underlying may occur, as the case may be, a long time after the agreement has been closed. For this reason, for derivatives, the EC proposed that the tax should become chargeable at the time the parties agree to the derivative contract.

An equally important issue is to determine the jurisdiction which will have the right to collect the tax. There are, in principle, three possible criteria: the tax residence of the parties involved in the transaction, the jurisdiction where the transaction takes place and the jurisdiction where the instrument subject to the transaction was issued. In its first proposal for a Directive, the EC only opted for the first possibility. The other two possibilities were ruled out because they involved greater risk of the trading in certain assets being displaced from the current market to other markets. However, the implications of this decision will have to be considered after adopting the criteria to also levy the tax on transactions in securities issued in the countries implementing the enhanced cooperation, as included in the EC proposal of February 2013.

If the second possibility is applied i.e. if collection of the tax is assigned to the jurisdiction where the transaction takes place, the risk of trading moving to other markets and, ultimately, the trading venues themselves being displaced to third countries could be considerable, as demonstrated by the experience of the Swedish FTT. A possible alternative to this option would be to demand payment of the tax in the jurisdiction where the contracts are settled. One advantage of this criterion compared with the other alternatives is that it does not necessarily require identification of the parties intervening in each transaction, thus reducing considerably the cost of processing the tax. However, given that on many occasions neither the place of trading nor the jurisdiction of residence of the parties coincide with the Member State where the contract is settled, this option could generate conflicts between Member States based on the distribution of money raised from the tax.

The criterion based on the place where the security was issued is the one which is currently in force in the United Kingdom. This method of defining the place where the FTT is paid works well if the tax is applied to share transactions. However, this criterion could favour derivatives trading being displaced to other markets as there

is no legal obligation to issue them in the same place as the underlying asset. However, this last effect is less important when, as in the case of the proposal made by the EC on 14 February 2013, this criterion is accompanied by another criterion to determine the taxpayers based on their place of residence.

The alternative of taxing transactions performed by residents of the countries operating the enhanced cooperation also involves the risk of displacement of trading to other markets, although the EC argues that it will create less distortion than the other options. In this case, the risk of displacement would not be determined by the possibility that trading might move to other markets or countries, but that the parties might move to other jurisdictions. This risk could especially materialise in the transfer of securities trading from some financial institutions to subsidiaries which are located outside the EU. Although this incentive would be lower the more the entity trades with assets issued in one of the countries which eventually implement the enhanced cooperation.

Another of the key aspects when designing an FTT is to define the taxable amount. In the case of spot transactions, extensive experience has been obtained from the implementation of this type of tax in various countries. In this case, the most reasonable alternative is to define the taxable amount as the amount of the purchase/sale transaction or, failing that, the amount of the transaction if it has been performed in a reference market. However, calculating the taxable amount in the case of derivative agreements leads to the dilemma of choosing between the premium of the derivative or the notional amount of the agreement.

The EC opted to propose the use of the notional amount as the taxable amount for the FTT in derivative agreements. The EC justified its proposal by arguing that the use of the notional amount allowed the FTT to be applied more easily and directly, at the same time guaranteeing low administrative and compliance costs. If, however, a taxable amount based on the market value of the derivative is used, it will be necessary to take into account the fact that it is sometimes difficult to determine the market value as there are no economic considerations in the transaction. In these cases, it would be necessary to have the help of Marked-to-Market or Model-to-Market models to obtain an approximate market value for the derivative agreement.

Another important argument for using the notional value as the taxable amount is that its use would make it more difficult to create an artificial reduction of the tax pressure through a creative design of derivative agreements as no tax incentives are generated with regard to derivatives with netting of contracts. Furthermore, the choice of the notional amounts makes it easier for the tax to be applied at the time the sale/purchase or transfer agreement is entered into and does not depend on the cash flows which the agreement may generate over its existence, which, as analysed above, may introduce undesired incentives.

With regard to the applicable tax rates, the EC opted to use different rates for spot transactions and derivative agreements. One single rate for all transactions could have advantages in terms of simplicity, both in applying and processing the tax. However, if the same rate applied to spot transactions was applied to derivative agreements, the amount of the tax could be disproportionate in many derivative agreements, especially compared with the premium effectively paid in derivative

agreements. Therefore, in this scenario, the use of a single rate similar to that proposed for share transactions could excessively raise the cost of hedging using derivatives and lead to a fall in the number of derivative agreements below a desired level.

One of the decisions which the EC has taken with regard to the rates to be applied in the FTT is that the rates should be low compared with those currently applied in other countries (0.1% for both parties in spot transactions and 0.01% for both parties in derivative agreements). Accordingly, for spot transactions it has opted for a rate of 0.2%, counting both parties to the transaction, compared with, for example, the rate of 0.5% applied to buyers of shares in the United Kingdom. This EC decision has a twofold aim: firstly to keep the distortion in financial markets caused by the FTT as low as possible. The second is for the incentives to avoid the tax to be very small as the FTT would be a small part of the total amount of the transaction.

Although all the aspects analysed up to this point are important, there is one characteristic of the future FTT which cannot be ignored. As commented above, although the initial EC proposal aimed to implement the FTT throughout the European Union, in the end only eleven countries in the Eurozone will adopt the tax under enhanced cooperation. This fact may generate uncertainty as regards the impact of the tax and its sustainability over time. It should be remembered that, in a tax of this type, a sufficiently generalised and harmonised application on an international level is essential for reducing its undesired effects in terms of the displacement of trading activity or the financial intermediaries themselves.

By means of a simple example based on game theory, it is possible to explain why it is important for there to be maximum coordination when applying this type of tax. Let us suppose that two countries, A and B, are studying whether to establish an FTT with the same characteristics in their jurisdictions. Neither country knows beforehand what decision the other country will take with regard to implementing the FTT. Both countries think that if they both implement the FTT at the same time, they may achieve greater levels of social welfare. The increase in welfare would come from strengthening financial stability and obtaining revenue which could be used for redistribution policies or improving efficiency in other production sectors.

However, in the event that one of the countries imposes the FTT and the other country does not, it is fairly likely that the country which imposes the FTT will see its welfare fall, while the other country will see its welfare increase. This is due to the fact that part of the markets and financial institutions operating in the market which imposes the tax may move to the country which has decided not to impose the tax. Accordingly, the country which imposes the tax would lose part of its financial system, and at the same time the amount that it raises through the tax would be small. On the other hand, the other country would attract at least part of the financial system of the country which imposes the tax, which would lead to more employment and taxes (more money raised through taxes on employment and business profits).

Let us suppose that the cells of the matrix presented in table 1 reflect the levels of welfare that each one of the countries would reach based both on their decision and on the decision of the other country. The level of welfare in country A is represented by the first element in each one of the cells of the matrix and the welfare of country B by the second element. We assume that the higher the score, the higher the welfare.

		Country B	
		No FTT	FTT
Country A	No FTT	100, 100	120, 80
	FTT	80, 120	110, 110

Source: CNMV.

We can see in the matrix that if the countries simultaneously and unilaterally establish an FTT (second row, second column), both would achieve higher levels of welfare. However, this possibility is not guaranteed as both countries have incentives not to implement the FTT with the hope that the other country will implement it, and thus attract towards their jurisdiction part of the trading activity and achieve an even greater level of welfare (second row, first column and first row, second column). Consequently, it is highly likely that the only way in which an FTT would be implemented, a solution which in theory would benefit both countries, is for both countries to be willing to cooperate with each other, negotiating a binding agreement so as to implement the tax.¹⁵

4 The benefits of establishing an FTT

There are essentially two potential benefits for which a government or, in this case, a set of EU countries, might propose implementing an FTT. The first is to correct market failures by imposing a price on possible negative externalities. In this case, the FTT would help change the behaviour of participants in financial markets so that it is more in line with socially desirable objectives. This type of tax is known in economics literature as a “pigouvian tax”.¹⁶ The second benefit is to increase tax revenues.

The existence of a market failure in financial markets was described by Keynes (1964) and Tobin (1978), although each of them referred to different financial markets: Keynes to the stock market and Tobin to the currency market.¹⁷

15 The uncooperative game between two countries represented in Table 1 is a version of the well-known prisoner’s dilemma. The Nash equilibrium of this game is uncooperative, i.e. the solution to the game that represents the best individual option for each participant in the event that the other participant also chooses their best response is the strategy pair (No FTT, No FTT). However, there is another strategy pair in the example game (FTT, FTT), where both players obtain a greater reward in terms of welfare i.e. in accordance with economic theory they produce a higher Pareto solution or balance greater than the Nash equilibrium. For further details about the prisoner’s dilemma, consult for example, R. Gibbons (1993), *A primer in game theory*, Antoni Bosch editor.

16 See A.C. Pigou (1920), *The economics of welfare*, London, Macmillan.

17 J.M. Keynes (1964), *The general theory of employment, interest and money*, San Diego, Harcourt Brace and Co.; J. Tobin. (1978), “A proposal for International monetary reform”, in *Eastern Economic Journal*, vol. 4, pp. 227-240. The analysis of these two markets was the starting point for authors such as J. Stiglitz (1989), “Using tax policy to curb speculative short-term trading”, in *Journal of Financial Service Research*, vol. 3, pp. 101-115 and L.H. Summers and V.P. Summers (1989), “When financial markets work too well: A cautious case for securities transaction tax”, in *Journal of Financial Services Research*, vol. 3, pp. 261-286, to propose that this type of tax should generally be applied to all financial markets. Following the breakout of

Tobin (1978) shares the view of financial markets described in the comparison made by Keynes (1964) between financial investment and a beauty contest organised by a newspaper. In this competition, the participants had to choose the six prettiest faces from 100 photographs. The prize would be awarded to the participant who could best predict which face would receive most votes from among all the participants in the competition. Therefore, the participants had to choose, not the faces which they thought the prettiest, but those which they thought would receive the most votes. In addition, each of the participants must bear in mind that the others also face the same strategy. With this analogy, Keynes tried to reflect the objectives of short-term trading, where the fundamental value of the asset traded could be less important for an investor that anticipating what other market participants would believe it could be worth.

Given this distinction between the fundamental long-term value of an asset and the value attributed to it in short-term trading, Keynes (1964) proposed the term “speculation” to classify short-term trading in financial markets. The view of this author was that speculation predominated in trading of an asset when access to trading was easy and cheap. If all participants in the market ultimately carry out short-term investing, the function of the market may be similar to that of a casino and the price of the assets would no longer suitably reflect their fundamental value.

Therefore, that “excess” of short-term trading could lead to a negative externality for long-term investors as it separates an asset’s market price from its fundamental value. Excessive short-term trading would make the creation of bubbles more likely, which could endanger financial stability. That is why Keynes proposed the introduction of a tax so that trading in stock markets would be more expensive, which would in turn reduce short-term trading.¹⁸ Another of the benefits of the tax put forward by Keynes was that it would improve corporate governance of companies. As companies would have longer time horizons, their managers could be less short-sighted in the sense of not having to offer results with short-term projects, being able to focus more on projects with greater profitability over the long-term.¹⁹

The analysis used by Tobin (1978) uses similar arguments when it aims to demonstrate that there is a negative externality in the currency market. In this article, Tobin argues that the introduction of a tax in this market would decrease short-term trading and could lead to more stable markets as volatility would be reduced. In general, the defenders of the tax argue that it would reduce market volatility and unproductive short-term speculation as investors would have more incentives to make long-term investments.

However, other authors argue that it would not always be advisable to reduce the participation of investors referred to as “speculators”. Dooley (1996) argues against the assumption that short-term investors do not invest in accordance with the as-

the crisis, other authors such as S. Schulmesiter, M. Schratzenstaller and O. Picek (2008), *A general financial transaction tax. Motives, revenues, feasibility and effects*, Research study by the Australian Institute of Economic Research, have argued about the advantages of imposing a financial transaction tax.

18 In Keynes (*op. cit.*) we can find the following quote: “.....It is usually agreed that casinos should, in the public interest, be inaccessible and expensive. And perhaps the same is true of Stock Exchanges.”

19 See, for example, L.A. Stout (1995), “Are stock markets costly casinos? Disagreement, market failure and securities regulation”, in *Virginia Law Review*, vol. 81, pp. 611-712.

set's fundamental price.²⁰ According to this author, there is no evidence that the investors who base their investments on the fundamentals of a company have an investment period in the assets greater than those referred to as "speculators". Following the same line, Song and Zhang (2005) find that a fall in the volume of investors who do not base their decisions on fundamentals and, therefore, the drop in market volatility, is contingent to the characteristics of the market itself.²¹

The empirical literature shows that the possible benefits of an FTT depend on the characteristics of the market affected. Accordingly, Hau (2006), with regard to the introduction of a minimum tick in the stock market, showed an increase in transaction costs resulting from the measure led to an increase in volatility in the Paris Bourse.²² Other examples of empirical studies which provide evidence along the same lines are those by Bond, Hawkins and Klemm (2004) and Jones and Seguin (1997).²³ The first of these studies analyses the effect that Stamp Duty has on transaction costs and, therefore, share prices in the United Kingdom. The second article analyses a reduction in transactions costs which took place on the New York Stock Exchange in the middle of the 1990s. In both articles, the authors reject the hypothesis that an increase in transaction costs leads to a fall in the volatility of asset prices.

Two more recent articles, Baltagi, Li and Li (2006) and Liu and Zhu (2009), show that it is difficult to obtain conclusive evidence on the effects of imposing an FTT.²⁴ The first article analyses the impact of increasing the tax from 0.3% to 0.5% in the Chinese stock market. The authors find that the measure reduced the volume of trading by one third and that volatility increased significantly. However, Liu and Zhu (2009) found in their analysis of the Japanese stock exchange that an increase in transaction costs led to a fall in volatility.

The evidence from these articles suggests that in order to study the possible impact of an FTT throughout the EU, or in a specific group of countries, it will be necessary to evaluate the impact on each one of the stock markets which it affects. Although it is fairly safe to predict that the creation of an FTT will lead to a drop in trading in the affected markets as a whole, it is not easy to know beforehand what effect the tax will have on volatility in these markets.

Another of the benefits indicated by FTT defenders is that introducing a tax of this type may help to reduce systemic risk.²⁵ In particular, they indicate that an FTT

20 J. Dooley (1996), "The Tobin tax: Good theory, weak evidence, questionable policy", in *The Tobin tax: Coping with financial volatility*, Oxford University Press.

21 F. M. Song and J. Zhang (2005), "Securities transaction tax and market volatility", in *The Economic Journal*, vol. 115, pp. 101-115.

22 H. Hau (2006), "The role of transaction costs for financial volatility: evidence from the Paris Bourse", in *Journal of European Economic Association*, vol. 4, pp. 862-890.

23 S. Bond, M. Hawkins and A. Klemm (2004), *Stamp duty on shares and its effects on share prices*, Institute for Fiscal Studies working paper 04/11; C.M. Jones and P.J. Seguin (1997), "Transaction costs and price volatility: evidence from commission deregulation", in *The American Economic Review*, vol. 87, pp. 728-737.

24 B.H. Baltagi, D. Li and Q. Li (2006), "Transaction tax and stock market behaviour: evidence from an emerging market", in *Empirical Economics*, vol. 31, pp. 393-408; S. Liu, and Z. Zhu (2009), "Transaction costs and price volatility: new evidence from the Tokyo Stock Exchange", in *Journal of Financial Service Research*, vol. 36, pp. 65-83.

25 According to Anthony *et al* (2012), systemic risk refers to the probability that a negative shock from one or some of the market participants may damage the financial system as a whole. Systemic risk in finan-

could reduce systemic risk through two routes: by reducing market volatility or by making it more difficult for bubbles to appear in financial markets. As discussed above, there is no clear evidence that establishing an FTT would lead to a reduction in market volatility.

With regard to the formation of bubbles in financial markets, Scheinkman and Xiong (2003) concluded, in a predominantly theoretical article, that a small tax on transactions would reduce speculative trading.²⁶ This result was confirmed by Porter and Smith (2003), who by means of a laboratory experiment were able to verify that an increase in transaction costs led to a reduction in the size of bubbles.²⁷

However, there are markets, such as the real estate market, where bubbles of a considerable size have appeared, as occurred recently in some countries, even though they were markets where transaction costs are high. It can therefore be expected that the results of introducing an FTT will have a limited effect on systemic risk caused by the formation of bubbles in financial asset prices.

The use of an FTT to ensure that the financial system makes a greater contribution to public finances has taken on greater importance since 2008 as a result of the public aid received by the financial sector. Shaviro (2012) demonstrates that implementing an FTT may allow the financial system to make a greater and fairer contribution to the public purse.²⁸

With regard to the September 2011 proposal for a directive to introduce an FTT throughout Europe, the European Commission suggests that the new tax could raise 37 billion euros per year. Subsequently, in the latest proposal for enhanced cooperation, the EC estimated that 34 billion euros would be collected in the countries which implement the enhanced cooperation and that 57.1 billion euros would be raised if it were implemented throughout the EU. Table 2 shows a breakdown of the tax revenue that the EC estimates for the countries which plan to implement the enhanced cooperation by type of instrument.

From a social equality point of view, taxes are important because they make it possible to redistribute income among the population and reach higher levels of social welfare. Against the current backdrop of financial restrictions in the public sector, being able to generate new revenue is one way of maintaining, as far as possible, that income distribution.²⁹

cial markets is mainly a result of the fact that credit institutions are exposed to the same risk (risk correlation) and the possibility that materialisation of a risk in a credit institution or a group of institutions may propagate to the rest of the financial system (contagion risk).

26 J. Scheinkman and W. Xiong (2003), "Overconfidence and speculative bubbles", in *Journal of Political Economy*, vol. 111, pp. 1183-1219.

27 D. Porter and V. Smith (2003), "Stock market bubbles in the laboratory", in *The Journal of Behavioral Finance*, vol. 4, pp. 7-20.

28 D. Shaviro (2012), *The Financial Transaction Tax versus the Financial Activities Tax*, NYU Law and Economics research paper 12/04.

29 See Annex I.

Potential revenue from FTT by instrument type

TABLE 2

Billion euros

Instrument	Potential revenue
Spot shares	4.6
Spot bonds	8.4
Interest rate linked derivatives	16.5
Equity linked derivatives	1.8
Currency linked derivatives	2.7
Total	34.0

Source: European Commission.

5 Costs of establishing an FTT

In general, taxes introduce incentives which affect the decisions of economic agents. They can therefore generate distortions in the allocation of resources through markets. The only exceptions to this rule are lump-sum taxes paid by everybody, although these taxes are often classified as regressive as they involve a proportionally higher burden for individuals with fewer resources.³⁰

In the designs applied to date, and in the design proposed by the European Commission, the FTT is a tax on the trading volume in the market of the affected financial asset. Therefore, this tax may generate undesired interference in market functioning. The potential effects of a tax of this type which need to be considered include the following:

- A possible reduction in trading volume of the financial assets and the possible consequences for financial institutions which act as intermediaries or participate in this activity, in particular as regards the employment generated by those institutions. As with other effects, those described herein may be offset by the benefits of the measure in terms of social welfare, for example, if it is concluded that trading volumes or the size of the financial sector are excessive and involve a risk for financial stability.
- Incentives to the displacement of trading activity or financial institutions.
- Possible increase in financing costs for companies which raise finance through securities markets.
- Distortions in the capital structures of companies and in the portfolios of savers.
- Potential reduction in revenue deriving from other taxes, for example capital gains taxes.
- Impact of implementation and compliance costs for financial institutions.

30 See, for example, E. Albi, J.M. González-Páramo and J. Zubiri (2000), *Economía pública II. Teoría de la imposición e ingresos públicos* [Public Economics II. Theory of taxation and government revenue], Ariel Economía.

One of the arguments which is most used by those who oppose the tax is that it will increase transaction costs, reducing trading volume and, consequently, market liquidity and efficiency. Various studies have demonstrated empirically that introducing an FTT leads to a fall in the trading volume in securities markets. Baltagi, Li and Li (2006), using stock market data, show that an increase of 1% in the tax rate applied in these markets would lead to a 0.5% fall in trading volume. For their part, Chou and Wang (2006), in an analysis of the Taiwan futures market, found that a 1% increase in the tax rate would lead to a fall of 1% in this market.³¹ In the case of the FTT proposed in 2011 for the EU, the EC estimates that introducing the tax would lead to a 15% total fall in the trading volume in the bond market and 75% fall in the derivatives market. However, as commented above, this fall in trading might not be considered an unbearable cost if we accept the current argument that the trading volume might be excessive from a social point of view.

It has also been shown empirically that introducing an FTT affects the efficiency of financial markets. The evidence is based on the effect of this type of tax on bid-ask spreads in different financial markets, where it has been seen that these taxes lead to an increase in spreads. Specifically, Wang *et al* (1997), Wang and Yau (2000) and Chou and Wang (2006) analysed various futures markets belonging to the Chicago Mercantile Exchange, both financial (equity and bond indexes) and for commodities (gold, silver, copper, wheat and soybean). These authors found that the bid-ask spread in these markets increased by between 0.6% and 2.6% when the tax rate rose by 1%.³² In another article, Schmit (2007) found that in the currency market, the increase in the bid-ask spread was 0.4% when the tax rate rose by 1%.³³

Kupiec (1996) indicates that one of the main costs resulting from the creation of an FTT would be the short-term fall in the price of financial assets and, consequently, the wealth of investors in these assets.³⁴ According to this author, the prices of financial assets would be adjusted, due to the fact that their potential buyers would take into account the higher transaction costs resulting from the FTT when buying and selling the assets. Economic history provides some examples regarding this type of effect. During the US Civil War, the introduction of a 0.5% tax on gold transactions led to a 15% fall in the price of gold. More recently, in 1986, the main Swedish share index fell by 2.2% on the same day of the announcement of a rise in the tax on equity transactions from 0.5% to 1%.

Furthermore, over the long term, the FTT could have a negative impact on economic growth. It is argued that the cost faced by companies when they try to raise funds through the market will be greater following introduction of the tax as investors will discount the increase in the cost associated with transactions in the secondary mar-

31 R. Chou and G. Wang (2006), "Transaction tax and market volatility of the Taiwan Stock Index Future", in *Journal of Future Markets*, vol. 26, pp. 1195-1216.

32 See G. Wang, J. Yau and T. Baptiste (1997), "Trading volume and transaction costs in future markets", in *Journal of Future Markets*, vol. 17, pp. 757-780; G. Wang and J. Yau (2000), "Trading volume, bid-ask spreads, and price volatility in future markets", in *Journal of Future Markets*, vol. 20, pp. 943-970.

33 R. Schmidt (2007), *The currency transaction tax: rate and revenues estimates*, Ottawa North South Institute working paper.

34 P. Kupiec (1996), "Noise traders, excess volatility, and a securities transaction tax", in *Journal of Financial Services Research*, vol. 10, pp. 115-129.

ket and will demand a greater return from the issuer. Consequently, it could be the case that introducing the tax would lead to a fall in investment and economic growth.

Among the studies which analyse this possible effect, Matheson (2011) concludes that a securities transaction tax on stocks of 10 basis points would lead to a 25-basis point increase in financing costs for a company which only raised funds through equity.³⁵ Taking this result as a starting point and assuming that companies raise finance both with their own capital and through debt issues, whose holders usually keep the securities for longer than in the case of shares, Anthony *et al* (2012) conclude that the impact could actually be between 15 and 30 basis points.³⁶ The same authors use the long-term relationship between the cost of financing and the growth of an economy to conclude that an increase in the tax of between 15 and 30 basis points would lead to a fall in long-term GDP of between 0.4% and 1.2%.³⁷

Another of the possible negative effects of introducing the tax, in addition to that mentioned above, is a distortion when setting optimal portfolios from an investor's point of view. Such a distortion could occur in the event that the tax, as envisaged in the September 2011 proposal for a directive by the European Commission, is not levied neutrally across trading in different assets. In this case, it would alter the relative prices of the assets, which would favour an under-weighting in a portfolio of the assets which are most frequently traded and which are subject to higher tax rates. Taking the Commission proposal as a reference, this effect could be more visible for repos on bonds and shares. If this effect materialises, issues of these instruments would have to be made less frequently than their issuers would like as they would be less attractive for final investors.

Although the introduction of a new tax involves *a priori* a new source of government revenue, the impact on the total tax collected could even be negative if the introduction of the tax generates distortions which affect the tax collecting capacity of existing taxes. As commented above, two of the possible effects of introducing an FTT are that the value of the portfolios of financial assets will be lower and that there will be a fall in economic growth. Should these effects materialise, we can expect a reduction or lower growth in some tax revenues, in particular those levied on capital gains and consumer spending. As part of the studies accompanying the 2011 proposal for a directive, the European Commission made an estimate of the net revenues that would be obtained by introducing the tax, if it was adopted in the European Union as a whole, and concluded that the revenue would amount to 9.8 billion euros per year, the equivalent of 0.08% of the EU's GDP.³⁸ Therefore, bearing in mind that the tax revenue attributed to the FTT was estimated at 37 billion euros

35 T. Matheson (2011), *Taxing financial transactions: issues and evidence*, IMF working paper 11/54.

36 To reach this conclusion, the authors assume a debt turnover in the investor portfolio of one year, and three months for shares. They also assume that the debt/total assets ratio is 0.5 and that the percentage which is financed through the market is 30%.

37 These estimates result from applying a standard growth model with a Cobb-Douglas production function. The ratio between the cost of capital and production comes from N. Dwenger (2010), *User cost elasticity of capital revisited*, Max Planck Institute working paper.

38 For further details of the simulations performed by the EC, see Annex 16 of the impact assessment published by the European Commission for the Proposal for a Council Directive on a common system of financial transaction tax and amending Directive 2008/7/EC published in 2011.

per year, the estimated loss in revenue from other taxes would amount to a figure of close to 27.2 billion euros per year. Under the new proposal and given the extension of the persons liable to pay the tax by including the issuance principle, the net tax revenues are expected to be higher than those estimated in the original EC proposal for a directive, although still relatively low in GDP terms.

Finally, it should be pointed out that creating a new tax requires an increase in administrative costs in financial institutions through the creation and expansion of the administration, auditing and compliance departments. In addition to these compliance costs in strict terms, the costs which may be incurred by financial institutions to avoid payment of the tax should also be taken into account. It is particularly important to highlight the incentive towards an increase in financial engineering with the aim of creating new financial instruments with the sole objective of them not being subject to the tax.

6 Conclusions

Both in the initial proposal for a directive and, subsequently, in the proposal for enhanced cooperation presented by the European Commission for establishing an FTT at a European level, we can identify two main benefits associated with creating the tax. The first is to reduce the volume of short-term trading in secondary securities markets, which is considered excessive. In the opinion of the European Commission, this reduction could help to increase financial stability. The second main benefit is to increase the tax revenue of the Member States of the EU at a time of considerable difficulty in this area, largely as a result of the aid channelled towards the financial sector and the negative impact on the economy of the crisis triggered in said sector.

The aforementioned proposal also identifies different costs associated with the measure. The most important of these could be as follows:

- If the number of financial institutions falls as a result of the smaller size of the financial economy, this would lead to a loss of jobs and a possible increase in prices in the sector due to lower competition. At the same time, the number of financial institutions with residence in the EU may also fall due to the incentive to avoid tax payments. There might be incentives for displacement of at least the brokerage business to countries not included in the enhanced cooperation or to design derivatives outside the scope by means of institutions resident in other States.
- It could increase the costs of financing for companies which raise finance through securities markets by the increase in transaction costs being discounted in the secondary market.
- Tax revenues could fall from other taxes, such as capital gains taxes.

An analysis of the identified costs and benefits does not allow a clear conclusion as regards the net impact of the measure.

One of the arguments in favour of introducing the FTT is that it could help to reduce market volatility and, consequently, help towards financial stability. However, the empirical evidence provided by academic literature is not conclusive. Depending on the market analysed, we can find examples where volatility increases and others where it falls with the introduction of the measure or an increase in a similar existing tax.

The financial literature provides arguments which back the idea that introducing an FTT reduces the probability of bubbles in financial markets, an effect which is undoubtedly positive in terms of financial stability. However, recent experience in other markets, such as the real estate market, where transaction taxes are applied, suggests that the measure may also have limited effectiveness in this regard.

According to EC estimates, introduction of the tax for the European Union as a whole under the terms defined in the September 2011 proposal would lead to an increase in the tax revenues of Member States of 0.08% of EU GDP. The revenue from the FTT established through enhanced cooperation is expected to be a greater percentage of aggregate GDP of the countries implementing enhanced cooperation due to the introduction of the issuance principle as cause of the chargeable event. However, at any event, the percentage increase is not expected to be particularly significant. This relatively modest increase in tax revenues would help towards mitigating the public deficit suffered by several Member States since the start of the crisis. Although perhaps the most important benefit of the measure would be that it would be identified with a greater contribution from the financial sector to the public budget, in line with widespread social demand.

With regard to the costs, the original proposal for a directive estimates that introduction of the FTT would lead to a reduction of between 0.3% and 1.2% of GDP due to the fall in investment as a result of the increase in financing costs arising from implementation of the FTT. In addition, it is important to take into account the negative impact of lower efficiency in secondary securities markets resulting from the loss of trading volume.

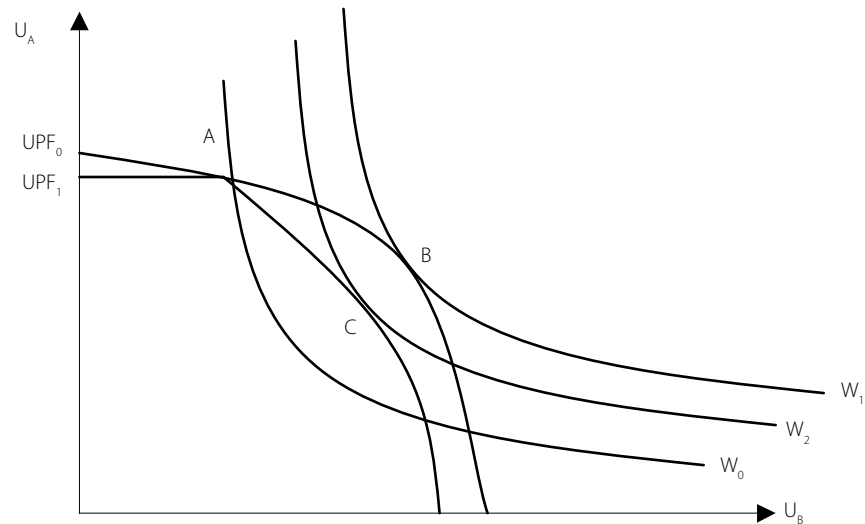
Accordingly, the introduction of the FTT may bring short-term benefits in terms of financial stability and a greater contribution from the financial sector to public finances. However, given the costs associated with its introduction, it might have been better for the Commission to have analysed in some depth the comparative advantages of this tax compared with other alternatives, such as establishing a financial activities tax, which, in line with the IMF proposal, would be levied on the profits and remuneration of financial institutions.

Annex I: On the redistributive effects of the FTT

The second theorem of welfare guarantees us that in perfectly competitive markets any efficient allocation between the different agents in an economy may be implemented providing appropriate transfers of income take place.³⁹ Figure 1 illustrates the potentially positive effect, in terms of social welfare, of a redistribution of income, in this case based on establishing an FTT.

Gain in social welfare from establishing an FTT

FIGURE 1



Source: CNMV.

In the figure, point A represents the allocation of utilities between these two individuals when there is no transfer of income between them. When income transfers are made between the individuals by means of taxes which are efficient, basically one individual transfers income to the other and the allocation of utility between both individuals will be located at point B. At this point, we can see how the social utility is clearly higher than when there is no income transfer, $W_0 < W_1$.

However, most income transfers are conducted through collecting taxes which introduce a distortion in the decisions taken by individuals, as is the case with the FTT, given that it is a tax on the quantities exchanged in a market. This means that introducing the tax in theory involves a restriction on the utilities which both individuals may reach on their own account due to the loss of economic efficiency inherent to the tax.⁴⁰

In the example illustrated in the figure, the distortion introduced by the tax is reflected in a displacement of the utility-possibility frontier UPF_0 to UPF_1 which

39 For a formal presentation of the Second theorem of Welfare, See Mas-Collel, M.D. Whinston and J.R. Green (1995), *Microeconomic Theory*, Oxford University Press.

40 This loss of efficiency is the result of the costs described in Section 5 of this article.

makes it impossible to reach point B.⁴¹ Even so, introduction of a tax makes it possible to displace the allocation of utilities from point A to point C, which represents a gain in social welfare ($W_0 < W_2$) compared with the initial situation. Therefore, even in this case, establishing an FTT could help to achieve a second best social optimum as it makes it possible to reach higher levels of welfare through taxation.

41 The Utility-Possibility Frontier represents the allocations of goods and services which are Pareto optimums.

Annex II: Calculations and hypotheses of the EC on the impact of the FTT

In order to estimate the gross tax revenue resulting from implementation of the FTT, the EC uses the following formula:

$$Revenue = Tax\ rate_{FTT} * Volume * Evasion * \left(1 + \frac{Tax\ rate_{FTT}}{Cost_{Transaction}}\right) Elasticity$$

where: $Tax\ rate_{FTT}$ is the FTT rate, $Volume$ is the volume of the financial asset before implementing the tax, $Evasion$ is the percentage of potential taxpayers expected to eventually pay the tax, $1 - rate_{EVIASION}$, $Cost_{Transaction}$ is the percentage of the transaction costs of the purchase/sale for the parties with regard to the price of the purchased asset. Finally, $Elasticity$ is a negative number which measures the percentage loss suffered by demand for an asset when the tax rate rises by 1%. Precisely because the elasticity is a negative number, the term $\left(1 + \frac{Tax\ rate_{FTT}}{Cost_{Transaction}}\right) Elasticity$ corrects downwards the potential tax revenue in order to take into account the fact that its introduction will generate lower demand for the taxed assets due to the higher transaction costs which would have to be paid by the parties involved in the trades.

In the calculations performed in the proposal for a directive, the EC considered: a ratio of tax evasion of 10% for shares and bonds and 90% for derivatives; elasticities of between 0 and 2, assuming in the baseline scenario an elasticity of 1 for spot markets and 1.5 for derivative markets; and a tax rate of between 0.01% and 0.1%.

In the case of bonds and shares, the EC considered losses in volumes in the range of 10-15%, and a reduction in derivatives trading from 70% to 90%. According to the EC calculations, an FTT applied to bonds and shares of 0.1% for each one of the two parties involved in the transactions, with a reduction in trading volumes of 15%, would lead to tax revenue of 13.6 billion euros for the EU as a whole. In the case of derivatives, assuming a fall in trading of 75%, tax revenue would amount to 23.4 billion euros. However, according to the methodology used by the EC, the revenue which could be provided by the FTT would be subject to great uncertainty, given that the estimates vary between 16 billion euros and 400 billion euros per year depending on the assumptions under which the calculation is made.

In the impact assessment which the EC performed for the enhanced cooperation proposal which it presented on 14 February, the EC estimated that including the issuance principal for determining the taxpayer liable for payment of the FTT would lead to a 10% reduction in the evasion rate in shares and bonds issued in the countries which implement the enhanced cooperation compared with the forecasts which accompanied the original proposal for a directive. According to the European Commission, introducing this new principal would mean that the eleven countries implementing the enhanced cooperation would raise additional tax revenue of 3.9 billion euros in the case of equity instruments and 8.3 billion euros in the case of fixed-income instruments.

All these estimates refer to the forecast for gross revenue resulting from implementing the FTT proposed by the EC. However, it is important to point out that imple-

menting the tax will also lead to the loss of tax revenue in other taxes, especially those levied on capital gains and consumer spending.

In the proposal for a directive, in order to make its forecasts on the impact that the FTT would have at a macroeconomic level and the net impact on tax revenues, the EC used a DSGE (Dynamic Stochastic General Equilibrium) model with the banking sector. In this model, it was assumed that the tax rate was 0.1% and that all the investment that was made was channelled exclusively through bonds and shares. The EC initially estimated that GDP would fall by between 0.5% and 1.8%. Subsequently, in December 2011, it revised these estimates and calculated that the loss in GDP terms would be between 0.3% and 1.2%. In the baseline scenario, the estimate for net tax revenue from the FTT was 0.08% of EU GDP.

Annual corporate governance report of listed companies in 2011

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1 Introduction

This article describes the main features of the corporate governance structures of listed companies in 2011. To this end, with the aim of detecting possible trends in the performance of the relevant variables, we have analysed the annual corporate governance reports (ACGR) from 2008 to 2011.

The article is structured into nine sections. The first three sections describe the ownership structure, the structure of the board of directors and the board committees, as well as the key aspects relating to the functioning of the board and its remuneration systems.

Sections 4 and 5 study the risk management policy and control systems which companies described in their ACGRs.

Sections 6 to 8 contain analyses of related-party transactions, conflicts of interest, general meetings and application of the “comply or explain” principle. The last section presents the final considerations.

2 Ownership structure

One of the key aspects which determine a company’s corporate governance is its ownership structure, as this determines the composition of its board, the board committees and the practices followed by both.

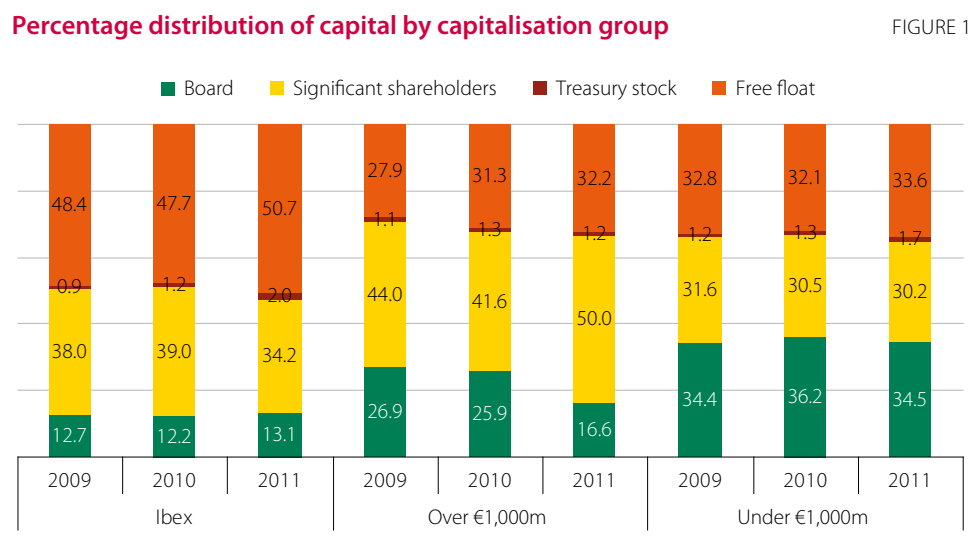
Accordingly, companies must identify in their ACGRs the shareholders which have a holding equal to or greater than 3% of the voting rights and those which, with a percentage below 3%, are able to propose or have proposed the appointment or removal of a member of the board of directors. This obligation is stricter in the case of directors, who must report any holding they own in the company’s capital.

According to data provided in the 2011 ACGRs, the aggregate share capital of Spanish listed companies¹ amounted to 42.65 billion euros, an increase of 5.2% on 2010. Stock market capitalisation fell by 10.2% compared with year-end 2010, following the trend of recent years.

1 The sample of companies analysed referred to in this report comprises 149 entities i.e. all the listed companies at 31 December 2011 registered in Spain and which, therefore, file ACGRs, except one company as it has an irregular financial year, and two companies because they have not filed their ACGRs. In 2010, the sample comprised 153 companies.

With regard to capital distribution, 32.5% of the share capital was held by non-director significant shareholders, 28.3% belonged to the board of directors, and 1.7% corresponded to treasury stock. Therefore, the free float amounted to 37.5%.

Figure 1 shows the capital distribution by stock market capitalisation groups.²



Source: Companies' ACGRs and CNMV.

The presence of non-director significant shareholders in listed companies has fallen by an average of 0.9 percentage points, and stands at 32.5%.

The free float rose by two percentage points on 2010. In 102 companies (68.5% of the total), the free float is higher than 25%, while it is lower than 5% in seven companies (4.7% of the total). The rest of the companies were concentrated in a range of free float of between 5% and 25%.

In 37 companies (24.8% of the total), there was a natural or legal person that held most of the voting rights or that exercised or could exercise control, compared with 43 companies in this situation in 2010 (28.1%).

The sum of significant shareholdings, including the share packages in the hands of the board, exceeded 50% of the share capital in 110 companies (73.8% of the total), of which 19 formed part of the Ibex 35.

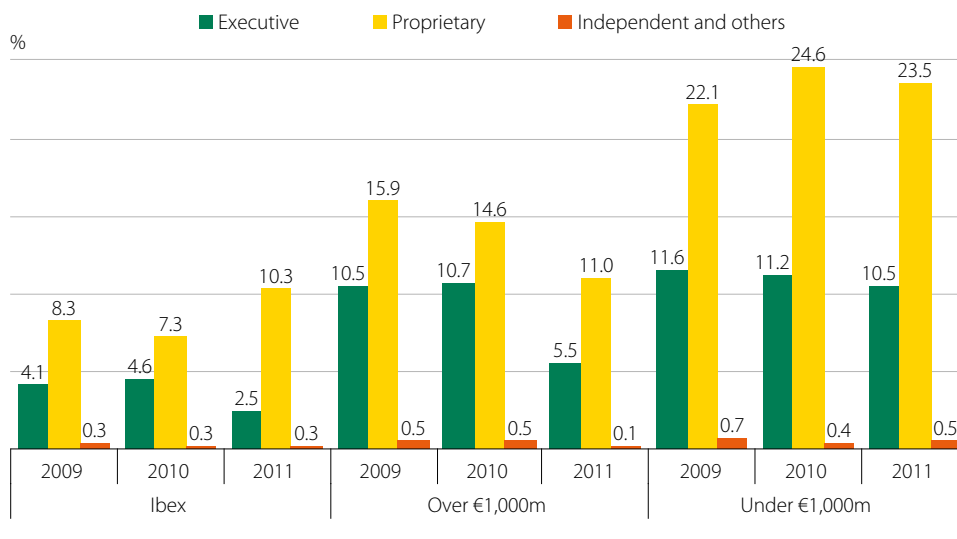
The 32.5% of the capital in the hands of non-director significant shareholders was spread as follows: 5.1% corresponded to natural persons resident in Spain, 21.1% corresponded to legal persons resident in Spain, and the remaining 6.3% corresponded to non-resident investors.

² The figures represent the arithmetic mean of the capital distribution of listed companies, taking the corresponding percentages for each company of the different categories included in the figure as the calculation base. The percentage representing non-director significant shareholders has been obtained after deducting the share packages in the hands of members of the board of directors.

Figure 2 shows in percentage terms the distribution of capital in the hands of the board according to the category of board members, grouping companies by stock market capitalisation.

Distribution of capital by director category

FIGURE 2



Source: Companies' ACGRs and CNMV.

75.7% of executive directors held an equity stake in the capital of the companies in which they worked. Eight of these exceeded 50%, while 25 declared shareholdings of between 10% and 50%.

3 Board of directors

3.1 Structure of the Board of directors

The figures relating to the size of the board and the categories of its members remained similar to those of previous years. The average size of the board of directors stood at 10.5 members (10.4 in 2010).

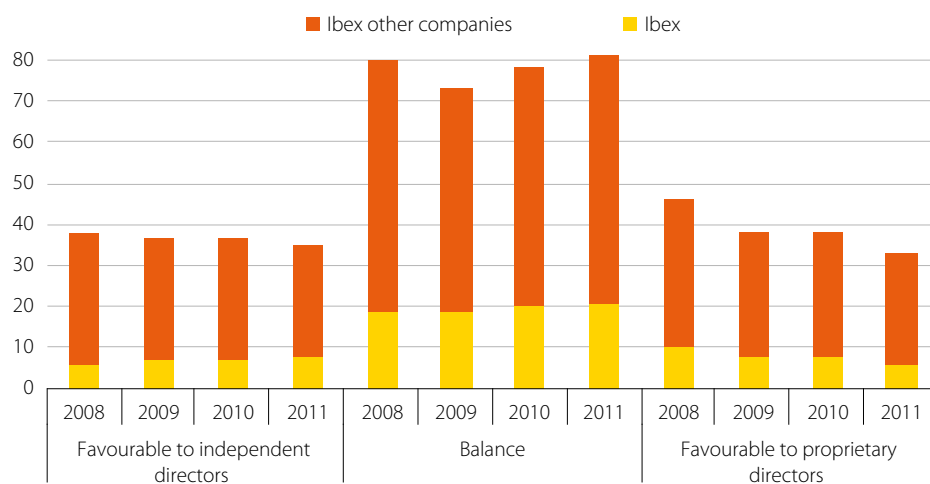
In 2011, 94% of listed companies had a majority of external directors. The proportion of executive directors has gradually fallen since 2008 in favour of independent directors, with changes of 1.9 and 2 percentage points respectively.

In 2011, despite the 1% increase in independent directors, on an aggregate level they remain well below the minimum of one third recommended by the Unified Code.

In this regard, the percentage of companies with a balance in the board or with a favourable proportion of independent directors continues to grow (increase of 5.9 percentage points over the last four years) in line with the recommendations of the Unified Code, as shown in the following figure:

Balance between proprietary and independent directors

FIGURE 3



Source: Companies' ACGRs and CNMV.

It should be highlighted that in 2011, only 4% of the directors who occupied the role of chairman of the board were independent directors (5.2% in 2010). However, the percentage of vice-chairmen who are independent directors has risen to 22.6% (20.6% in 2010).

The average length of time the members have served on the board remained the same (7.8 years), with executive directors having a longer tenure (10.8 years), followed by proprietary directors (7.4 years).

3.2 Gender diversity

The Unified Code considers that gender diversity is an efficiency objective which listed companies should work towards. It recommends that companies with few or no women on their boards should make a specific effort to find possible candidates whenever they need to cover a vacancy.

In this regard, the European Commission has launched a proposal for a directive of the European Parliament and of the Council³ on improving the gender balance among non-executive directors of listed companies, with the exception of small and medium-sized enterprises. To do this, it sets a minimum objective of a 40% presence of the underrepresented sex among the non-executive directors of listed companies by 2020.

In Spain, gender diversity is one of the aspects in which there is clear progress relating to board composition, although there remains plenty of room for improvement.

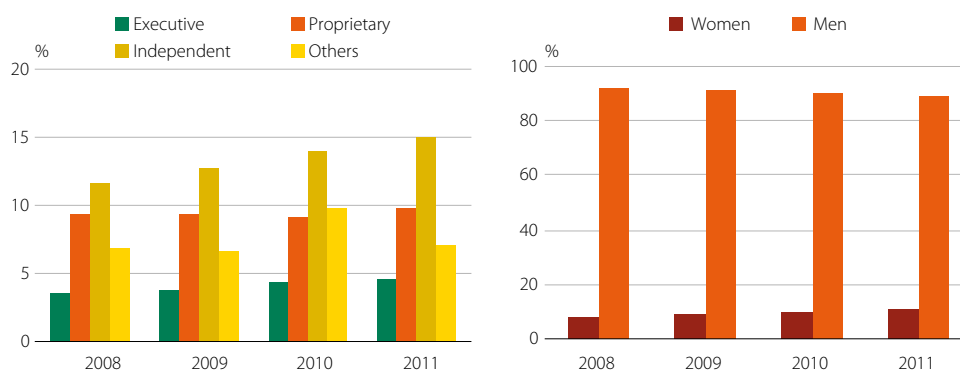
In 2011, 66.4% of listed companies had a woman present on the board, an increase of 2.3 percentage points on the previous year.

Figure 4 shows the presence of women on boards according to the director category.

³ http://ec.europa.eu/justice/gender-equality/files/womenonboards/directive_quotas_en.pdf

Percentage of women on boards

FIGURE 4



Source: Companies' ACGRs and CNMV.

In the period 2008-2011, the percentage of women on boards rose by 2.3 percentage points, reaching 10.4% in 2011. With regard to the director category over the period 2008-2011, there was a clear increase in the percentage of independent directors, from 11.7% in 2008 to 14.9% in 2011. In 2011, the positions occupied by women directors on the governance bodies were similar to the levels of the previous year, accounting for 11.7% of the audit committee and 10.8% of the appointments committee.

3.3 Functioning of the board

The Unified Code issues no opinion on separating the offices of chairman of the board and the chief executive officer. However, Recommendation 17 suggests that when the chairman is also the chief executive, an independent director should be empowered to request the calling of board meetings or the inclusion of new business on the agenda to coordinate and give voice to the concerns of external directors and to lead the board's evaluation of the chairman.

Over the last three years, the number of companies in which the chairman is also the chief executive has fallen by six percentage points (3.9 percentage points compared with 2010). 70.5% of these companies have implemented the checks and balances recommended by the Unified Code. This percentage of checks and balances increased by 6.5 percentage points on 2010.

In addition, over the last three years, the companies which have established a casting vote in the event of tied votes have increased by 4.1 percentage points, to 62.4%.

The number of companies appointing a vice-chairman has dropped by 14% over the last four years. In 2011, the percentage of independent vice-chairmen rose by 4.4 percentage points, while the percentage of executive vice-chairmen dropped by 2.9 percentage points. Vice-chairmen posts falling to propriety directors dropped below 50% for the first time.

The Unified Code issues no opinion as to whether the secretary should also be a board member, but recommends safeguarding his or her independence, impartiality and professionalism in the discharge of this function. The number of companies in which the board secretary is also a director has fallen, as shown in figure 5.



Source: Companies' ACGRs and CNMV.

The percentage of secretaries who are directors has fallen by 7.2 percentage points over the last four years to 21.5%. 44.8% of these are executive directors (36.4% in 2010), 27.6% are proprietary directors (30.3% in 2010), 17.2% are independent directors (18.2% in 2010) and 10.3% are other external directors (15.1% in 2010).

With regard to the number of board meetings, the Unified Code recommends that the Board should meet with the necessary frequency to properly perform its functions. In this regard, boards met on an average of 9.8 occasions, in line with the two previous years. However, it should be noted that the number of board meetings convened at companies with market capitalisation over 1 billion euros stood at 11, 19.4% up on 2010.

The Transparency Act requires all listed companies to draw up board regulations, with specific measures aimed at guaranteeing its effective stewardship. In 2011, 53.7% of companies amended their board regulations. Most of the amendments (61%) were the result of the latest regulatory changes in the Spanish Capital Companies Act, the Audit Act and the Securities Market Act. The main reason why companies reported amendments to their regulations in 2011 (72.5%) was related to the composition and functioning of the audit committee. Other amendments performed by over 30% of the companies which have adapted their regulations are related to the duties of the appointments and remuneration committee (32.5%) and with the functioning of the board of directors (35%).

3.4 Board committees

In 2011, the percentage of companies with board committees remained similar to the previous year, with a 2.4 percentage point increase in companies with an appointments and remuneration committee (from 86.9% in 2010 to 89.3% in 2011).

An executive committee is more common in companies with a high stock market capitalisation: 71.4% of Ibex companies compared with 28.8% of companies with a

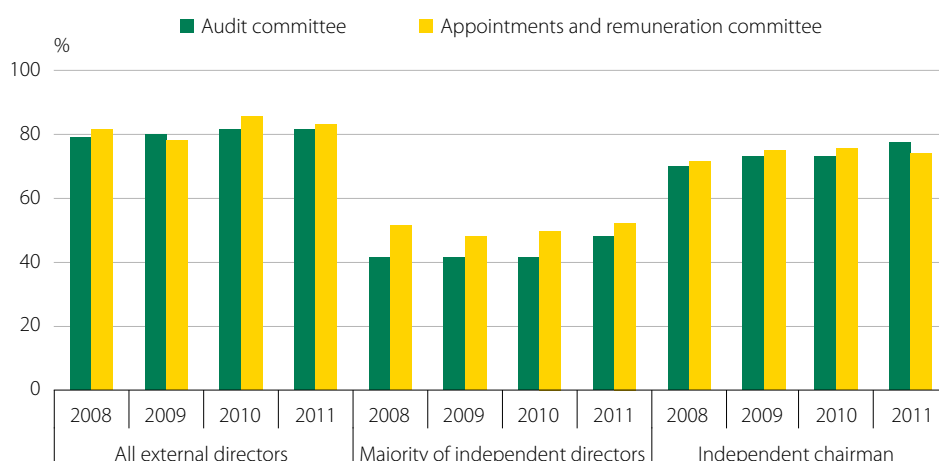
stock market capitalisation below 1 billion euros. The average number of members (5.8) of the executive committee remains in line with the previous year, but with a fall of 1.5 percentage points in the representation of executive directors. The percentage representation of executive directors, as in previous years, was higher than on the board, even though the Unified Good Governance Code recommends that the percentages of the different director categories should be similar on the executive committee and on the board so that their duties are exercised from the same perspective.

The appointments and remuneration committee (established in 89.3% of the companies) has an average size of 3.7 directors, while the audit committees, which are a mandatory requirement for all listed companies, are made up of an average of 3.6 members. The Unified Code recommends that these two committees should be exclusively made up of external directors and that they should be chaired by independent directors. For the appointments and remuneration committee, it recommends that the majority of its directors should be independent.

Figure 6 shows the composition of the audit committees and the appointments and remuneration committees.

Composition of the appointments and remuneration committee and the audit committee

FIGURE 6



Source: Companies' ACGRs and CNMV.

Most companies have followed the recommendations that their members should be external directors (81.6% on the audit committee and 83.5% on the appointments and remuneration committee) and that they should be chaired by independent directors (76.9% on the audit committee and 73.6% on the appointments and remuneration committee). Only 51.9% of the appointments and remuneration committees follow the recommendation that most of the directors should be independent.

4 Remunerations of the board and senior management

2011 was the first year in which public listed companies had to draw up an annual report on the remuneration of their directors. This report must include full, clear and understandable information on the company's remuneration policy approved by the board for the year in progress. It must also include, as the case may be, the planned remuneration for future years and an overall summary of how said policy was applied during the year, detailing the individual remuneration accrued by each one of the directors.

The annual report on directors' remuneration must be circulated and put to the advisory vote of the company's general meeting as a separate point on the agenda.

In the absence of a standard format, companies have drawn up their annual reports on directors' remuneration in accordance with the minimum contents prescribed by law, but without following the same format. A review of the 2011 reports submitted to 2012 general meetings permits the following conclusions:

- As there is no standardised format, the reports have uneven structures and it is difficult in some cases to extract all the information on the remuneration accrued by a director for all remuneration items.

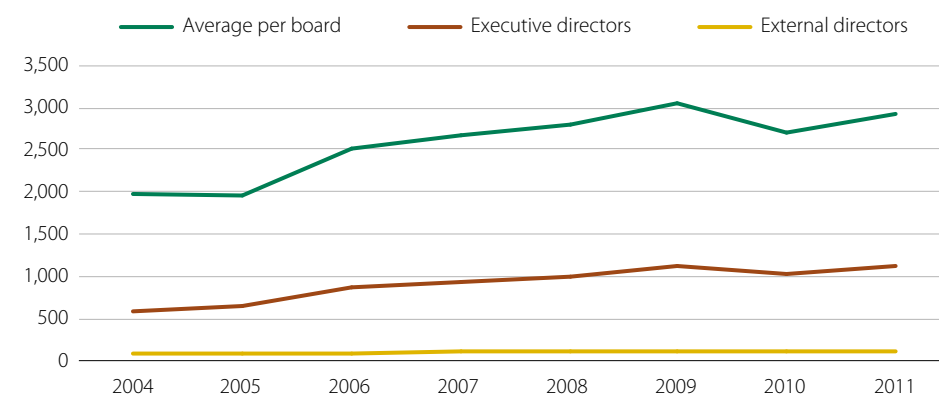
Reports are divided into chapters by remuneration item and quantify the payments received under each, but frequently omit to sum them together to arrive at the total amount. Furthermore, some companies offer a summary of what each director is paid in respect of their board responsibilities but omit the salaries and variable remuneration they receive in their capacity as senior officers.

- Others make no mention of the remuneration accruing to directors who left the board in the course of the year.
- In certain cases, reports failed to state the amounts paid to directors for serving on the governing bodies of subsidiary companies.

In addition to the requirement to prepare an annual report on directors' remuneration, companies must include in their ACGRs aggregate quantitative information on the remuneration accrued by the board of directors. Companies must break down certain remuneration items, such as fixed remuneration, variable remuneration, expenses, directors' fees, share-based compensation and other benefits. The ACGRs must also reflect the total aggregate remuneration by director category accrued in the company and its group.

With regard to senior management, the company must identify the members who were not at the same time executive directors and indicate the total remuneration accruing in their favour over the year.

Figure 7 tracks the average remuneration of listed companies' boards, executive directors and external directors for the period 2004-2011.



Source: Companies' ACGRs and CNMV.

Average remuneration per board in 2011 amounted to 2.9 million euros. Three companies reported one-off increases in director pay due to a rise in variable remuneration, and the payment of exit money to an outgoing director in respect of a post contractual non-competition clause.

Excluding these three companies, average board remuneration in comparable companies rose by 1.5%.

Including the effect of these three companies, average board pay rose by 7.8%. At the 145 companies filing ACGRs in 2010 and 2011, board remuneration rose by 6.1%

14.5% of listed companies reported a remuneration increase exceeding 20%. At 11%, the increase ranged from 10% to 20%, while a further 20.7% reported increases of below 10%. Conversely, 44.1% of listed firms reported lower board remuneration than in 2010. In 23 companies (15.9% of the total) this decline ran to over 20%. In 13 companies board remuneration fell by between 10% and 20%, and in 28 companies, remuneration fell by below 10%. Finally, 9.7% of companies reported no change in their levels of board remuneration.

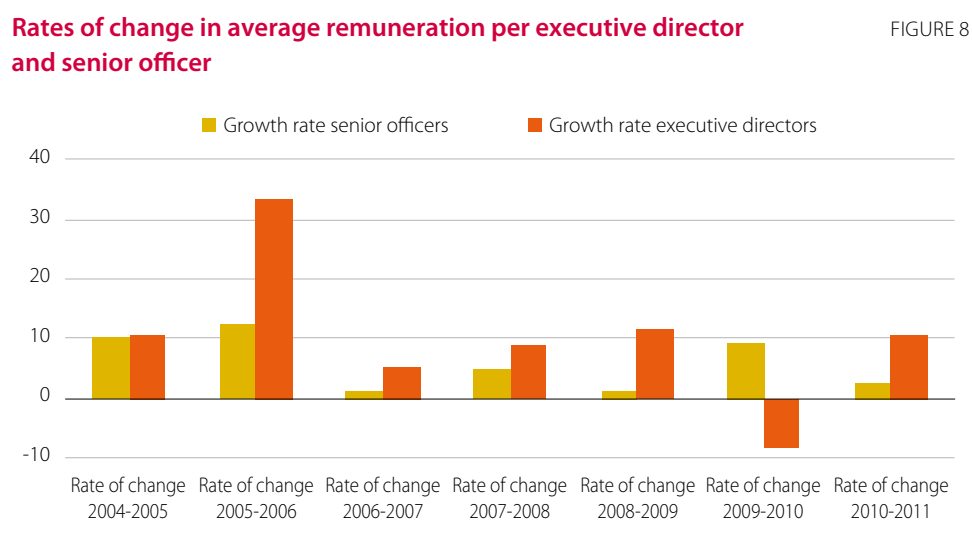
The average annual remuneration per director stood at 279,300 euros, an increase of 4% in comparable companies on 2010. Taking into account the effect of the three aforementioned companies, annual remuneration per director rose by 7.3%.

Average annual remuneration per executive director stood at 1.1 million euros, an increase of 1.8% in comparable companies on 2010. Taking into account the aforementioned three companies, average remuneration increased by 10.3%. At the 145 companies filing ACGRs in 2010 and 2011, average remuneration rose by 9%.

The average remuneration of external directors amounted to 109,686 euros, a year-on-year increase of 7%.

With regard to the different remuneration items, the variable component, excluding share-based compensation, gained ground in 2011 compared with 2010, while non-performance related pay (fixed remuneration, expenses and fees) fell by 2.3 percentage points.

Figure 8 shows the rate of change in the remuneration of senior officers and executive directors.



Source: Companies' ACGRs and CNMV.

Companies reported a total of 1,116 senior officers in 2011 ACGRs (1,164 in 2010). Their average remuneration stood at 466,678 euros, 2.6% more than the figure for 2010.

This increase was partly due to the increases in two companies which offset the fall of one company which reduced the remuneration of the senior officers from an average of 6.8 million euros in 2010 to 1 million euros in 2011.

5 Financial reporting and risk management systems

Risk management has proved to play a key role for many years, and particularly since the start of the financial crisis. Both the OECD, in its February 2010 report,⁴ and the European Commission, in its Green Paper on corporate governance published in April 2011⁵ have addressed the role of risk management. These publications established that the policy and appetite for risk should be set at the highest level within the company.

The Unified Code recommends that the board should present the annual accounts to the general shareholders' meeting without reservations or qualifications in the audit report. Should such reservations or qualifications exist, both the chairman of the audit committee and the auditors should give a clear account to shareholders of

4 *Corporate Governance and the Financial Crisis: Conclusions and good practices to enhance implementation of the principles*, February 2010.

5 The Green Paper on the EU Corporate Governance Framework, published in April 2011, contains a series of initiatives aimed at improving companies' corporate governance, particularly that of European listed companies.

their scope and content. The percentage of audit reports issued with a qualified opinion (excepting changes affecting inter-year comparability) of all the issuers of listed securities more than doubled from 0.9% in 2010 to 2.3% in 2011.

Listed companies must describe their risk management policy and control systems in their ACGRs. Consequently, the vast majority of companies reported on the existence of their risk management systems. However, not every company included a description of the content of those systems.

The main risks identified by companies were non-performing loans, funding constraints and the lack of liquidity in the financial system, commodity price volatility, the real estate downturn and regulatory and exchange-rate risks.

The number of companies reporting the materialisation of risks other than those inherent to their sector rose by 4.3 percentage points in 2011. At the same time, the number of companies which did not identify materialised risks fell by 2.6 percentage points in 2011 (a fall of 14.4 percentage points since 2008).

Act 12/2010, of 30 June, amended the Securities Market Act, enlarging the functions of the audit committee to include overseeing the effectiveness of the company's internal control and risk management systems. The Unified Code recommends that the audit committee regularly review the systems. In this regard, 2011 saw a continued progression in the percentage of companies charging the audit committees with supervision of risk control systems to 78.5% in 2011. This percentage has risen by a full 20 points since 2008.

The recommendations of the Unified Code on the functions of the audit committee are followed in almost all cases by at least 99% of companies. The establishment and supervision of a "whistle-blowing" mechanism is once again the least taken up of these recommendations (with 78.5%), although this figure rose by 8.6 percentage points on 2010. The other two recommendations relating to the functions of the audit committee are followed by less than 99% of companies. The first of these is to monitor the independence and effectiveness of the internal audit function, which is followed by 90% of companies. The second is to ensure that all group companies are audited by the same firm, which is followed by 93% of companies.

6 Internal risk control and management systems relating to the financial reporting process (ICFR)

The Sustainable Economy Act introduced a new Article 61 *bis* to the Securities Market Act,⁶ which extended the content of ACGRs, requiring a description of the main characteristics of the internal risk control and management systems relating to the financial reporting process. This new requirement entered into force for financial years starting on or after 1 January 2011.

6 See the article by A. Aguilar, F. Ibáñez and Á. Domínguez, "Modifications to the securities market as a result of the Sustainable Economy Act", in the CNMV's Quarterly Bulletin of the third quarter of 2011.

Most issuers of listed securities (except for 6%) have provided a more or less detailed outline of their ICFR in 2011 ACGRs, pursuant to the Securities Market Act. 71% followed the format proposed by the expert group⁷ or in the draft CNMV Circular.⁸ However, in some cases, the content was too general or, in the case of 12% of companies, plainly insufficient, as they did not describe specific internal controls on financial reporting (ICFR). Other companies reported that they were still in the process of documenting or rolling out the mechanisms.

Below is a summary of the most important aspects reported by companies with regard to the five components of the ICFR:

1. The entity's control environment for financial reporting: companies generally describe the existence of internal control mechanisms; 80% of the companies identified the board of directors as responsible for the existence and maintenance of ICFR, and over 85% identified the audit committee as responsible for its oversight.
2. Evaluation of financial reporting risks: around 87% of companies break down the characteristics of their processes for identifying financial reporting risks.
3. Control activities: 89% of companies describe the activities which they have implemented so as to mitigate risks of errors in financial reporting. However, they have not clearly identified the maximum authority level within the company responsible for reviewing the main estimates, measurements and forecasts.
4. Information and communication: around 91% of companies say channels are in place for communicating accounting policies to the teams preparing the financial statements, as well as mechanisms for the capture of supporting information.
5. Monitoring of system operation: in general companies have identified the audit committee as the body responsible for monitoring; 90% gave an account of the monitoring activities and most indicated that the internal audit function supported the committee in its monitoring role.

7 Related-party transactions and conflicts of interests

Listed companies are required to report in their ACGRs any transactions which they perform with significant shareholders, directors and senior officers, along with any intra-group transactions not eliminated in the consolidation process. This disclosure requirement is confined to related-party transactions of significant amounts or that are important for a correct understanding of financial statements.

7 In June 2010, the CNMV posted a document on its website prepared by an expert group setting out a series of recommendations on systems of internal control over financial reporting for listed companies.

8 Draft CNMV Circular to amend the ACGR form, sent out to public consultation on 26 October 2011, with a dedicated section for ICFR disclosures.

Furthermore, Article 229 of the Spanish Capital Companies Act requires directors to inform the board of any situation of conflict, whether direct or indirect, between their own and the company's interest and to refrain from taking part in the relevant resolutions or decisions.

The aggregate amount of related-party transactions performed in 2011 with significant shareholders stood at 65.35 billion euros. 75.2% of this amount corresponded to transactions reported by five companies.

60.4% of the aggregate total corresponded to loans, guarantees or sureties from banks or savings banks holding significant interests in listed companies. In 2011, the aggregate amount of loans granted fell by 32% on 2010, while guarantees and sureties required increased by 38%.

15.3% of the transactions conducted with shareholders corresponded to sales and purchases of goods, a further 15.1% corresponded to dividends paid during the year and the rest corresponded to other normal business operations.

A total of 50 companies reported related-party transactions with directors and senior officers totalling 1.15 billion euros. Transactions at two firms alone accounted for 62.2% of the aggregate amount at the companies analysed.

The amount of transactions with directors and senior officers was down by 72% with respect to the previous year. This was mainly the result of one company, whose transactions accounted for 47.8% of the aggregate total in 2010, reporting no transactions in 2011.

Listed companies have to report in their ACGRs all material transactions with group companies that are not eliminated in the consolidation process, alongside those concluded with associates, whenever such transactions are outside normal trading and financial flows.

The aggregate amount of these transactions, declared in 2011 by 19 listed companies (21 in 2010), totalled 37.44 billion euros (4.95 billion euros in 2010).

This increase was due to the fact that 94.2% of the total volume had been reported by one company as the result of it taking over the banking business of another entity belonging to the same group.

A total of 28 companies reported some conflict of interest in 2011, involving 135 directors.

The nature of the director conflicts reported in 2011 was essentially unchanged with respect to previous years. Companies highlighted the following conflicts:

- Approval of directors' contractual and/or pay conditions.
- Approval of major transactions involving the transfer of funds or the recognition of obligations between the company and director related parties.

- Director classification in accordance with the definitions of the Unified Code.
- Appointment of the director as a member of board committees.

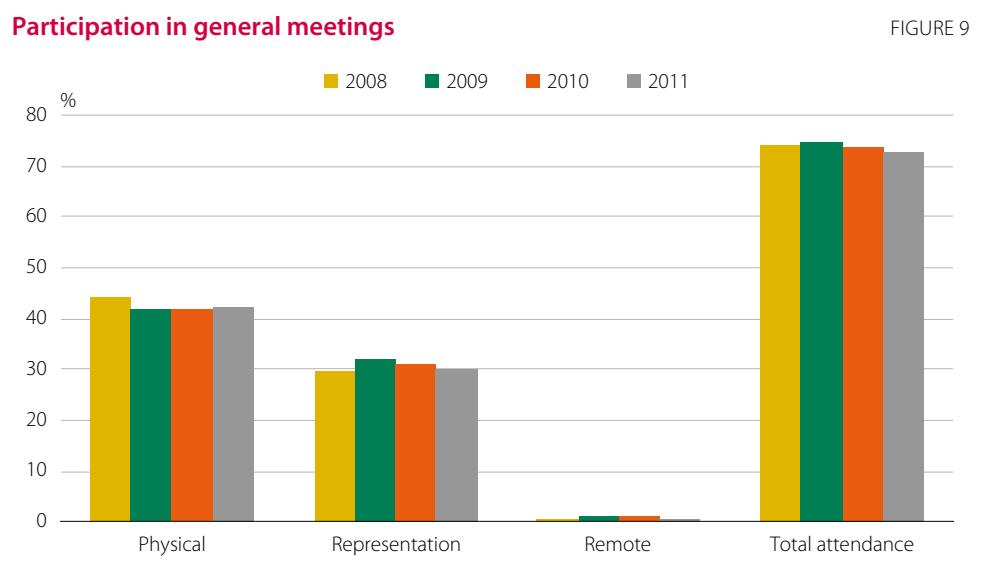
8 General Shareholders' Meeting

One area of corporate governance where international organisations such as the OECD and the European Commission have been calling most strongly for improvement since the start of the crisis is the involvement of shareholders in general, and institutional investors in particular, in the governance of listed companies.

Over recent years in Spain, companies have adopted measures to facilitate shareholder participation in general meetings. Furthermore, the reform of the Spanish Capital Companies Act has introduced significant new aspects in order to bring about this goal. Among other measures, public listed companies must have a website where they publish all the documentation relating to the organisation and conduct of general meetings sufficiently in advance, as well as the resolutions adopted. The website must include an electronic shareholders' forum to facilitate shareholder communication in the lead-up to the meeting. Through this forum, shareholders can propose motions to be tabled, give support for such motions, or try to mobilise a sufficient percentage of votes to exercise a minority right.

The Unified Code also devotes a chapter to the general meeting, including recommendations on the powers of the meeting, advance information on proposals, separate voting on separate items and the possibility of split votes.

Figure 9 shows the average participation of the shareholders of listed companies in the general meetings held between 2008 and 2011. It also differentiates between the different types of attendance at the meetings: physical presence, through representation and by remote voting.



Source: Companies' ACGRs and CNMV.

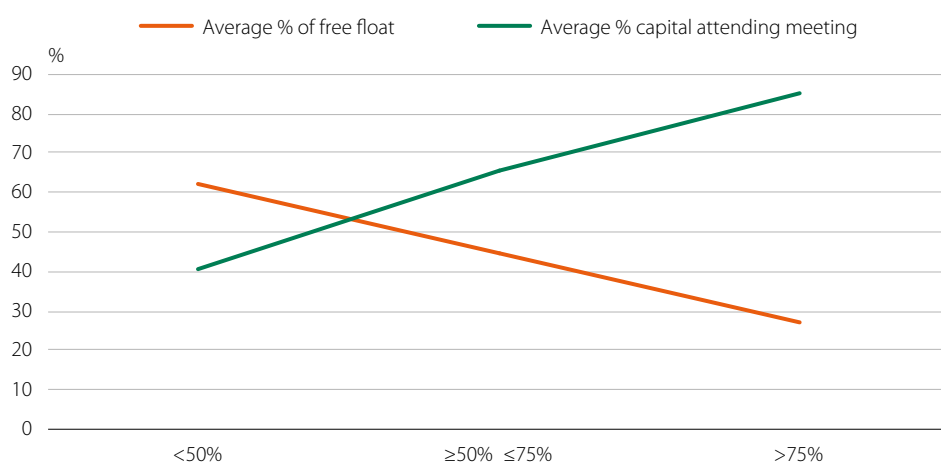
Average shareholder attendance at general meetings stood at 73% of the share capital, a fall of 0.9 percentage points on the previous year. In terms of the type of participation, physical attendance was the only one to register an increase, rising from 41.8% in 2010 to 42.3% in 2011, breaking the downward trend prevailing since 2008.

In 13 companies, the physical attendance of shareholders at the meeting exceeded 90% of the capital. In 5 of these companies, the percentage of physical attendance stood at 100%. In these companies, the general shareholders' meetings reported in the ACGRs were held in 2011 prior to the companies' stock market launches.

Figure 10 shows the average figures in 2011 for attendance and the free float for each one of the brackets analysed as regards attendance at general meetings.

General meeting attendance vs. free float

FIGURE 10



Source: Companies' ACGRs and CNMV.

Over recent years, companies have adopted measures to encourage minority shareholders to participate in general meetings. However, as shown in the above figure, the existence of a greater percentage of minority shareholders leads to lower participation in the meetings, which increases as the average free float falls.

9 "Comply or explain" principle

Under the "comply or explain" principle, companies must state their degree of compliance with the Code's 58 recommendations - indicating whether they comply with them fully, partially or not at all - giving reasons, as the case may be, for any practices or criteria departing from the recommendations.

On an aggregate level, the declarations included in the 2011 ACGRs on the level to which they have followed the Unified Code recommendations demonstrated, among others, the following aspects:

- Listed companies comply on average with 81.3% of the Code's recommendations (78.1% in 2010) and partially with a further 7.6% (8.9% in 2010). There-

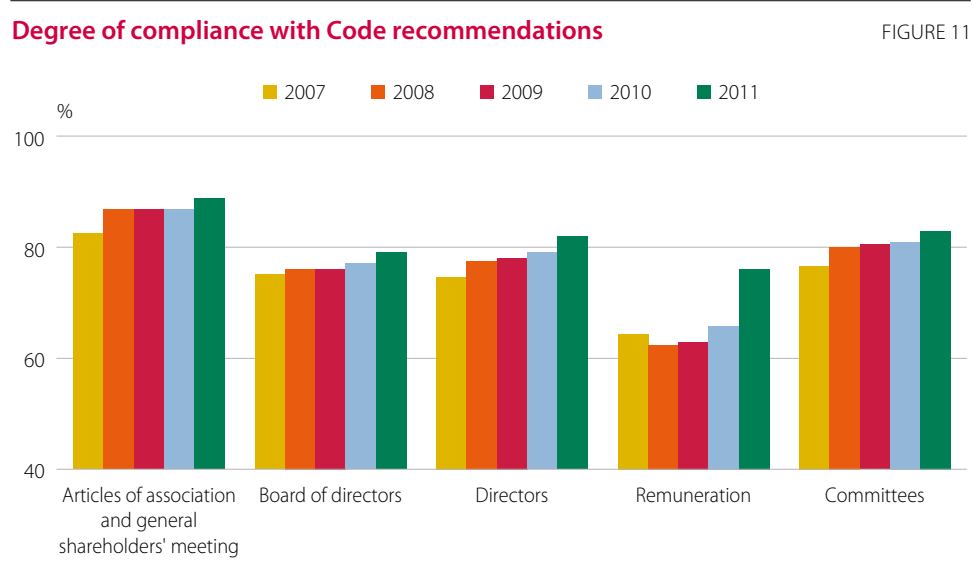
fore, on an aggregate level they do not follow, even partially, 11.1% of the recommendations.

This increase is largely a consequence of the implementation in Spanish law of recommendation 40 (that the board submit a report on directors' remuneration policy to the general meeting) and Recommendation 41 (that the notes to the annual accounts should detail individual compensation).

- 46 companies (30.9% of the total) follow over 90% of Unified Code recommendations, with four reporting that they are 100% compliant. Conversely, 5.4% of listed companies report a degree of compliance with the recommendations below 50%.
- All listed companies reported compliance with Code Recommendation 53 (the board of directors should seek to present accounts to the general meeting without auditor reservations or qualifications).
- On average, 7.6% of Unified Code recommendations are partially complied with. The recommendations with the highest level of partial compliance were: Recommendation 26 (time and effort devoted by directors) and Recommendation 42 (composition of the executive committee), which were followed partially by 43.6% and 40.3% of companies respectively.

Both of these recommendations include several good governance practices demanding different levels of effort. This may explain why partial compliance is so high.

Figure 11 includes the total average level of compliance of listed companies with the recommendations of the Unified Code, grouped by category, between 2007 and 2011:



Source: Companies' ACGRs and CNMV.

The level of compliance with Code recommendations rose from 78.1% in 2010 to 81.3% in 2011. The most significant increase was seen in the recommendations re-

lating to approval and transparency of directors' remuneration, up from 65.3% in 2010 to 76% 2011.

Excluding the Code recommendations that have since become legally enforceable, the one where the advance in compliance was most marked was Recommendation 11 - if an external director is deemed neither proprietary nor independent, the company should disclose and explain this circumstance - which was adhered to in full by 73.3% in 2010 and 85.5% in 2011.

The recommendation whose compliance fell most sharply was number 42, referring to the mix of directors on the executive committee. In 2011, 29 firms declared themselves fully compliant with this recommendation compared with 31 in 2010.

62.1% of listed companies reported higher compliance with the Unified Code than in the previous year.

Since 2008, the CNMV has published the results of analysis of a sample of the explanations offered by Spanish listed companies in their ACGRs.

For the 2011 ACGRs, an analysis was conducted of a sample of 530 explanations (33% of the total) on the 10 Unified Code recommendations with the lowest compliance scores. Except in the ACGRs of Ibex companies, no significant improvement was noted as regards the quality of the information offered by companies to explain the reasons why they deviate from the recommendations.

A large part of the information analysed is considered to be excessively generic or redundant, which has led the CNMV to send notices with recommendations on how to improve the quality of the explanations included in the ACGRs.

With regard to these results, it should be pointed out that following the annual review process of the ACGRs, the CNMV sent 12 notices to the same number of companies about the sub-optimal quality of their explanations for non-compliance with Unified Code recommendations. Most of these notices included individualised guidelines as to how they could improve explanations in future years.

10 Conclusions

In line with the trend of recent years, the level of compliance with the recommendations of the Unified Code reported by listed companies in their ACGRs increased once again in 2011, up to 81.3%.

62.1% of companies reported a higher level of compliance with the Unified Code in 2011 than in 2010. This improvement was mainly focused on the recommendations relating to directors' remuneration, part of which were incorporated into Spanish law through the Sustainable Economy Act.

There was no significant improvement, except in the ACGRs of Ibex companies, with regard to the quality of the information offered by companies to explain the reasons why they deviate from said recommendations.

A large part of the information analysed is considered to be excessively generic or redundant, which has led the CNMV to send notices with recommendations on how to improve the quality of the explanations included in the ACGRs.

The free float rose by almost 2 percentage points to 37.5% (35.6% in 2010), which has been directly reflected in the composition of the boards, with a 1% increase in the presence of independent directors. This follows the trend seen over the last four years of an increase in companies with a balanced board or with a favourable proportion of independent directors.

Companies continue to improve, albeit slowly, the gender diversity of their boards, with an increase of 2.3 percentage points in the presence of women on the boards over the last four years. This issue will be the focus of a great deal of attention over the coming years if the proposals for improvements in gender diversity contained in the proposal for a directive of the European Parliament and of the Council formulated by the European Commission materialise.

Another significant change, with regard to the board, is the reduction of 3.9 percentage points in the number of companies in which the chairman is also the chief executive, while at the same time the proportion of independent vice-chairmen has increased by 4.4 percentage points.

Another important new aspect which affects transparency requirements is the requirement to disseminate and submit an annual report on director remuneration to an advisory vote in the general meeting.

Due to the lack of implementing legislation as regards the Sustainable Economy Act, the reports presented to the 2012 general shareholders' meetings respect the minimum contents established by law, but they are not standardised as there is still no official standard format. In some cases, it is complicated to extract the full amount of the remuneration accrued by a director for all the remuneration items. In addition, some companies have not included the remuneration accrued by directors which left their office during 2011.

Average remuneration per board in 2011 amounted to 2.9 million euros. This represents a 1.5% increase with regard to the average in 2010 if we exclude the one-off increase recorded in the boards of three companies. Including these three companies, the increase in average remuneration totalled 7.8% compared with 2010.

III Regulatory novelties

Financial advisory firms in Spain

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1 Introduction

The transposition of the Directive on Markets in Financial Instruments (MiFID)¹ to Spanish law has led to a significant modification as regards the provision of investment services and ancillary services, organisational requirements and conduct of business rules required of those who provide these services. The key changes introduced include the extension of the catalogue of investment services covered by legislation to include investment advice, which had previously been considered as a supplementary ancillary service. Both this change and the set of amendments introduced in the law aim to enhance investor protection in a context marked by greater sophistication and complexity of financial instruments.

Letter g) of Section 1 of Article 63 of the Securities Market Act 24/1988, of 28 July, establishes that investment advice is an investment service and defines it as “the provision of personal recommendations to a client, either upon its request or at the initiative of the investment firm, in respect of one or more transactions relating to financial instruments”. Generic, non-personalised recommendations which may be made in the context of marketing securities or financial instruments shall not be considered as advice for the purposes of this legislation. These recommendations will be classified as commercial communications.

Although this article does not aim to analyse the difficulties surrounding the concept of investment advice, a brief mention must be made of the fact that it has not been easy to establish a definition and the limits to its scope since the MiFID classified it as an investment service. Various interpretive documents have been published on this issue which outline criteria and guidelines for understanding and differentiating investment advice from the simple marketing of a financial instrument as a stage prior to provision of the service of reception, transmission or execution of orders.^{2, 3}

Following the guidelines included in those documents and in Spanish legislation implementing the aforementioned Article 63 of the Securities Market Act, on 23 Decem-

1 Directive 2004/39/EC of the European Parliament and of the Council, of 21 April 2004, on markets in financial instruments, transposed to Spanish law by Act 47/2007, of 19 December, which amends the Securities Market Act 24/1988, of 28 July.

2 Number 4 of Article 63 of the Securities Market Act indicates that marketing investment services and acquiring clients are not in themselves investment services, but activities prior to each one of the investment services listed in the preceding sections which may be performed separately from the provision of the service itself.

3 See the documents issued at the time by the Committee of European Securities Regulators (CESR): *CESR's Technical Advice on Possible Implementing Measures of Directive 2004/39 EC on Markets in Financial Instruments* (ref.: CESR/05-290b, 29/4/2005); *Consultation Paper - Understanding the definition of advice under MiFID* (ref.: CESR/09-665, 14/10/2009); *Question & Answers - Understanding the definition of advice under MiFID* (ref.: CESR/10-293, 19/4/2010); *Feedback Statement - Understanding the definition of advice under MiFID* (ref.: CESR/10/294, 19/4/2010).

ber 2010, the CNMV published a *Guía sobre la prestación del servicio de asesoramiento en materia de inversión* [‘Guide on the provision of investment advice’], in which it concludes that an entity is providing investment advice when it simultaneously meets two conditions: i) that there is a recommendation on specific financial instruments, whether explicit or implicit, and ii) that the recommendation is personalised i.e. that it is presented as suitable for the investor based on his/her personal circumstances.⁴

In summary, the transposition of the MiFID to Spanish law has involved recognising and classifying investment advice as an investment service subject to compliance with the general obligations applicable to any other investment service and supervised by the CNMV. Therefore, pursuant to the Securities Market Act, investment advice can only be provided by entities which are expressly authorised to perform activities related to securities markets and which must comply with certain prudential requirements and other organisational requirements and conduct of business rules. The Securities Market Act reserves this activity for credit institutions, collective investment scheme management companies, broker-dealers and brokers, portfolio management companies and a new type of entity specialised in this service: financial advisory firms (Spanish acronym: EAFI), providing their legal regime, articles of association and specific authorisation enable them to provide the service.

This article focuses on EAFIs with the aim of presenting their main features, describing their recent development and reflecting on some issues which are of interest for this activity, particularly on the potential impact of the MiFID reform which is currently in process on the sector. Section 2 describes the regulation affecting these firms. Section 3 addresses the recent evolution of their main indicators in terms of activity and economic/financial position. Section 4 analyses the impact on EAFIs of the possible ban on incentives from third parties through the reform of the MiFID. Finally, the article closes with a section of conclusions.

2 Financial advisory firms (EAFIs)

Advisory services have been freely provided in Spain for many years. Any person or entity could perform this activity, irrespective of their professional experience, their knowledge and their solvency. However, with the regulatory classification of advice as an investment service, with the intention that the service be provided in a more transparent manner and that the investment recommendations match the client profile, investment advice may now only be given by authorised entities subject to compliance with very strict requirements and controls. It should be pointed out that although the MiFID was transposed in December 2007, it was not until 2009 that both companies and natural persons, which had been regularly and professionally providing investment advice, were required to request mandatory authorisation from the CNMV.⁵

Act 47/2007, of 19 December, which transposed the MiFID Directive to the Securities Market Act at the same time as classifying investment advice as a principal investment

⁴ This guide is available at http://www.cnmv.es/DocPortal/GUIAS_Perfil/GuiaAsesoramientoInversion.pdf

⁵ See the First Transitory Provision of Royal Decree 217/2008, of 15 February, on the legal regime of investment firms and other institutions which provide investment services.

service, created a new type of investment firm with the title *empresa de asesoramiento financiero* [‘financial advisory firm’]. The requirements to access and perform this activity are regulated in Title V of the Securities Market Act, in Chapter III of Title I of Royal Decree 217/2008, of 15 February, on the legal regime of investment firms and other institutions which provide investment services and in CNMV Circular 10/2008 on EAFIs.

Number 5 of Article 64 of the Securities Market Act defines EAFIs as those natural or legal persons which may exclusively provide investment advice, advice to companies and preparation of reports and financial analyses.

In order to carry on their activity, they must obtain mandatory administrative authorisation from the CNMV⁶ and be included in the corresponding register. They may not perform transactions on their own account or for third parties unless, and subject to possible regulatory limitations, the transactions are aimed at administering their own assets, and they are not authorised to hold client funds or securities. Under no circumstances will their activities be covered by the Investment Guarantee Fund. Furthermore, EAFIs may not act as agents of another investment firm or credit institution and they may not hire agents.⁷

The activity for which EAFIs are subject to authorisation⁸ is that of making personalised recommendations, either on a one-off or recurring basis, to their clients. To do this, they must meet certain financial and operating requirements which generally relate to meeting organisational and internal control requirements.⁹ In performing their activity, the professionals are required to have suitable knowledge and experience in the securities market and their actions must meet the conduct of business rules provided in the pertinent legislation. Furthermore, EAFIs must have a customer service department for addressing the complaints and claims filed by their clients and they are subject to legislation on the prevention of money-laundering.

Among others, the requirements related to the obligation to have a compliance function, the obligation to assess suitability in providing the investment advice and to establish the necessary mechanisms and forecasts to avoid the conflicts of interest which may arise in their activity, are particularly significant.

EAFIs are responsible for maintaining an appropriate and proportional organisational structure with a compliance function, which may be outsourced, that must verify compliance with certain policies and procedures within the organisation. These policies and procedures are related, *inter alia*, with the Internal Conduct Regulation, staff professionalism, conflict-of-interest management and the conduct of business rules applicable to the firms, and also the requirement to keep the registers required by legislation.¹⁰

6 The obligation to register individually with the regulatory body is not a generalised practice in other countries. In some countries, it is the professional colleges or associations which must be registered and the regulatory body empowers them to oversee financial advisers.

7 Pursuant to Article 65.1 of the Securities Market Act, agents may provide advisory services on the financial instruments and the investment services of the company which they represent.

8 Article 73 of the Securities Market Act provides different reasons for revoking the authorisation, which include delays in starting to provide the investment advice service.

9 See Section 2 of Chapter III of Royal Decree 217/2008, of 15 February.

10 The CNMV is currently drawing up a Circular which will regulate the internal organisational requirements of the control functions for investment firms as a whole.

Providing investment advice requires preparation of a suitability test to collect all the information necessary on the clients' knowledge and experience, on their financial situation and on their investment goals, so as to be able to offer them the financial products and services which are most appropriate for them.¹¹ EAFIs, like the other entities authorised to offer this service, must provide investment advice in the best interest of the client. This requires transparency i.e. the client must be suitably informed and the recommendations must be personalised or individualised (the recommended product must meet the client's risk profile in accordance with the result of the suitability assessment). The recommendations must also be specific (they must be made on specific financial products) and understandable for the client. It must always be explained in writing how the recommendation made meets the client's characteristics and objectives.¹²

In performing their activity, EAFIs may receive certain incentives or commissions from third parties providing that this does not undermine their obligation to act with due diligence in the interest of the client and providing they previously inform the client of this situation. These incentives or commissions must be managed appropriately so as to prevent the appearance of conflicts of interest which may affect the independence of their actions. With regard to these incentives, Section 4 of this article analyses in more detail retrocessions and the consequences of any possible limitation, as provided in the proposal for reform of the MiFID currently under discussion.

The law requires that EAFIs publish their prospectuses on maximum fees¹³ and that they should post them on their corresponding websites in an easily accessible place, irrespective of whether they choose another media channel for their publication. They may set an annual minimum and the commissions may be established depending on the amount of the assets under advice, their increase in value over a particular period or by both criteria. They may also apply a fee for the time spent analysing the portfolio.

In addition to the aforementioned organisational requirements and conduct of business rules, EAFIs are subject to prudential obligations whereby they must meet certain financial requirements in order to guarantee their solvency.¹⁴ Legal persons registered as EAFIs are considered public interest entities pursuant to Royal Decree 1517/2011,¹⁵ with the aim of improving their functioning and allowing auditors to

11 The treatment of the suitability test will be different depending on the classification of clients as retail clients or professional clients.

12 This obligation, which appears among the proposals for the reform of the MiFID that are currently under discussion in the European institutions, is already included in Article 79 *bis* of the Securities Market Act. It is expected to be implemented by means of a CNMV Circular.

13 CNMV Circular 7/2012, of 12 December, on the fees prospectus and the content of standard agreements, establishes the concepts, methods for calculation and the basis on which commissions may be charged for providing investment advice.

14 Article 22 of Royal Decree 217/2008, of 15 February, requires that legal persons registered as EAFIs have an initial capital of 50,000 euros, or a civil liability insurance, or a guarantee, with total coverage of 1,500,000 euros per year for all the claims, or a combination of both mechanisms which provides similar cover. Natural persons registered as EAFIs must take out an insurance policy with the aforementioned characteristics.

15 Royal Decree 1517/2011, of 31 October, which approves the Regulation implementing the consolidated text of the Account Auditing Act, approved by Legislative Royal Decree 1/2011, of 1 July.

collaborate with the CNMV in supervising these entities. They are obliged to submit their annual accounts to an audit and to send this audit together with the annual accounts and corresponding management report to the CNMV. For their part, natural persons registered as EAFIs are required to send an annual report to the CNMV. This report must be prepared by an independent expert who shall issue his/her opinion on the accuracy and reliability of certain information relating to their activities.¹⁶

Finally, it should be pointed out that in exercising their activities, EAFIs are subject to supervision, inspection and penalties by the CNMV.

3 Recent developments in the sector's activity, revenue and results

This section presents some basic figures on the development of the sector over 2011 and 2012, which are summarised in table 1. The aggregate information shown has been obtained from the half-yearly information which EAFIs submit to the CNMV on their activity and financial position and information on the conduct of business rules which they submit annually to the supervisory body, as well as the annual accounts and, in the case of legal persons, the audit report. The indicators selected, which are summarised in table 1, are the number of firms, the number of clients and the assets under financial investment advice, the revenue and results. The table also includes some aggregate figures on the features of the recommendations made by these firms to their clients in providing investment advice.

Development of EAFIs in 2011 and 2012

TABLE 1

Thousand euros	December 2011	Change on dec. 2010 (%)	December 2012	Change on dec. 2011 (%)
No. of firms	82	57.7	101	23.2
Legal persons	60	50.0	75	25.0
Natural persons	22	83.3	26	18.2
No. of clients receiving financial advice	3,677	51.3	3,468	-5.7
Retail clients (%)	96.3	51.0 ¹	94.1	-7.8
Assets under advice	16,033,109	1.5	14,708,739	-8.3
Retail clients (%)	13.6	27.2 ²	21.8	46.7
Revenue	31,052	49.7	25,347	-18.4
Commissions for financial advice	22,469	48.8	18,573	-17.3
Retrocessions	4,724	35.3	4,631	-2.0
Other revenue	3,860	79.6	2,141	-44.5
Profit (loss) after tax	7,474	9.9	3,550	-52.5

Source: CNMV.

1 Change in number of retail clients.

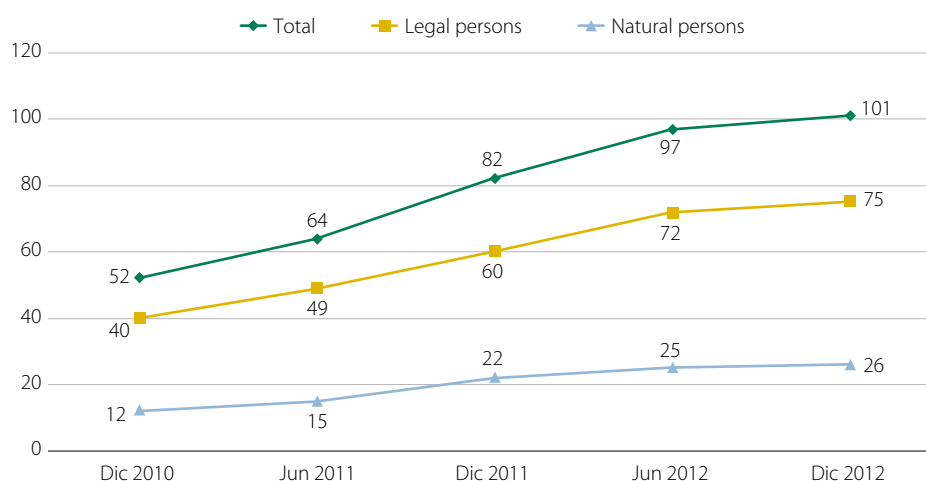
2 Change in assets under advice for retail clients.

16 The scope of the work of the expert is determined in the First Additional Provision of CNMV Circular 1/2011, of 21 January, on the Securities Market, which amends the CNMV Circular of 30 December on the solvency of investment firms and their consolidatable groups.

As shown in figure 1, the number of EAFIs registered with the CNMV grew sharply in 2011 and in the first half of 2012.¹⁷ In the second half of last year, the number grew at a more moderate rate to a total of 101 firms at the end of the year, of which 75 were legal persons and the rest natural persons.

Number of EAFIs

FIGURE 1



Source: CNMV.

In 2011, the assets under advice rose by 3.2% on 2010, while the number of clients grew by 51.3%. The figures for 2012 reveal a drop in both numbers, of 8.3% and 5.7% compared with the previous year, although the fall was largely concentrated in two firms. The firms established legally as companies accounted for around 90% of the assets under advice at year-end 2012. One single firm accounted for 60% of the total. As shown in table 1, on that date the assets under advice of EAFIs essentially corresponded to institutional clients (78%), although in terms of numbers, the bulk of clients were retail clients (94%).

The provision of investment advice is heavily concentrated in Spanish banks. In December 2011, the last date for which data is available, Spanish banks accounted for 95% of the total number of clients, as shown in table 2. For their part, EAFIs on that date held a very low share of the total, around 1%, although they accounted for around 24% of the clients of investment firms in this service. The retail profile is heavily dominant among clients of this type of firm, although we can see a significantly higher number of institutional or professional investors, in relative terms, in EAFIs.

In performing their activity, EAFIs issued 60,971 purchase recommendations and 43,364 sales recommendations in 2012, relating to assets with a total market value of 7,000 million and 9,000 million euros respectively. 84% of the purchase recommendations and 60% of the sales recommendations related to units or shares issued by collective investment schemes, followed by recommendations on shares at a much lower percentage (9%). The number of purchase recommendations on high-

¹⁷ The EAFIs register was started in 2009. At the end of that year, a total of 16 firms were registered, two of which were natural persons.

risk products such as warrants, contracts for differences and other structured products was low and generally aimed at professional clients.

Number of clients regarding investment advice

TABLE 2

December 2011

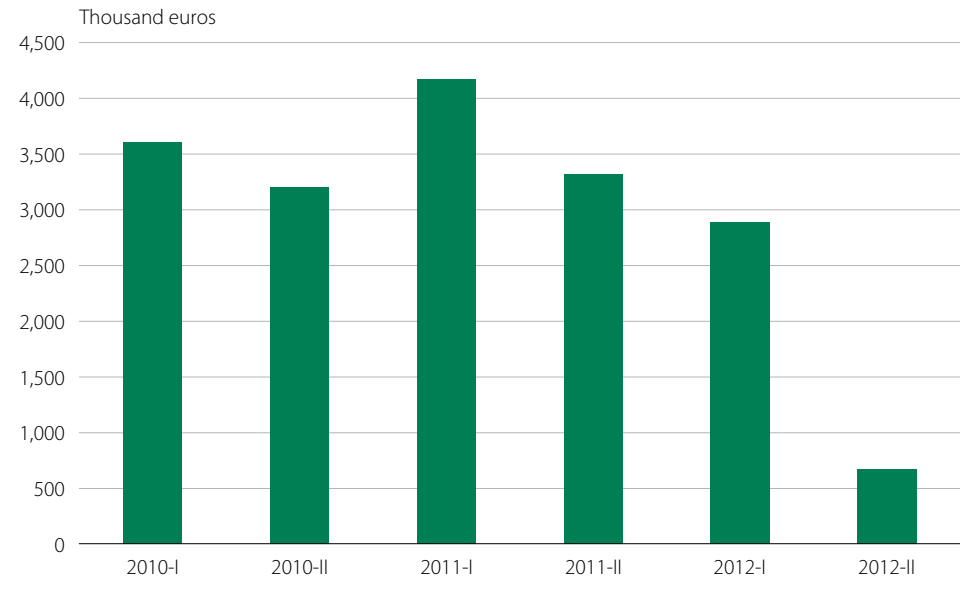
Type of firm	Number	%	Retail clients (%)	Change on 2010 (%)
EAFIs	3,798	1.0	93.3	48.4
Broker-dealers/dealers	10,640	2.8	97.5	-78.5
Portfolio management companies	1352	0.4	99.6	50.2
Total investment firms	15,790	4.2	96.6	-70.1
Spanish credit institutions	355,684	94.6	99.4	46.0
Other	4,691	1.2	99.1	-37.3
Total	376,165	100.0	99.3	23.8

Source: CNMV.

The revenue of EAFIs comes from investment advice, incentives received from third parties in the form of retrocession of commissions made by the clients of said service, and advisory services for companies on capital structures, mergers, preparing investment reports and financial analysis, among other activities. In 2012, total revenue for the sector amounted to 25 million euros. 73% of this amount corresponded strictly to commissions for investment advice, although if we include retrocessions, this percentage rises to 92% (see table 1). In 2011, these percentages stood at 72% and 88% respectively. It should, however, be pointed out that in 2012, 62 of the 101 firms registered at year-end declared that they had not received retrocessions and that three firms accounted for 57% of the amount received for this item. Around 36% of the fees for investment advice in 2012 came from the retail segment.

As shown in table 1, the revenue of EAFIs rose sharply in 2011. However, the figures for 2012 reveal a drop in all its components, which reflects the fall both in assets managed in the non-retail segment as well as the rest of the advisory activities in the sector. The ratio of the revenue for providing investment advice, including the incentives received, and the assets under advice remained relatively stable over both years (0.17% in 2011 and 0.16% in 2012), with a high spread, which reflects the diversity of the business models existing within the sector. EAFIs generally apply fixed fees to institutional clients and retail investors with a high level of assets which are lower than the fees that would result from applying a percentage to the assets under advice.

The sector obtained aggregate profits after tax in 2011 of 7.4 million euros, 7.9% up on the previous year. In 2012, profits fell sharply to 3.6 million euros. At year-end, there were 24 loss-making firms, one more than in 2011, which account for 24% of the total (28% in 2011 and 35% in 2010). Total losses were around 399 thousand euros, compared with 500 thousand in 2011 and close to 400 thousand in 2010. As shown in figure 2, profits have fallen since the second half of 2011, although in 2012 the fall was mainly concentrated in four firms, whose revenue in Spain accounts for 46% of total revenue for the sector. EAFIs in the form of companies accounted for the bulk of the profits generated by the sector. Specifically, in 2012, these firms generated 89% of the sector's profits after tax.



Source: CNMV.

4 Incentives for investment advice in the reform of the MiFID

The proposal for the reform of the MiFID put forward by the European Commission includes a review of the scope of investment advice as it considers that the content of the Directive in this manner is insufficient. Among other new aspects,¹⁸ in order to enhance transparency in price setting, it revises the regulation on the incentives received by advisers. This issue is controversial and has been the subject of an intense debate to the point that the compromise texts published by the Council and by the Parliament contain different positions on this issue, which will require negotiation prior to producing the compromise text which the EU presidency plans to close in the first half of 2013.¹⁹ Both proposals ban incentives when the firms providing the investment service are classified as independent, but there are doubts on the interpretation of the scope of the ban.

Irrespective of the definitive wording of the legislation on this point, the definition of independent advice included in both texts also raises uncertainty. In this regard,

18 In general terms, the information requirements are strengthened as the proposal requires that advisers should explain why they recommend certain products and how they meet the client's risk profile. It also strengthens the information provided to clients as regards complex products (risk, valuation, evolution of underlying assets for structured products). In addition, it specifies the concept of monitoring advice (updating information on the client and the recommendations made).

19 The latest compromise text of the Council was published on 13 February 2013 (<http://register.consilium.europa.eu/pdf/en/13/st06/st06016-re01.en13.pdf>). On 5 October 2012, the European Parliament published the text with amendments to the Commission proposal published, in turn, on 20 October 2011 (<http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2012-0406+0+DOC+XML+V0//EN>).

both the text of the Parliament and the text of the Council indicate that in order to consider the advice provided as independent, firms must assess “a sufficiently large number of investment products or financial instruments available on the market” or “... sufficiently diversified with regard to their type and issuers or product providers”. In order to avoid discretionary interpretations, this wording will need to be more specific with regard to the number and diversity of the financial instruments and providers which must be assessed to meet the conditions for the advice given to be considered as independent.²⁰

In view of the published compromise texts, everything seems to indicate that if the current approach is maintained, then firms providing independent advice will not be able to receive incentives. The proposal for amendment of the MiFID also advocates increasing the transparency of the advisory service by requiring companies which provide the service to inform the investor on whether the advice offered is independent or not. If it is independent, they must inform the client that their recommendations are made after assessing a sufficiently large number of financial instruments (from different providers) available on the market. They must also set and clearly and explicitly inform the client on the amount of the fees that the client will be directly charged.

Current Spanish legislation allows EAFIs to charge retrocessions providing certain requirements are met so as to avoid any conflict of interest which may arise in performing their activity.²¹ If the ban envisaged in the reform of the MiFID materialises, EAFIs will not be able to receive incentives from third parties when they provide independent advice. However, it should be pointed out that independent advice has not, to date, been a dominant line in the business models developed by the sector and, therefore, many firms may continue to receive incentives providing they do not provide an advisory service labelled as independent and providing they comply with the information requirements that will be set out in the legislation. As indicated above, although incentives account for around 18% of the sector’s total revenue, most of the amount received for this item is concentrated in only a few firms. Consequently, the elimination of the incentives included in the reform of the MiFID is not expected to have an excessively harsh impact on the sector.

5 Conclusions

Despite the financial crisis, the number of EAFIs registered with the CNMV has risen sharply over recent years, from 16 firms in 2009 to 107 firms in March 2013. However, EAFIs continue to be relatively unknown firms, given their recent crea-

20 The proposal of the Commission text indicates that this issue will be subject to level 2 implementing measures.

21 Article 59b) of Royal Decree 217/2008, of 15 February, allows incentives to be received providing they increase the quality of the service provided, they do not hinder the firm’s obligation to act in the client’s optimal interest and that the client is informed of this situation in a full, accurate and understandable manner before the service is provided.

tion. This is also the case, unlike in other countries, of independent investment advice in general.²²

As mentioned above, the market share of EAFIs, despite the growth in the number of firms, is still very low in a market which is dominated by banks. In addition, EAFIs face the situation that, in Spain, it was not common for clients to explicitly pay for financial advice. The progress, through EAFIs, of independent advisory services may help to improve the quality of the advice and reduce conflicts of interest.

The experience of the financial crisis, which has revealed major problems relating to the advice given to investors and the marketing of investment products, underlines the importance of promoting independent advice. It is important that clients understand that they are ultimately responsible for making investment decisions and that it may be of great use to them to use a specialised and quality advisory service in this process, which must always be provided by duly authorised firms. The development of financial education programmes, which constitutes a priority for the CNMV, may help to disseminate in the future the informed and prudent use of these services.

While the final resolution on the possible elimination of incentives received by investors from third parties is still not clearly defined, it is reasonable to affirm that the reform of the MiFID that is currently in progress will involve a change in the business models of EAFIs, which will need to further personalise the advisory service and base it on a better knowledge of their clients. The current circumstances are difficult, but EAFIs, like other investment firms, must play an active role in helping investors recover confidence in the financial system. This objective will be strengthened if they develop policies and procedures to ensure that their activities are in line with legislation and that their professionals have sufficient training and experience to make recommendations exclusively in their clients' interest.

22 This service is particularly widespread in the UK and the US. We can highlight, in particular, the Independent Financial Adviser (IFA), authorised by the regulator in the United Kingdom and the Registered Investment Adviser (RIA) in the United States, supervised by the federal regulator if it has more than 100 million dollars from clients under advice or by state securities agencies if the figure is lower.

IV Legislative Annex

New legislation approved since publication of the CNMV bulletin for the fourth quarter of 2012, in chronological order, is as follows:

- **Act 11/2012, of 19 December**, on urgent environmental measures

This Act introduces an Additional Provision 21 in the Securities Market Act so as to include the trading of greenhouse gas emission allowances which are not financial instruments within the scope of application of market abuse legislation.

- **Royal Decree 1698/2012, of 21 December**, which amends current legislation on the prospectus and transparency requirements for securities issues as a result of the transposition of Directive 2010/73.

This Royal Decree transposes to Spanish law existing EU legislation on the prospectus for admission to trading and public offers of securities as well as on transparency with regard to information on issuers.

Among other aspects, the legislative amendment affects the format and content of the prospectus summary, which is standardised throughout the European Union. It also extends the existing exemptions for preparation of the summary and of the prospectus itself, and raises the threshold which distinguishes retail investors from professional investors to 100,000 euros. It also expands the circumstances in which civil liability can arise as a result of defects in the prospectus. Finally, it should be noted that it expressly exempts issues of commercial paper with maturity of less than one year from the requirement for a Final Terms document.

With regard to transparency, it amends the obligations on the language in which certain regulated information must be published.

- **Order ECC/1/2013, of 2 January**, which provides for the creation of State debt in 2013 and January 2014 and establishes the standardised collective action clauses.

This Order provides for the creation of State debt for 2013 and 2014, delegating certain powers to the General Secretariat of the Treasury and Financial Policy. In order to protect the stability of the Eurozone, the Order also regulates the inclusion of collective action clauses in issues of sovereign debt. These clauses allow amendment of the characteristics of bonds in accordance with certain provisions.

- **CNMV Circular 1/2013, of 30 January**, on reporting information relating to investment firms and their parent companies and management companies of collective investment schemes.

This Circular establishes, for investment firms and the management companies of collective investment schemes, the reporting regime, the content of disclosure requirements, the manner in which information is sent and the deadlines for reporting the modifications which may arise in their authorisation conditions.

- **Royal Decree-Law 3/2013, of 22 February**, which amends the fee regime for the administration of justice and the free legal aid system.

Among other measures, this legislation temporarily increases flexibility, in line with events over recent years, with regard to the legal grounds for capital reductions and dissolution due to losses.

- **Royal Decree-Law 4/2013, of 22 February**, on measures to support entrepreneurs and stimulate growth and job creation.

With the aim of facilitating the access of Spanish companies to non-bank financing, this legislation raises the limit imposed in Article 405 of the Capital Companies Act, whereby the total amount of a company's issues may not be greater than the paid-up share capital plus reserves. In particular, this limit is raised for investment in multilateral trading facilities and for those issues which are aimed at institutional investors.

V Statistics Annex

1 Markets

1.1 Equity

Share issues and public offerings¹

TABLE 1.1

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
CASH VALUE³ (million euro)								
Total	16,016.5	17,145.9	21,142.1	3,188.3	5,296.5	5,695.3	6,961.9	4,789.4
Capital increases	15,407.0	17,018.9	19,910.7	3,188.3	5,245.9	5,290.5	6,185.9	4,789.4
Of which, primary offerings	958.7	6,238.8	2,457.3	871.5	1,510.8	75.0	0.0	0.0
With Spanish tranche	61.6	5,827.1	2,457.3	871.5	1,510.8	75.0	0.0	0.0
With international tranche	897.2	411.7	0.0	0.0	0.0	0.0	0.0	0.0
Secondary offerings	609.5	127.0	1,231.4	0.0	50.6	404.8	776.0	0.0
With Spanish tranche	79.1	124.7	1,231.4	0.0	50.6	404.8	776.0	0.0
With international tranche	530.4	2.3	0.0	0.0	0.0	0.0	0.0	0.0
NOMINAL VALUE (million euro)								
Total	6,318.3	5,704.8	4,705.9	975.4	1,512.5	1,008.8	1,209.2	4,964.4
Capital increases	6,309.3	5,698.8	4,595.2	975.4	1,509.7	977.3	1,132.8	4,964.4
Of which, primary offerings	6.8	2,070.6	613.1	522.9	82.1	8.2	0.0	0.0
With Spanish tranche	6.4	1,888.4	613.1	522.9	82.1	8.2	0.0	0.0
With international tranche	0.4	182.2	0.0	0.0	0.0	0.0	0.0	0.0
Secondary offerings	9.0	6.0	110.6	0.0	2.8	31.5	76.4	0.0
With Spanish tranche	8.9	5.9	110.6	0.0	2.8	31.5	76.4	0.0
With international tranche	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0
NO. OF FILES⁴								
Total	69	92	105	23	25	27	30	21
Capital increases	67	91	103	23	25	26	29	21
Of which, primary offerings	12	8	7	4	2	1	0	0
Of which, bonus issues	15	22	22	2	6	10	4	8
Secondary offerings	3	2	3	0	1	1	1	0
NO. OF ISSUERS⁴								
Total	46	46	38	13	16	20	17	13
Capital increases	45	45	38	13	15	19	16	13
Of which, primary offerings	12	8	7	4	2	1	0	0
Secondary offerings	2	2	3	0	1	1	1	0

1 Includes registered offerings with issuance prospectuses and listings admitted to trading without register issuance prospectuses.

2 Available data: February 2013.

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	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
PRIMARY OFFERINGS								
Total	958.7	6,238.8	2,457.3	871.5	1,510.8	75.0	0.0	0.0
Spanish tranche	61.6	5,815.7	6.8	5.3	1.5	0.0	0.0	0.0
Private subscribers	2.5	2,206.3	4.1	2.5	1.5	0.0	0.0	0.0
Institutional subscribers	59.1	3,609.4	2.8	2.8	0.0	0.0	0.0	0.0
International tranche	897.2	411.7	0.0	0.0	0.0	0.0	0.0	0.0
Employees	0.0	11.4	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	2,450.5	866.3	1,509.2	75.0	0.0	0.0
SECONDARY OFFERINGS								
Total	609.5	127.0	1,231.4	0.0	50.6	404.8	776.0	0.0
Spanish tranche	79.1	124.7	0.0	0.0	0.0	0.0	0.0	0.0
Private subscribers	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Institutional subscribers	79.1	124.7	0.0	0.0	0.0	0.0	0.0	0.0
International tranche	530.4	2.3	0.0	0.0	0.0	0.0	0.0	0.0
Employees	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	1,231.4	0.0	50.6	404.8	776.0	0.0

1 Available data: February 2013.

Companies listed¹

TABLE 1.3

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
Total electronic market ³	129	130	127	128	128	127	127	127
Of which, without Nuevo Mercado	129	130	127	128	128	127	127	127
Of which, Nuevo Mercado	0	0	0	0	0	0	0	0
Of which, foreign companies	6	7	7	7	7	7	7	7
Second Market	6	7	8	7	7	7	8	8
Madrid	2	2	2	2	2	2	2	2
Barcelona	4	5	6	5	5	5	6	6
Bilbao	0	0	0	0	0	0	0	0
Valencia	0	0	0	0	0	0	0	0
Open outcry ex SICAVs	28	27	23	24	24	24	23	23
Madrid	13	13	11	11	11	11	11	11
Barcelona	18	17	13	14	14	14	13	13
Bilbao	8	8	7	7	7	7	7	7
Valencia	6	6	4	4	4	4	4	4
Open outcry SICAVs	1	0	0	0	0	0	0	0
MAB ⁴	3,144	3,083	3,015	3,064	3,059	3,034	3,015	3,005
Latibex	29	29	27	27	27	27	27	27

1 Data at the end of period.

2 Available data: February 2013.

3 Without ETFs (Exchange Traded Funds).

4 Alternative Stock Market.

Capitalisation¹

TABLE 1.4

Million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
Total electronic market ³	531,194.2	498,148.1	532,039.7	487,334.8	443,405.2	490,027.9	532,039.7	551,673.0
Of which, without Nuevo Mercado	531,194.2	498,148.1	532,039.7	487,334.8	443,405.2	490,027.9	532,039.7	551,673.0
Of which, Nuevo Mercado	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which, foreign companies ⁴	61,317.5	82,471.4	99,072.0	90,381.7	85,013.5	89,988.0	99,072.0	107,391.4
Ibex 35	322,806.6	320,672.5	324,442.0	306,878.6	272,514.9	302,019.9	324,442.0	334,302.5
Second Market	109.9	59.7	20.6	56.8	57.8	46.3	20.6	60.4
Madrid	22.8	25.5	20.3	22.6	23.6	23.6	20.3	11.1
Barcelona	87.1	34.2	0.3	34.2	34.2	22.7	0.3	49.3
Bilbao	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valencia	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Open outcry ex SICAVs	5,340.7	3,704.9	3,233.0	3,482.1	3,364.7	3,257.6	3,233.0	3,178.1
Madrid	1,454.7	833.3	667.1	729.9	682.9	673.4	667.1	642.9
Barcelona	3,580.2	3,242.3	2,945.9	3,120.6	3,053.6	2,953.6	2,945.9	2,888.1
Bilbao	45.9	328.8	77.8	323.7	78.9	78.9	77.8	248.7
Valencia	760.4	240.2	350.9	423.5	379.6	369.4	350.9	352.0
Open outcry SICAVs ⁵	126.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0
MAB ^{5,6}	24,718.6	23,646.0	23,776.0	24,524.4	23,315.7	24,188.7	23,776.0	24,284.3
Latibex	210,773.5	402,008.5	350,635.5	414,431.2	358,599.2	369,568.3	350,635.5	332,746.7

1 Data at the end of period.

2 Available data: February 2013.

3 Without ETFs (Exchange Traded Funds).

4 Foreign companies capitalisation includes their entire shares, whether they are deposited in Spain or not.

5 Calculated only with outstanding shares, not including treasury shares, because capital stock is not reported until the end of the year.

6 Alternative Stock Market.

Trading

TABLE 1.5

Million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Total electronic market ²	1,026,478.5	917,383.3	691,558.3	175,186.1	196,896.4	151,267.7	168,208.0	108,707.4
Of which, without Nuevo Mercado	1,026,478.5	917,383.3	691,558.3	175,186.1	196,896.4	151,267.7	168,208.0	108,707.4
Of which, Nuevo Mercado	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which, foreign companies	6,415.3	5,206.3	4,102.1	1,505.8	963.9	851.6	780.8	748.0
Second Market	3.0	2.3	0.4	0.1	0.2	0.2	0.0	0.0
Madrid	2.8	1.7	0.4	0.1	0.2	0.2	0.0	0.0
Barcelona	0.3	0.5	0.0	0.0	0.0	0.0	0.0	0.0
Bilbao	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valencia	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Open outcry ex SICAVs	157.2	42.8	49.9	16.5	7.3	8.3	17.7	4.1
Madrid	15.7	16.1	3.0	1.6	0.4	0.8	0.3	2.2
Barcelona	135.7	26.4	37.7	14.4	6.9	7.4	9.0	1.9
Bilbao	3.9	0.1	8.5	0.0	0.0	0.0	8.5	0.0
Valencia	1.9	0.3	0.7	0.6	0.1	0.0	0.0	0.0
Open outcry SICAVs	8.1	5.6	0.0	0.0	0.0	0.0	0.0	0.0
MAB ³	4,147.9	4,379.9	4,329.6	1,218.1	1,104.5	947.0	1,060.0	821.1
Latibex	521.2	357.7	313.2	73.3	61.7	89.5	88.7	64.0

1 Available data: February 2013.

2 Without ETFs (Exchange Traded Funds).

3 Alternative Stock Market.

Trading on the electronic market by type of transaction¹

TABLE 1.6

Million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
Regular trading	983,584.5	873,485.4	658,891.4	168,765.0	187,871.7	143,171.9	159,082.8	105,268.3
Orders	541,879.8	505,870.1	299,022.0	103,947.2	81,004.3	61,468.6	52,601.8	56,163.7
Put-throughs	58,678.1	69,410.4	80,617.0	12,028.9	30,160.1	21,441.3	16,986.8	9,297.5
Block trades	383,026.6	298,204.9	279,252.4	52,788.9	76,707.3	60,262.0	89,494.2	39,807.1
Off-hours	17,209.5	9,801.8	9,630.0	816.2	2,006.8	3,506.5	3,300.4	1,534.3
Authorised trades	2,660.5	3,492.6	7,936.9	1,026.7	2,301.0	2,202.6	2,406.5	947.4
Art. 36.1 SML trades	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Tender offers	312.0	4,216.8	9.6	0.0	9.6	0.0	0.0	0.0
Public offerings for sale	1,448.2	3,922.1	0.0	0.0	0.0	0.0	0.0	0.0
Declared trades	2,273.4	2,212.7	545.0	0.0	539.7	2.4	3.0	0.2
Options	11,474.7	11,730.3	9,603.4	2,301.1	2,991.2	1,472.1	2,838.9	270.6
Hedge transactions	7,515.8	8,521.5	4,942.0	2,277.0	1,176.4	912.3	576.3	686.7

1 Without ETFs (Exchange Traded Funds).

2 Available data: February 2013.

Margin trading for sales and securities lending

TABLE 1.7

Million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
TRADING								
Securities lending ²	556,246.7	493,602.4	395,859.3	98,303.7	115,376.8	79,731.5	102,447.3	79,106.4
Margin trading for sales of securities ³	598.0	518.3	199.2	76.1	100.3	16.8	6.1	32.3
Margin trading for securities purchases ³	65.9	73.0	44.4	16.0	7.0	11.1	10.3	8.5
OUTSTANDING BALANCE								
Securities lending ²	36,195.9	35,626.7	34,915.1	29,608.2	33,174.2	39,075.3	34,915.1	35,856.5
Margin trading for sales of securities ³	9.9	7.0	1.2	6.7	13.2	1.6	1.2	10.0
Margin trading for securities purchases ³	5.0	3.9	2.5	3.9	2.2	2.5	2.5	2.8

1 Available data: February 2013.

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 registered¹ at the CNMV

TABLE 1.8

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
NO. OF ISSUERS								
Total	115	101	71	37	29	19	32	14
Mortgage covered bonds	25	30	26	12	11	15	11	7
Territorial covered bonds	6	7	11	6	7	2	0	0
Non-convertible bonds and debentures	39	23	24	15	12	6	8	6
Convertible bonds and debentures	2	5	3	1	2	0	1	0
Backed securities	36	34	16	5	2	1	9	3
Commercial paper	58	49	35	17	12	5	9	1
Of which, asset-backed	2	2	1	0	0	0	1	0
Of which, non-asset-backed	56	47	34	17	12	5	8	1
Other fixed-income issues	0	0	0	0	0	0	0	0
Preference shares	0	1	0	0	0	0	0	0
NO. OF ISSUES								
Total	349	353	334	117	100	48	69	38
Mortgage covered bonds	88	115	94	27	22	27	18	13
Territorial covered bonds	9	42	18	8	8	2	0	0
Non-convertible bonds and debentures	154	87	134	48	50	13	23	17
Convertible bonds and debentures	3	9	7	1	4	0	2	0
Backed securities	36	45	35	15	2	1	17	7
Commercial paper	59	53	46	18	14	5	9	1
Of which, asset-backed	2	2	1	0	0	0	1	0
Of which, non-asset-backed	57	51	45	18	14	5	8	1
Other fixed-income issues	0	0	0	0	0	0	0	0
Preference shares	0	2	0	0	0	0	0	0
NOMINAL AMOUNT (million euro)								
Total	226,448.9	288,992.0	357,830.2	120,821.9	91,425.1	60,679.5	84,903.7	35,998.4
Mortgage covered bonds	34,378.5	67,226.5	102,170.0	26,000.0	33,350.0	29,800.0	13,020.0	7,995.0
Territorial covered bonds	5,900.0	22,334.2	8,974.0	3,200.0	4,100.0	1,674.0	0.0	0.0
Non-convertible bonds and debentures	24,356.0	20,191.7	86,441.5	31,304.9	15,230.7	91.1	39,814.9	15,517.7
Convertible bonds and debentures	968.0	7,125.9	3,563.1	1,128.2	1,592.3	0.0	842.5	0.0
Backed securities	63,260.5	68,412.8	23,799.6	9,195.3	1,535.3	1,884.0	11,185.0	4,643.8
Spanish tranche	62,743.0	63,455.9	20,627.1	7,810.3	1,535.3	1,884.0	9,397.5	4,120.7
International tranche	517.5	4,956.9	3,172.5	1,385.0	0.0	0.0	1,787.5	523.1
Commercial paper ³	97,586.0	103,501.0	132,882.0	49,993.4	35,616.9	27,230.5	20,041.2	7,841.9
Of which, asset-backed	5,057.0	2,366.0	1,821.0	616.0	630.0	275.0	300.0	180.0
Of which, non-asset-backed	92,529.0	101,135.0	131,061.0	49,377.4	34,986.9	26,955.5	19,741.2	7,661.9
Other fixed-income issues	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Preference shares	0.0	200.0	0.0	0.0	0.0	0.0	0.0	0.0
Pro memoria:								
Subordinated issues	9,154.2	29,198.9	7,633.5	2,772.2	1,788.3	580.9	2,492.0	824.2
Underwritten issues	299.0	10.0	0.0	0.0	0.0	0.0	0.0	0.0

1 Includes issuance and trading prospectuses.

2 Available data: February 2013.

3 The figures for commercial paper refer to the amount placed in the year.

Issues admitted to trading on AIAF

TABLE 1.9

Nominal amount in million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Total	223,404.5	278,656.0	363,952.5	127,394.8	85,145.2	69,879.2	81,533.4	36,912.5
Commercial paper	99,784.4	102,042.0	134,346.9	51,871.2	32,233.4	31,278.3	18,964.1	9,101.3
Bonds and debentures	24,728.6	12,311.9	92,733.5	36,439.3	15,868.4	692.9	39,732.8	15,540.9
Mortgage covered bonds	32,861.0	68,346.5	103,470.0	27,500.0	28,800.0	34,350.0	12,820.0	9,195.0
Territorial covered bonds	5,900.0	20,334.2	8,974.0	2,500.0	4,800.0	1,674.0	0.0	0.0
Backed securities	60,030.5	75,421.4	24,428.1	9,084.3	3,443.3	1,884.0	10,016.5	3,075.3
Preference shares	100.0	200.0	0.0	0.0	0.0	0.0	0.0	0.0
Matador bonds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

1 Available data: February 2013.

AIAF. Issuers, issues and outstanding balance

TABLE 1.10

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
NO. OF ISSUERS								
Total	614	634	613	613	611	596	572	569
Commercial paper	67	60	45	45	51	49	46	45
Bonds and debentures	91	93	91	91	95	96	94	94
Mortgage covered bonds	29	33	43	43	47	46	50	50
Territorial covered bonds	11	12	13	13	16	18	19	18
Backed securities	442	459	437	437	427	415	391	386
Preference shares	60	59	60	60	60	60	60	60
Matador bonds	12	12	12	12	12	12	12	12
NO. OF ISSUES								
Total	4,084	3,630	4,382	4,382	5,116	5,285	5,208	5,020
Commercial paper	1,507	958	1,778	1,778	2,547	2,757	2,762	2,599
Bonds and debentures	611	645	624	624	628	600	583	577
Mortgage covered bonds	202	253	296	296	301	316	334	340
Territorial covered bonds	25	26	49	49	52	58	55	53
Backed securities	1,629	1,641	1,527	1,527	1,480	1,446	1,366	1,343
Preference shares	96	93	94	94	94	94	94	94
Matador bonds	14	14	14	14	14	14	14	14
OUTSTANDING BALANCE² (million euro)								
Total	870,981.1	850,181.7	882,395.1	882,395.1	906,229.5	899,458.8	886,354.6	869,296.1
Commercial paper	41,647.0	23,233.6	37,549.1	37,549.1	62,370.8	66,983.5	75,777.8	69,617.8
Bonds and debentures	150,886.3	146,077.7	131,756.8	131,756.8	144,455.8	132,981.0	125,944.4	125,584.5
Mortgage covered bonds	185,343.8	195,734.8	241,149.7	241,149.7	257,034.8	283,064.8	309,736.1	309,606.1
Territorial covered bonds	16,030.0	18,350.0	31,884.2	31,884.2	31,834.2	35,284.2	33,579.6	33,397.3
Backed securities	442,831.5	434,835.1	407,908.0	407,908.0	391,012.1	364,253.6	327,492.8	317,299.7
Preference shares	33,183.8	30,891.8	31,088.6	31,088.6	18,463.1	15,833.0	12,765.1	12,755.7
Matador bonds	1,058.8	1,058.8	1,058.8	1,058.8	1,058.8	1,058.8	1,058.8	1,035.0

1 Available data: February 2013.

2 Nominal amount.

AIAF. Trading

TABLE 1.11

Nominal amount in million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
BY TYPE OF ASSET								
Total	4,383,118.7	7,388,185.7	3,119,755.1	928,497.2	555,233.8	674,389.1	961,635.0	282,728.8
Commercial paper	385,238.9	227,534.5	199,794.9	57,736.6	42,897.4	55,717.4	43,443.5	21,715.5
Bonds and debentures	922,393.1	484,705.8	164,098.6	41,431.0	40,927.5	44,398.4	37,341.6	42,969.6
Mortgage covered bonds	271,441.8	662,177.0	994,071.3	247,459.2	168,803.9	302,081.0	275,727.2	95,443.3
Territorial covered bonds	14,458.2	544,780.9	595,599.6	179,057.4	180,778.2	108,473.6	127,290.5	17,712.3
Backed securities	2,784,775.4	5,462,806.2	1,136,966.1	394,669.6	114,957.9	156,980.5	470,358.1	104,559.0
Preference shares	4,635.7	6,065.0	28,781.3	8,132.1	6,593.8	6,616.4	7,438.9	329.1
Matador bonds	175.7	116.3	443.2	11.2	275.1	121.8	35.1	0.0
BY TYPE OF TRANSACTION								
Total	4,383,118.7	7,388,185.7	3,119,755.1	928,497.2	555,233.8	674,389.1	961,635.0	282,728.8
Outright	288,927.3	343,099.6	428,838.0	151,533.7	121,364.6	78,110.9	77,828.8	47,244.4
Repos	304,493.2	198,514.7	108,771.9	41,562.1	29,885.1	18,513.0	18,811.8	12,438.5
Sell-buybacks/Buy-sellbacks	3,789,698.3	6,846,571.5	2,582,145.2	735,401.4	403,984.2	577,765.2	864,994.5	223,045.9

1 Available data: February 2013.

AIAF. Third-party trading. By purchaser sector

TABLE 1.12

Nominal amount in million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Total	553,896.6	487,543.3	454,385.7	157,876.8	129,837.4	84,419.9	82,251.6	52,146.6
Non-financial companies	162,949.5	131,765.2	77,452.1	21,411.0	17,333.2	19,618.1	19,089.8	11,562.3
Financial institutions	289,950.4	256,975.8	282,733.9	103,512.7	90,698.5	46,946.5	41,576.2	24,860.4
Credit institutions	102,372.1	139,538.2	207,555.6	69,411.4	68,400.6	38,309.4	31,434.2	16,256.9
IICs ² , insurance and pension funds	125,899.4	103,899.9	69,568.7	32,613.5	21,122.2	7,132.0	8,701.1	7,432.5
Other financial institutions	61,678.9	13,537.7	5,609.6	1,487.8	1,175.8	1,505.2	1,440.9	1,171.0
General government	3,117.7	2,602.7	5,448.2	3,372.9	747.2	1,005.9	322.3	311.9
Households and NPISHs ³	14,244.4	10,230.3	11,517.9	2,793.4	2,373.7	3,137.1	3,213.5	859.8
Rest of the world	83,634.6	85,969.3	77,233.7	26,786.8	18,684.8	13,712.3	18,049.8	14,552.2

1 Available data: February 2013.

2 IICs: Instituciones de Inversión Colectiva / CIS: Collective Investment Schemes.

3 Non-profit institutions serving households.

Issues admitted to trading on equity markets¹

TABLE 1.13

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
NOMINAL AMOUNTS (million euro)								
Total	868.0	2,681.6	7,522.0	4,875.9	1,765.9	880.2	0.0	779.3
Non-convertible bonds and debentures	400.0	0.0	0.0	0.0	0.0	0.0	0.0	779.3
Convertible bonds and debentures	468.0	2,681.6	7,522.0	4,875.9	1,765.9	880.2	0.0	0.0
Backed securities	0.0	0.0	0.0	0.0	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
NO. OF ISSUES								
Total	8	6	7	2	2	3	0	2
Non-convertible bonds and debentures	7	0	0	0	0	0	0	0
Convertible bonds and debentures	1	6	7	2	2	3	0	2
Backed securities	0	0	0	0	0	0	0	0
Others	0	0	0	0	0	0	0	0

1 Private issuers. Includes issuance and trading prospectuses.

2 Available data: February 2013.

Equity markets. Issuers, issues and outstanding balances

TABLE 1.14

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
NO. OF ISSUERS								
Total	60	59	52	57	56	55	52	51
Private issuers	46	46	39	44	43	42	39	38
Non-financial companies	5	4	3	4	4	4	3	3
Financial institutions	41	42	36	40	39	38	36	35
General government ²	14	13	13	13	13	13	13	13
Regional governments	3	3	3	3	3	3	3	3
NO. OF ISSUES								
Total	247	240	220	231	224	224	220	216
Private issuers	145	133	122	126	124	125	122	122
Non-financial companies	7	6	3	6	5	5	3	3
Financial institutions	138	127	119	120	119	120	119	119
General government ²	102	107	98	105	100	99	98	94
Regional governments	64	74	67	73	69	68	67	65
OUTSTANDING BALANCES³ (million euro)								
Total	41,091.3	43,817.5	37,636.4	47,939.8	45,444.9	43,726.1	37,636.4	36,645.7
Private issuers	19,261.5	17,759.6	13,625.4	21,694.6	19,645.5	16,429.5	13,625.4	13,032.5
Non-financial companies	376.6	375.4	194.9	375.4	195.1	195.1	194.9	195.0
Financial institutions	18,884.8	17,384.2	13,430.6	21,319.2	19,450.4	16,234.4	13,430.6	12,837.5
General government ²	21,829.9	26,057.8	24,010.9	26,245.2	25,799.4	27,296.6	24,010.9	23,613.2
Regional governments	19,442.4	24,014.4	22,145.0	24,276.9	23,932.2	25,429.9	22,145.0	21,847.3

1 Available data: February 2013.

2 Without public book-entry debt.

3 Nominal amount.

Trading on equity markets

TABLE 1.15

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Nominal amounts in million euro								
Electronic market	504.5	386.1	1,198.3	131.6	784.5	137.5	144.6	927.9
Open outcry	7,525.6	4,942.5	3,746.6	2,101.8	392.6	904.7	347.6	108.9
Madrid	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Barcelona	7,146.7	4,885.4	3,407.8	1,813.8	389.9	863.1	341.0	7.0
Bilbao	2.3	0.5	0.2	0.1	0.0	0.0	0.0	0.0
Valencia	376.6	56.6	338.7	287.8	2.7	41.6	6.6	101.9
Public book-entry debt	331.1	883.4	1,189.0	396.6	321.4	464.4	6.6	5.2
Regional governments debt	62,029.0	63,443.7	54,015.1	13,144.2	14,588.0	13,761.1	12,521.7	5,750.0

1 Available data: February 2013.

Organised trading systems: SENAF y MTS. Public debt trading by type

TABLE 1.16

Nominal amounts in million euro	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Total	265,966.0	84,090.9	84,090.9	18,979.0	9,235.0	4,979.0	6,841.0	7,181.0
Outright	110,011.0	81,905.0	81,905.0	18,979.0	9,235.0	4,979.0	6,841.0	7,181.0
Sell-buybacks/Buy-sellbacks	155,433.0	2,185.9	2,185.9	0.0	0.0	0.0	0.0	0.0
Others	522.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

1 Available data: February 2013.

1.3 Derivatives and other products

1.3.1 Financial derivatives markets: MEFF

Trading on MEFF

TABLE 1.17

Number of contracts	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Debt products	14	18	45,240	2	10,796	18,659	15,783	3,519
Debt futures ²	14	18	45,240	2	10,796	18,659	15,783	3,519
Ibex 35 products ^{3,4}	6,946,167	5,819,264	5,410,311	1,120,323	1,884,757	1,370,029	1,035,203	894,750
Ibex 35 plus futures	6,280,999	5,291,956	4,745,067	1,022,021	1,683,154	1,183,751	856,141	773,755
Ibex 35 mini futures	357,926	307,411	242,477	49,547	95,423	62,721	34,786	31,925
Ibex 35 dividend impact futures	–	3,154	2,162	555	382	210	1,015	466
Call mini options	122,158	86,096	225,704	18,669	55,375	64,746	86,915	48,880
Put mini options	185,083	133,801	194,902	29,532	50,423	58,601	56,347	39,724
Stock products ⁵	57,291,482	55,082,944	55,753,236	16,534,500	14,627,113	12,394,790	12,196,833	6,407,602
Futures	19,684,108	24,758,956	21,220,876	7,087,730	6,357,895	3,397,488	4,377,763	2,375,916
Stock dividend futures	–	–	25,000	1,500	0	0	23,500	18,300
Call options	17,186,515	12,050,946	14,994,283	4,333,910	2,977,728	4,272,914	3,409,731	1,963,340
Put options	20,420,859	18,273,042	19,513,077	5,111,360	5,291,490	4,724,388	4,385,839	2,050,046
Pro-memoria: MEFF trading on Eurex								
Debt products ⁶	373,113	267,713	161,376	39,172	51,603	28,209	42,392	30,116
Index products ⁷	604,029	451,016	266,422	78,776	71,498	61,078	55,070	21,779

1 Available data: February 2013.

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 1.18

WARRANTS ²	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Premium amount (million euro)	4,915.3	5,544.6	3,834.3	922.4	1,202.9	751.3	957.7	1,062.1
On stocks	2,537.4	3,211.7	2,231.7	509.7	685.2	468.2	568.6	604.8
On indexes	1,852.6	1,786.8	1,273.5	310.3	435.7	229.7	297.8	394.8
Other underlyings ³	525.4	546.0	329.1	102.4	82.0	53.3	91.4	62.5
Number of issues	8,375	9,237	7,073	1,733	1,798	1,319	2,223	2,303
Number of issuers	9	9	7	6	4	5	6	5
OPTION BUYING AND SELLING CONTRACTS								
Nominal amounts (million euro)	64.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
On stocks	47.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
On indexes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other underlyings ³	17.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Number of issues	7	0	0	0	0	0	0	0
Number of issuers	1	0	0	0	0	0	0	0

1 Available data: February 2013.

2 Includes issuance and trading prospectuses.

3 Includes the following underlying: baskets of stocks, exchange rates, interest rates and commodities.

Equity markets. Warrants and ETF trading

TABLE 1.19

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
WARRANTS								
Trading (million euro)	1,603.2	1,550.2	762.9	243.4	178.6	195.2	145.7	137.6
On Spanish stocks	759.8	654.2	349.0	103.7	78.0	94.9	72.4	64.3
On foreign stocks	60.7	97.8	87.6	34.3	15.5	17.4	20.4	26.0
On indexes	689.5	518.2	268.6	75.7	73.4	75.1	44.5	41.9
Other underlyings ²	93.2	280.0	57.7	29.8	11.7	7.9	8.3	5.3
Number of issues ³	7,750	13,165	11,980	3,176	3,069	2,919	2,816	2,390
Number of issuers ³	10	9	34	9	9	9	7	7
CERTIFICATES								
Trading (million euro)	22.0	92.1	16.8	6.5	6.6	2.7	1.1	0.1
Number of issues ³	16	32	13	4	4	3	2	1
Number of issuers ³	2	2	7	2	2	2	1	1
ETFs								
Trading (million euro)	6,229.7	3,495.4	2,935.7	1,027.0	454.0	639.1	639.1	896.4
Number of funds	65	75	74	75	75	73	74	74
Assets ⁴ (million euro)	827.8	327.2	274.7	297.4	262.5	277.3	274.7	n. a.

1 Available data: February 2013.

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 Assets from national collective investment schemes is only included because assets from foreign ones are not available.

n.a.: No available data.

1.3.3 Non-financial derivatives

Trading on MFAO¹

TABLE 1.20

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
Number of contracts								
On olive oil								
Extra-virgin olive oil futures ³	165,840	63,173	78,566	10,050	10,577	33,350	34,639	18,888

1 Olive oil futures market.

2 Available data: February 2013.

3 Nominal amount of the contract: 1,000 kg.

2 Investment services

Investment services. Spanish firms, branches and agents

TABLE 2.1

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
BROKER-DEALERS								
Spanish firms	50	49	46	48	48	47	46	46
Branches	80	78	15	23	25	17	15	14
Agents	6,560	6,589	6,267	6,516	6,531	6,305	6,267	6,242
BROKERS								
Spanish firms	45	45	41	45	45	43	41	41
Branches	13	14	10	12	12	12	10	10
Agents	689	655	601	620	633	622	601	541
PORTFOLIO MANAGEMENT COMPANIES								
Spanish firms	6	6	6	6	6	6	6	6
Branches	5	5	5	5	5	5	5	5
Agents	2	2	2	2	2	2	2	2
FINANCIAL ADVISORY FIRMS²								
Spanish firms	58	82	101	91	97	101	101	105
CREDIT INSTITUTIONS³								
Spanish firms	186	187	172	190	188	181	172	165

1 Available data: February 2013.

2 Investment services company created by Law 47/2008, of 19 December, which modifies Law 24/1988, of 28 July, on the Securities Market, and regulated by Circular CR CNMV 10/2008, of 30 December.

3 Source: Banco de España.

Investment services. Foreign firms

TABLE 2.2

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Total	2,671	2,814	2,992	2,861	2,907	2,950	2,992	3,021
European Economic Area investment services firms	2,238	2,377	2,534	2,418	2,459	2,501	2,534	2,564
Branches	40	36	37	36	35	39	37	36
Free provision of services	2,198	2,341	2,497	2,382	2,424	2,462	2,497	2,528
Credit institutions ²	433	437	458	443	448	449	458	457
From EU member states	423	429	448	434	438	439	448	447
Branches	55	55	55	55	56	55	55	55
Free provision of services	368	374	393	379	382	384	393	392
Subsidiaries of free provision of services institutions	0	0	0	0	0	0	0	0
From non-EU states	10	8	10	9	10	10	10	10
Branches	8	7	8	7	8	8	8	8
Free provision of services	2	1	2	2	2	2	2	2

1 Available data: February 2013.

2 Source: Banco de España and CNMV.

Intermediation of spot transactions¹

TABLE 2.3

	IV 2011				IV 2012			
	Spanish organised markets	Other Spanish markets	Foreign markets	Total	Spanish organised markets	Other Spanish markets	Foreign markets	Total
Million euro								
FIXED-INCOME								
Total	894,746	1,963,649	131,870	2,990,265	652,591	1,833,612	138,884	2,625,087
Broker-dealers	104,750	557,772	88,465	750,987	241,643	477,969	95,479	815,091
Brokers	789,996	1,405,877	43,405	2,239,278	410,948	1,355,643	43,405	1,809,996
EQUITY								
Total	187,116	1,051	15,099	203,266	139,200	3,460	13,037	155,697
Broker-dealers	182,389	931	13,822	197,142	134,707	568	11,760	147,035
Brokers	4,727	120	1,277	6,124	4,493	2,892	1,277	8,662

1 Period accumulated data. Quarterly.

Intermediation of derivative transactions^{1,2}

TABLE 2.4

Million euro	IV 2011				IV 2012			
	Spanish organised markets	Foreign organised markets	Non-organised markets	Total	Spanish organised markets	Foreign organised markets	Non-organised markets	Total
Total	455,161	116,726	1,386,748	1,958,635	362,237	96,703	841,082	1,300,022
Broker-dealers	454,034	60,889	1,268,455	1,783,378	361,123	59,690	722,789	1,143,602
Brokers	1,127	55,837	118,293	175,257	1,114	37,013	118,293	156,420

- 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.
- 2 Period accumulated data. Quarterly.

Portfolio management. Number of portfolios and assets under management¹

TABLE 2.5

	IV 2011			IV 2012		
	IIC ²	Other ³	Total	IIC ²	Other ³	Total
NUMBER OF PORTFOLIOS						
Total	147	13,262	13,409	116	10,866	10,982
Broker-dealers	89	6,394	6,483	67	4,055	4,122
Brokers	53	3,584	3,637	44	3,636	3,680
Portfolio management companies	5	3,284	3,289	5	3,175	3,180
ASSETS UNDER MANAGEMENT (thousand euro)						
Total	1,924,432	7,630,157	9,554,589	1,443,031	7,739,511	9,182,542
Broker-dealers	961,931	3,204,236	4,166,167	961,837	2,618,216	3,580,053
Brokers	863,856	1,498,088	2,361,944	373,503	1,553,717	1,927,220
Portfolio management companies	98,645	2,927,833	3,026,478	107,691	3,567,578	3,675,269

- 1 Data at the end of period. Quarterly.
- 2 IIC: Instituciones de Inversión Colectiva / CIS: Collective Investment Schemes. Includes both resident and non resident IICs management.
- 3 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.

Financial advice. Number of contracts and assets advised¹

TABLE 2.6

	IV 2011			IV 2012		
	Retail clients	Professional clients	Total ²	Retail clients	Professional clients	Total ²
NUMBER OF CONTRACTS						
Total	7,602	124	7,726	8,914	426	9,340
Broker-dealers	1,492	12	1,504	1,183	13	1,196
Brokers	4,736	102	4,838	6,019	406	6,425
Portfolio management companies	1,374	10	1,384	1,712	7	1,719
ASSETS ADVISED (thousand euro)						
Total	3,333,448	4,466,705	7,800,153	4,863,960	2,392,376	7,256,336
Broker-dealers	863,386	61,711	925,097	568,359	27,613	595,972
Brokers	1,875,867	1,018,647	2,894,514	3,590,416	1,899,566	5,489,982
Portfolio management companies	594,195	3,386,347	3,980,542	705,185	465,197	1,170,382

- 1 Data at the end of period. Quarterly.
- 2 Includes retail, professional and other clients.

Aggregated income statement. Broker-dealers

TABLE 2.7

Thousand euro ¹	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
I. Interest income	102,054	91,542	56,161	7,206	32,651	43,328	56,161	1,612
II. Net commission	533,858	490,517	410,740	119,253	234,842	324,639	410,740	35,411
Commission revenues	798,152	776,641	589,027	181,675	331,330	460,661	589,027	51,396
Brokering	555,207	529,711	348,403	121,864	200,721	276,779	348,403	32,994
Placement and underwriting	8,499	7,446	6,869	2,686	4,089	4,689	6,869	828
Securities deposit and recording	22,367	21,060	19,775	4,738	10,091	15,090	19,775	1,635
Portfolio management	13,880	16,186	14,883	3,658	6,881	10,005	14,883	1,381
Design and advising	53,722	60,712	12,067	13,546	26,539	19,856	12,067	809
Stocks search and placement	36	485	50	0	25	31	50	5
Market credit transactions	9	8	8	4	6	6	8	2
IICs ³ marketing	65,487	59,588	45,050	12,237	23,113	33,927	45,050	4,755
Other	78,944	81,446	141,924	22,943	59,864	100,278	141,924	8,987
Commission expenses	264,294	286,124	178,287	62,422	96,488	136,022	178,287	15,985
III. Financial investment income	48,588	271,956	9,403	109	92,439	39,959	9,403	-33,369
IV. Net exchange differences and other operating products and expenses	26,081	-194,355	-28,522	36,111	-56,355	24,051	-28,522	43,018
V. Gross income	710,580	659,659	447,782	162,679	303,577	431,977	447,782	46,672
VI. Operating income	276,253	207,379	35,304	44,102	92,286	129,448	35,304	13,074
VII. Earnings from continuous activities	196,834	148,553	-12,057	40,971	78,460	107,043	-12,057	10,567
VIII. Net earnings of the period	196,834	148,553	-12,057	40,971	78,460	107,043	-12,057	10,567

1 Accumulated data from the beginning of the year to the last day of every quarter. It includes companies removed throughout the year.

2 Available data: January 2013.

3 IIC: Instituciones de Inversión Colectiva / CIS: Collective Investment Schemes.

Results of proprietary trading. Broker-dealers

TABLE 2.8

Thousand euro ¹	Interest income		Financial investment income		Exchange differences and other items		Total	
	IV 2011	IV 2012	IV 2011	IV 2012	IV 2011	IV 2012	IV 2011	IV 2012
	Total	91,803	56,218	271,214	9,403	-179,490	-44,283	183,527
Money market assets and public debt	2,327	4,055	13,630	14,881	-	-	15,957	18,936
Other fixed-income securities	20,272	17,089	58,801	-17,073	-	-	79,073	16
Domestic portfolio	17,934	15,180	49,149	-29,993	-	-	67,083	-14,813
Foreign portfolio	2,338	1,909	9,651	12,920	-	-	11,989	14,829
Equities	54,249	35,220	-460,992	321,374	-	-	-406,743	356,594
Domestic portfolio	36,991	19,064	-26,610	-11,061	-	-	10,381	8,003
Foreign portfolio	17,258	16,156	-434,381	332,436	-	-	-417,123	348,592
Derivatives	-	-	669,506	-308,833	-	-	669,506	-308,833
Repurchase agreements	1,357	-3,871	-	-	-	-	1,357	-3,871
Market credit transactions	0	0	-	-	-	-	0	0
Deposits and other transactions with financial intermediaries	16,321	5,440	-	-	-	-	16,321	5,440
Net exchange differences	-	-	-	-	-198,530	-37,363	-198,530	-37,363
Other operating products and expenses	-	-	-	-	30,162	8,787	30,162	8,787
Other transactions	-2,724	-1,716	-9,731	-946	-11,122	-15,707	-23,577	-18,369

1 Accumulated data from the beginning of the year to the last day of every quarter. It includes companies removed throughout the year.

Aggregated income statement. Brokers

TABLE 2.9

Thousand euro ¹	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
I. Interest income	1,629	2,481	1,912	348	946	1,401	1,912	190
II. Net commission	109,165	97,886	93,246	24,588	46,663	67,075	93,246	8,495
Commission revenues	126,055	112,351	108,198	28,113	53,623	77,220	108,198	9,938
Brokering	38,176	36,354	38,112	9,586	17,993	28,968	38,112	4,449
Placement and underwriting	2,748	2,870	3,128	751	1,620	1,871	3,128	24
Securities deposit and recording	366	441	576	103	311	458	576	43
Portfolio management	19,489	12,352	14,476	2,904	5,487	8,356	14,476	952
Design and advising	3,618	5,349	3,123	1,249	2,455	3,822	3,123	331
Stocks search and placement	304	61	88	0	0	0	88	0
Market credit transactions	27	42	30	7	14	23	30	2
IICs ³ marketing	23,946	21,381	25,949	4,915	9,880	15,124	25,949	2,160
Other	37,381	33,500	22,715	8,598	15,864	18,599	22,715	1,979
Commission expenses	16,890	14,465	14,952	3,525	6,960	10,145	14,952	1,443
III. Financial investment income	456	622	1,255	122	787	1,093	1,255	50
IV. Net exchange differences and other operating products and expenses	-1,416	-1,539	-1,459	-341	-953	-1,340	-1,459	-144
V. Gross income	109,834	99,450	94,954	24,717	47,443	68,229	94,954	8,591
VI. Operating income	9,457	7,758	4,598	2,194	2,589	3,398	4,598	1,428
VII. Earnings from continuous activities	6,452	5,489	3,583	1,989	2,357	2,960	3,583	1,467
VIII. Net earnings of the period	6,452	5,489	3,583	1,989	2,357	2,960	3,583	1,467

1 Accumulated data from the beginning of the year to the last day of every quarter. It includes companies removed throughout the year.

2 Available data: January 2013.

3 IIC: Instituciones de Inversión Colectiva / CIS: Collective Investment Schemes.

Aggregated income statement. Portfolio management companies

TABLE 2.10

Thousand euro ¹	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
I. Interest income	407	682	733	215	390	559	733	86
II. Net commission	10,097	7,988	7,879	1,873	3,832	5,921	7,879	645
Commission revenues	20,994	18,477	17,887	4,428	8,864	13,408	17,887	1,520
Portfolio management	18,020	16,582	16,307	4,078	8,115	12,168	16,307	1,417
Design and advising	1,160	1,894	1,579	350	749	1,240	1,579	103
IICs ³ marketing	34	0	0	0	0	0	0	0
Other	1,779	0	0	0	0	0	0	0
Commission expenses	10,897	10,489	10,008	2,555	5,032	7,487	10,008	875
III. Financial investment income	51	186	4	-19	-51	-41	4	12
IV. Net exchange differences and other operating products and expenses	22	-11	-1	-3	48	9	-1	3
V. Gross income	10,577	8,845	8,615	2,066	4,219	6,448	8,615	746
VI. Operating income	1,154	1,526	1,406	263	639	1,071	1,406	189
VII. Earnings from continuous activities	939	1,042	953	195	439	728	953	135
VIII. Net earnings of the period	939	1,042	953	195	439	728	953	135

1 Accumulated data from the beginning of the year to the last day of every quarter. It includes companies removed throughout the year.

2 Available data: January 2013.

3 IIC: Instituciones de Inversión Colectiva / CIS: Collective Investment Schemes.

Surplus equity over capital adequacy requirements¹

TABLE 2.11

Thousand euro	Surplus		Number of companies according to its surplus percentage									
	Total											
	amount	% ²	<50	<100	<150	<200	<300	<400	<500	<750	<1000	>1000
Total	1,101,120	306.85	18	19	9	5	11	12	4	7	2	6
Broker-dealers	1,033,147	336.43	4	3	7	3	8	8	3	4	1	5
Brokers	53,318	160.61	13	14	2	2	2	3	1	3	0	1
Portfolio management companies	14,655	79.01	1	2	0	0	1	1	0	0	1	0

1 Available data: December 2012.

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.

Return on equity (ROE) before taxes^{1,2}

TABLE 2.12

	Average ³	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	3.19	31	16	17	13	11	2	1	0	2	
Broker-dealers	2.97	14	10	8	7	4	2	0	0	1	
Brokers	6.25	15	5	6	6	7	0	1	0	1	
Portfolio management companies	4.23	2	1	3	0	0	0	0	0	0	

1 ROE has been calculated as:

$$ROE = \frac{\text{Earnings before taxes (annualized)}}{\text{Own Funds}}$$

Own Funds = Share capital + Paid-in surplus + Reserves – Own shares + Prior year profits and retained earnings – Interim dividend.

2 Available data: December 2012.

3 Average weighted by equity, %.

Financial advisory firms. Main figures

TABLE 2.13

Thousand euro	2009	2010	2011	2011		2012	
				I	II	I	II
ASSETS ADVISED¹							
Total	1,410,985	15,802,743	16,033,109	16,498,814	16,033,109	14,663,856	14,769,051
Retail clients	364,284	1,715,084	2,181,943	1,895,320	2,181,943	2,415,002	3,259,987
Professional	1,046,702	13,995,206	13,831,973	14,501,823	13,831,973	12,205,216	11,454,933
Other	0	92,453	19,193	101,671	19,193	43,638	54,132
COMMISSION INCOME²							
Total	3,183	20,745	31,052	14,116	31,052	13,940	25,828
Commission revenues	3,183	20,629	30,844	14,080	30,844	13,855	25,653
Other income	0	116	209	36	209	85	175
EQUITY							
Total	1,500	10,057	12,320	10,469	12,320	13,098	15,249
Share capital	1,043	3,014	3,895	3,386	3,895	4,328	4,485
Reserves and retained earnings	36	242	950	2,915	950	5,904	7,139
Income for the year ²	421	6,801	7,474	4,168	7,474	2,866	3,626

1 Data at the end of each period. Half-yearly.

2 Accumulated data from the beginning of the year to the last day of every semester.

3 Collective investment schemes (IICs)^{a,b}

Number, management companies and depositories of collective investment schemes registered at the CNMV

TABLE 3.1

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
Total financial IICs	5,627	5,460	5,246	5,402	5,373	5,293	5,246	5,222
Mutual funds	2,429	2,341	2,205	2,306	2,284	2,224	2,205	2,195
Investment companies	3,133	3,056	2,981	3,033	3,025	3,007	2,981	2,970
Funds of hedge funds	32	27	24	27	28	26	24	24
Hedge funds	33	36	36	36	36	36	36	33
Total real estate IICs	16	14	14	14	14	14	14	15
Real estate investment funds	8	6	6	6	6	6	6	6
Real estate investment companies	8	8	8	8	8	8	8	9
Total foreign IICs marketed in Spain	660	739	754	765	743	749	754	753
Foreign funds marketed in Spain	379	426	421	443	421	418	421	418
Foreign companies marketed in Spain	281	313	333	322	322	331	333	335
Management companies	123	114	105	112	110	110	105	105
IIC depositories	114	97	84	92	90	87	84	83

1 Available data: February 2013.

Number of IICs investors and shareholders

TABLE 3.2

	2010	2011	2012	2012				2013
				I	II	III	IV ¹	I ²
Total financial IICs	5,578,524	5,249,813	4,815,732	5,173,640	5,046,010	4,939,311	4,815,732	4,841,318
Mutual funds	5,160,889	4,835,193	4,410,741	4,759,243	4,634,772	4,531,940	4,410,741	4,437,321
Investment companies	417,635	414,620	404,991	414,397	411,238	407,371	404,991	403,997
Total real estate IICs	76,223	30,678	26,155	30,693	28,655	28,522	26,155	26,147
Real estate investment funds	75,280	29,735	25,218	29,754	27,716	27,587	25,218	25,226
Real estate investment companies	943	943	937	939	939	935	937	921
Total foreign IICs marketed in Spain ³	865,767	761,380	816,417	768,467	788,852	819,014	817,309	–
Foreign funds marketed in Spain	193,233	177,832	162,363	175,621	179,987	186,613	163,255	–
Foreign companies marketed in Spain	666,534	583,548	654,054	592,846	608,865	632,401	654,054	–

1 Provisional data for foreign IICs.

2 Available data: January 2013.

3 Exchange traded funds (ETFs) data is not included.

IICs total net assets

TABLE 3.3

Million euro	2010	2011	2012	2012				2013
				I	II	III	IV ¹	I ²
Total financial IICs	170,073.1	155,982.6	147,729.8	156,460.3	148,594.6	149,122.7	147,729.8	150,584.8
Mutual funds ³	143,918.2	132,368.6	124,039.9	131,994.5	125,120.7	125,108.2	124,039.9	126,479.6
Investment companies	26,155.0	23,614.0	23,689.9	24,465.8	23,473.9	24,014.5	23,689.9	24,105.1
Total real estate IICs	6,437.5	4,807.1	4,485.5	4,757.7	4,691.2	4,608.6	4,485.5	4,991.1
Real estate investment funds	6,115.6	4,494.6	4,201.5	4,446.9	4,386.0	4,313.9	4,201.5	4,160.8
Real estate investment companies	321.9	312.5	284.1	310.8	305.1	294.7	284.1	830.3
Total foreign IICs marketed in Spain ⁴	36,692.9	29,969.5	37,990.7	31,835.1	34,537.8	38,359.2	37,990.7	–
Foreign funds marketed in Spain	8,535.9	6,382.9	6,248.7	6,583.3	7,188.4	7,571.7	6,248.7	–
Foreign companies marketed in Spain	28,156.9	23,586.6	31,742.0	25,251.9	27,349.4	30,787.5	31,742.0	–

1 Provisional data for foreign IICs.

2 Available data: January 2013.

3 For September 2012, mutual funds investments in financial IICs reached 3.0 billion euro.

4 Exchange traded funds (ETFs) data is not included.

a IICs: Instituciones de Inversión Colectiva / CIS: Collective Investment Schemes.

b In this document, neither hedge funds nor funds of hedge funds are included in the figures referred to mutual funds.

Mutual funds asset allocation¹

TABLE 3.4

Million euro	2010	2011	2012	2011	2012	II	III	IV ²
				IV	I			
Asset	143,918.2	132,368.6	124,039.9	132,368.6	131,994.5	125,120.7	125,108.2	124,039.9
Portfolio investment	137,295.4	126,370.0	118,444.3	126,370.0	125,415.1	119,257.1	119,558.0	118,444.3
Domestic securities	89,630.2	90,394.3	82,930.7	90,394.4	88,306.4	83,543.1	83,428.6	82,930.7
Debt securities	68,575.1	72,076.1	66,001.7	72,076.2	71,341.5	67,492.7	67,268.3	66,001.7
Shares	3,829.2	3,087.0	3,140.8	3,087.0	2,896.1	2,812.9	2,942.0	3,140.8
Investment collective schemes	7,338.6	6,038.5	3,172.1	6,038.5	3,827.9	3,566.2	3,326.8	3,172.1
Deposits in Credit institutions	9,460.8	8,961.2	10,340.1	8,961.2	10,049.9	9,415.4	9,650.0	10,340.1
Derivatives	426.2	231.5	276.0	231.5	191.0	256.0	241.6	276.0
Other	0.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign securities	47,626.5	35,968.1	35,509.4	35,968.1	37,097.8	35,708.0	36,123.3	35,509.4
Debt securities	30,337.4	22,713.5	20,491.2	22,713.6	22,699.0	21,937.0	21,553.5	20,491.2
Shares	8,385.8	7,037.3	7,668.6	7,037.3	7,443.8	7,069.7	7,452.0	7,668.6
Investment collective schemes	8,404.7	6,061.6	7,110.9	6,061.6	6,746.4	6,485.3	6,928.3	7,110.9
Deposits in Credit institutions	108.0	23.0	45.8	23.0	58.8	59.8	37.4	45.8
Derivatives	387.1	131.6	192.3	131.6	149.1	154.7	151.5	192.3
Other	3.6	1.1	0.6	1.1	0.7	1.5	0.6	0.6
Doubtful assets and matured investment	38.6	7.5	4.2	7.5	10.9	6.0	6.1	4.2
Intangible assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net fixed assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cash	6,531.4	5,837.6	5,367.8	5,837.6	6,398.4	5,630.4	5,324.0	5,367.8
Net balance (Debtors - Creditors)	91.4	161.1	227.8	161.1	181.0	233.3	226.2	227.8

1 Hedge funds and funds of hedge funds are not included in these figures due to the entry into force, on 31 December 2008, of Circular CR CNMV 3/2008 which establishes a different deadline in reporting accounting information to CNMV.

2 Provisional data.

Investment companies asset allocation

TABLE 3.5

Million euro	2010	2011	2012	2011	2012	II	III	IV ¹
				IV	I			
Asset	26,155.0	23,614.0	23,689.9	23,614.0	24,465.8	23,473.9	24,014.5	23,689.9
Portfolio investment	25,187.3	22,521.9	22,520.3	22,521.9	23,175.1	22,149.6	22,300.8	22,520.3
Domestic securities	12,881.4	12,385.3	11,571.0	12,385.3	12,695.2	11,613.0	11,196.4	11,571.0
Debt securities	5,435.9	7,460.8	6,021.8	7,460.8	7,415.3	7,006.9	6,562.6	6,021.8
Shares	2,988.6	2,508.5	2,273.6	2,508.5	2,385.9	2,275.2	2,149.5	2,273.6
Investment collective schemes	758.7	667.4	701.6	667.4	694.0	646.1	650.7	701.6
Deposits in Credit institutions	3,675.2	1,721.7	2,532.1	1,721.7	2,164.7	1,649.6	1,794.8	2,532.1
Derivatives	-5.9	-5.2	7.7	-5.2	1.9	1.4	4.0	7.7
Other	29.0	32.2	34.3	32.2	33.4	33.9	34.6	34.3
Foreign securities	12,298.1	10,131.1	10,945.0	10,131.1	10,473.9	10,531.5	11,100.0	10,945.0
Debt securities	3,606.8	3,070.6	2,489.9	3,070.6	2,966.6	3,024.4	2,972.9	2,489.9
Shares	4,166.0	3,384.3	3,589.5	3,384.3	3,493.5	3,345.4	3,433.4	3,589.5
Investment collective schemes	4,390.5	3,516.3	4,700.8	3,516.3	3,840.0	3,997.7	4,523.9	4,700.8
Deposits in Credit institutions	12.1	10.8	15.9	10.8	13.8	12.1	11.0	15.9
Derivatives	119.9	145.1	147.1	145.1	156.3	147.6	154.6	147.1
Other	2.8	3.9	1.8	3.9	3.9	4.2	4.2	1.8
Doubtful assets and matured investment	7.9	5.5	4.3	5.5	6.0	5.1	4.4	4.3
Intangible assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net fixed assets	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Cash	832.0	854.6	959.8	854.6	1,071.7	1,030.2	1,530.9	959.8
Net balance (Debtors - Creditors)	135.5	237.4	209.8	237.4	218.8	294.0	182.7	209.8

1 Provisional data.

Financial mutual funds: number, investors and total net assets by category¹

TABLE 3.6

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
NO. OF FUNDS								
Total financial mutual funds	2,408	2,310	2,185	2,300	2,255	2,197	2,185	2,173
Fixed-income ³	537	508	454	491	479	459	454	452
Mixed fixed-income ⁴	160	140	125	140	132	128	125	125
Mixed equity ⁵	138	128	117	130	122	119	117	117
Euro equity	172	148	127	143	135	129	127	125
Foreign equity	232	220	211	222	220	214	211	210
Guaranteed fixed-income	276	351	398	375	385	393	398	402
Guaranteed equity ⁶	499	420	361	404	384	369	361	352
Global funds	192	203	192	200	198	194	192	187
Passive management	61	59	85	64	75	75	85	88
Absolute return	141	133	115	131	125	117	115	115
INVESTORS								
Total financial mutual funds	5,160,889	4,835,193	4,410,741	4,759,243	4,634,772	4,531,940	4,410,741	4,437,321
Fixed-income ³	1,622,664	1,384,946	1,261,634	1,362,443	1,326,504	1,297,686	1,261,634	1,264,679
Mixed fixed-income ⁴	270,341	206,938	188,574	204,653	195,137	193,992	188,574	189,524
Mixed equity ⁵	171,336	145,150	138,096	145,472	141,784	140,387	138,096	138,606
Euro equity	266,395	237,815	220,433	224,886	225,774	220,342	220,433	226,572
Foreign equity	501,138	448,539	398,664	442,753	432,816	417,276	398,664	398,524
Guaranteed fixed-income	790,081	1,042,658	1,075,852	1,071,544	1,070,002	1,082,897	1,075,852	1,090,591
Guaranteed equity ⁶	1,065,426	912,298	727,867	874,249	832,332	783,203	727,867	716,286
Global funds	105,720	127,336	101,321	113,396	105,966	105,824	101,321	101,283
Passive management	90,343	100,416	125,003	101,901	108,166	110,678	125,003	138,854
Absolute return	277,445	229,097	173,297	217,946	196,291	179,655	173,297	172,402
TOTAL NET ASSETS (million euro)								
Total financial mutual funds	143,918.2	132,368.6	124,039.9	131,994.5	125,120.7	125,108.2	124,039.9	126,479.6
Fixed-income ³	56,614.6	46,945.5	40,664.6	45,101.8	42,837.8	41,512.2	40,664.6	41,089.4
Mixed fixed-income ⁴	7,319.0	5,253.6	5,500.9	5,686.9	5,430.9	5,512.9	5,500.9	5,625.0
Mixed equity ⁵	3,470.5	2,906.1	3,179.9	3,234.2	3,040.3	3,116.2	3,179.9	3,329.3
Euro equity	5,356.8	4,829.2	5,270.2	4,815.6	4,516.5	4,891.7	5,270.2	5,581.6
Foreign equity	8,037.3	6,281.2	6,615.0	6,813.2	6,373.7	6,663.2	6,615.0	6,748.1
Guaranteed fixed-income	26,180.2	35,058.0	36,445.0	36,677.0	35,421.7	36,489.9	36,445.0	37,243.3
Guaranteed equity ⁶	22,046.5	18,014.5	14,412.7	17,408.5	15,943.0	15,383.0	14,412.7	14,279.3
Global funds	4,440.3	5,104.7	4,358.6	4,545.5	4,272.1	4,288.4	4,358.6	4,424.3
Passive management	2,104.8	1,986.2	2,991.2	2,053.9	2,190.9	2,456.2	2,991.2	3,509.6
Absolute return	8,348.1	5,989.7	4,601.9	5,657.8	5,093.9	4,794.4	4,601.9	4,649.9

1 Mutual funds which have sent reports to the CNMV, excluding those in process of dissolution or liquidation.

2 Available data: January 2013.

3 From III 2011 on includes: Fixed income euro, Foreign fixed-income, Monetary market funds and Short-term monetary market funds. Until II 2011 included: Fixed income euro, Foreign fixed-income and Monetary market funds.

4 Mixed euro fixed-income and Foreign mixed fixed-income.

5 Mixed euro equity and Foreign mixed equity.

6 Guaranteed equity and partial guarantee.

Financial mutual funds: Detail of investors and total net assets by type of investors

TABLE 3.7

	2010	2011	2012	2012				2013
				I	II	III	IV	I ¹
INVESTORS								
Total financial mutual funds	5,160,889	4,835,193	4,410,741	4,759,243	4,634,772	4,531,940	4,410,741	4,437,321
Individuals	5,019,902	4,706,193	4,293,058	4,632,866	4,509,469	4,410,151	4,293,058	4,318,808
Residents	4,954,891	4,645,384	4,237,521	4,572,796	4,451,177	4,353,203	4,237,521	4,263,297
Non-residents	65,011	60,809	55,537	60,070	58,292	56,948	55,537	55,511
Legal entities	140,987	129,000	117,683	126,377	125,303	121,789	117,683	118,513
Credit Institutions	524	490	473	502	492	485	473	486
Other resident Institutions	139,550	127,765	116,572	125,169	124,123	120,632	116,572	117,344
Non-resident Institutions	913	745	638	706	688	672	638	683
TOTAL NET ASSETS (million euro)								
Total financial mutual funds	143,918.1	132,368.6	124,039.9	131,994.5	125,120.7	125,108.2	124,039.9	126,479.6
Individuals	113,660.6	106,627.6	101,963.3	108,015.5	102,223.9	102,386.1	101,963.3	104,026.9
Residents	111,900.1	105,088.0	100,515.3	106,439.7	100,763.1	100,914.7	100,515.3	102,563.5
Non-residents	1,760.5	1,539.6	1,448.0	1,575.7	1,460.9	1,471.4	1,448.0	1,463.4
Legal entities	30,257.5	25,741.1	22,076.6	23,979.1	22,896.8	22,722.0	22,076.6	22,452.7
Credit Institutions	1,926.1	1,446.7	1,075.4	1,373.5	1,274.6	1,258.3	1,075.4	917.5
Other resident Institutions	27,644.6	23,880.7	20,657.1	22,223.1	21,259.1	21,116.5	20,657.1	21,173.2
Non-resident Institutions	686.9	413.7	344.1	382.5	363.1	347.2	344.1	362.0

1 Available data: January 2013.

Subscriptions and redemptions of financial mutual funds by category¹

TABLE 3.8

Million euro	2010	2011	2012	2011		2012		
				IV	I	II	III	IV
SUBSCRIPTIONS								
Total financial mutual funds	78,805.2	58,145.0	50,968.1	11,231.9	12,932.8	11,089.10	18,221.5	8,724.7
Fixed-income	41,656.1	27,206.2	32,904.2	6,875.0	7,776.1	5,877.50	14,366.3	4,884.3
Mixed fixed-income	3,538.8	1,332.4	1,423.8	224.7	358.9	362.7	310.6	391.6
Mixed equity	1,221.7	815.7	589.0	166.0	101.5	195.1	94.7	197.7
Euro equity	1,673.0	2,085	1,261.0	513.6	284.5	354.1	312.1	310.3
Foreign equity	4,455.2	3,835.1	1,693.8	303.8	561.2	385.1	393.4	354.1
Guaranteed fixed-income	11,513.4	13,965.7	7,972.7	1,743.7	2,340.3	2,535.10	1,851.5	1,245.8
Guaranteed equity	5,120.1	2,570.7	1,419.9	368.7	474.4	494.1	272.4	179
Global funds	3,018.1	3,261.6	1,270.6	316.5	468.3	295.5	168.6	338.2
Passive management	683.8	924.7	1,402.2	357.9	249.6	366.8	263.6	522.2
Absolute return	5,924.8	2,147.7	1,031.0	362.0	318.1	223.1	188.3	301.5
REDEMPTIONS								
Total financial mutual funds	104,385.6	68,983.6	62,463.7	14,519.2	14,585.3	14,184.90	21,398.1	12,295.4
Fixed-income	68,806.1	37,633.9	38,566.7	8,405.7	8,503.0	7,658.80	16,247.2	6,157.7
Mixed fixed-income	4,955.7	3,258.1	2,075.4	674.4	596.8	486.3	484.2	508.1
Mixed equity	1,311.8	1,136.2	870.6	240.8	235.5	221.1	163.0	251
Euro equity	2,369.9	1,933.0	1,370.7	465.7	436.0	286.3	314.2	334.2
Foreign equity	3,303.3	4,652.7	2,064.0	489.1	575.2	498.9	449.3	540.6
Guaranteed fixed-income	6,797.4	6,737.4	8,307.2	1,350.4	1,756.2	2,537.70	1,793.0	2,220.3
Guaranteed equity	7,620.2	5,632.3	4,773.0	934.0	1,206.0	1,194.70	1,077.5	1,294.8
Global funds	2,694.4	2,316.3	1,278.4	576.9	310.4	367.6	269.7	330.7
Passive management	1,474.1	1,199.2	830.1	553.1	220.3	252.2	195.8	161.8
Absolute return	5,053.0	4,484.7	2,327.5	829.2	745.8	681.3	404.2	496.2

1 Estimated data.

Financial mutual funds asset change by category: Net subscriptions/redemptions and return on assets

TABLE 3.9

Million euro	2010	2011	2012	2011	2012	II	III	IV
				IV	I			
NET SUBSCRIPTIONS/REDEMPTIONS								
Total financial mutual funds	-25,580.6	-10,853.1	-14,597.3	-3,282.4	-3,421.1	-4,419.4	-3,177.2	-3,579.6
Fixed-income	-27,149.9	-10,423.6	-7,737.3	-1,538.6	-2,496.5	-2,060.0	-1,885.4	-1,295.4
Mixed fixed-income	-1,417.0	-1,980.4	-18.8	-521.6	302.2	-167.8	-46.1	-107.1
Mixed equity	-90.0	-375.5	35.8	-73.9	219.8	-100.8	-45.2	-38.0
Euro equity	-696.9	142.0	-115.4	49.7	-171.8	18.2	13.5	24.7
Foreign equity	1,152.1	-796.0	-425.3	-185.1	-17.2	-180.8	-38.6	-188.7
Guaranteed fixed-income	4,716.0	7,809.3	-338.8	569.5	749.0	-430.5	215.7	-873.0
Guaranteed equity	-2,500.1	-4,053.9	-4,225.9	-785.2	-896.4	-1,030.4	-1,040.2	-1,258.9
Global funds	323.6	972.2	-1,021.0	-187.8	-710.2	-199.8	-105.5	-5.5
Passive management	-790.3	60.8	823.8	-146.9	30.2	233.6	140.0	420.0
Absolute return	871.7	-2,207.9	-1,571.9	-462.5	-430.2	-501.0	-385.4	-255.3
RETURN ON ASSETS								
Total financial mutual funds	135.7	-673.3	6,288.9	1,622.1	3,053.1	-2,452.8	3,175.6	2,513.0
Fixed-income	64.5	744.9	1,457.2	258.2	653.0	-203.9	560.1	448.0
Mixed fixed-income	-56.4	-85.1	266.1	59.4	131.1	-88.2	128.2	95.0
Mixed equity	-53.4	-189.0	238.2	82.5	108.3	-93.0	121.1	101.8
Euro equity	-254.1	-666.9	558.8	170.1	158.2	-316.1	361.8	354.9
Foreign equity	877.4	-947.2	759.1	437.9	549.2	-258.8	328.2	140.5
Guaranteed fixed-income	-170.4	1,070.4	1,727.4	247.5	870.5	-824.3	852.8	828.4
Guaranteed equity	-392.8	21.8	624.0	99.7	290.5	-435.2	480.2	288.5
Global funds	123.1	-307.8	274.9	138.2	151.1	-73.7	121.8	75.7
Passive management	-109.7	-163.9	196.8	73.1	42.7	-96.5	135.6	115.0
Absolute return	107.7	-150.5	184.1	55.4	98.4	-63.0	85.8	62.9

Financial mutual funds return on assets. Detail by category

TABLE 3.10

% of daily average total net assets	2010	2011	2012	2011	2012	II	III	IV
				IV	I			
MANAGEMENT YIELDS								
Total financial mutual funds	1.09	0.45	6.03	1.47	2.56	-1.73	2.83	2.31
Fixed-income	0.78	2.28	4.33	0.74	1.65	-0.3	1.58	1.34
Mixed fixed-income	0.61	-0.15	6.05	1.41	2.59	-1.33	2.65	2.06
Mixed equity	0.11	-4.30	9.2	3.28	3.71	-2.67	4.34	3.68
Euro equity	-3.05	-10.77	12.84	4.07	3.7	-6.4	8.15	7.49
Foreign equity	14.8	-11.05	13.51	7.55	8.7	-3.51	5.48	2.6
Guaranteed fixed-income	-0.11	3.77	5.3	0.85	2.51	-2.3	2.58	2.5
Guaranteed equity	-0.46	1.29	5.26	0.87	1.97	-2.34	3.36	2.26
Global funds	4.15	-4.55	7.8	2.97	3.79	-1.42	3.18	2.11
Passive management	-2.50	-6.27	7.99	3.98	2.38	-4.46	5.92	4.23
Absolute return	2.49	-0.90	4.93	1.2	1.99	-0.9	2.11	1.67
EXPENSES. MANAGEMENT FEE								
Total financial mutual funds	0.91	0.93	0.94	0.24	0.24	0.23	0.23	0.24
Fixed-income	0.65	0.64	0.66	0.16	0.17	0.16	0.16	0.17
Mixed fixed-income	1.20	1.17	1.1	0.3	0.29	0.27	0.27	0.27
Mixed equity	1.65	1.59	1.51	0.4	0.39	0.38	0.37	0.36
Euro equity	1.78	1.80	1.77	0.45	0.44	0.44	0.44	0.44
Foreign equity	1.84	1.77	1.74	0.45	0.47	0.43	0.41	0.42
Guaranteed fixed-income	0.62	0.72	0.79	0.19	0.19	0.19	0.2	0.21
Guaranteed equity	1.24	1.24	1.23	0.31	0.3	0.3	0.31	0.31
Global funds	1.06	1.11	1.01	0.28	0.33	0.23	0.23	0.22
Passive management	0.72	0.75	0.81	0.21	0.22	0.2	0.2	0.19
Absolute return	1.06	1.08	1.03	0.28	0.3	0.26	0.23	0.24
EXPENSES. DEPOSITORY FEE								
Total financial mutual funds	0.09	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Fixed-income	0.08	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Mixed fixed-income	0.10	0.12	0.08	0.03	0.02	0.02	0.02	0.02
Mixed equity	0.12	0.12	0.12	0.03	0.03	0.03	0.03	0.03
Euro equity	0.11	0.12	0.12	0.03	0.03	0.03	0.03	0.03
Foreign equity	0.12	0.12	0.12	0.03	0.03	0.03	0.03	0.03
Guaranteed fixed-income	0.07	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Guaranteed equity	0.10	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Global funds	0.09	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Passive management	0.07	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Absolute return	0.08	0.08	0.08	0.02	0.02	0.02	0.02	0.02

Mutual funds quarterly returns. Detail by category

TABLE 3.11

In %	2010	2011	2012	2011	2012	II	III	IV
				IV	I			
Total financial mutual funds	0.35	-0.08	5.50	1.35	2.41	-1.75	2.72	2.08
Fixed-income	0.11	1.56	3.54	0.58	1.51	-0.47	1.35	1.12
Mixed fixed-income	-0.54	-1.34	4.95	1.20	2.3	-1.55	2.41	1.75
Mixed equity	-0.98	-5.64	7.83	3.02	3.25	-2.9	4.12	3.3
Euro equity	-2.94	-11.71	12.31	4.05	3.34	-6.34	8.16	7.28
Foreign equity	14.22	-10.83	13.05	7.53	8.91	-3.63	5.27	2.32
Guaranteed fixed-income	-0.67	3.28	4.85	0.71	2.48	-2.32	2.42	2.27
Guaranteed equity	-1.79	0.14	5.07	0.68	1.63	-2.43	3.89	1.99
Global funds	3.22	-4.64	7.44	2.90	3.56	-1.23	2.95	2.03
Passive management	-2.36	-7.33	7.1	4.11	1.97	-4.31	5.50	4.04
Absolute return	1.53	-1.87	3.84	0.93	1.68	-1.04	1.81	1.36

Hedge funds and funds of hedge funds

TABLE 3.12

	2009	2010	2011	2011	2012			
				IV	I	II	III	IV ¹
HEDGE FUNDS								
Investors/shareholders	1,917	1,852	2,047	2,047	2,077	2,169	2,305	2,304
Total net assets (million euro)	652.0	646.2	728.1	728.1	775.3	774.5	828.7	838.1
Subscriptions (million euro)	248.7	236.6	201.1	50.5	71.5	60.7	83.0	34.9
Redemptions (million euro)	198.3	268.6	92.5	39.0	49.8	41.9	52.5	35.7
Net subscriptions/redemptions (million euro)	50.4	-32.0	108.6	11.5	21.7	18.7	30.5	-0.9
Return on assets (million euro)	62.2	26.3	-26.5	12.8	25.5	-19.6	23.8	10.2
Returns (%)	14.94	5.37	-2.60	2.16	3.66	-2.42	2.72	1.29
Management yields (%) ²	13.76	6.33	-1.88	2.16	3.68	-1.65	2.51	1.07
Management fee (%) ²	2.55	1.91	1.66	0.38	0.38	0.37	0.32	0.22
Financial expenses (%) ²	0.11	0.07	0.06	0.01	0.01	0.01	0.01	0.00
FUNDS OF HEDGE FUNDS								
Investors/shareholders	5,321	4,404	3,805	3,805	3,592	3,607	3,513	3,385
Total net assets (million euro)	810.2	694.9	573.0	573.0	568.0	561.4	561.3	545.8
Subscriptions (million euro)	302.4	47.9	10.6	2.2	2.0	7.4	13.7	-
Redemptions (million euro)	585.4	184.8	120.1	51.1	13.5	13.3	21.2	-
Net subscriptions/redemptions (million euro)	-283.0	-136.9	-109.6	-48.9	-11.5	-5.9	-7.5	-
Return on assets (million euro)	71.9	21.7	-12.3	4.5	6.4	-0.7	9.4	-
Returns (%)	7.85	3.15	-1.70	0.85	1.15	-2.21	1.36	0.40
Management yields (%) ³	11.54	4.38	-0.47	1.09	1.45	0.16	1.66	-
Management fee (%) ³	1.34	1.25	1.25	0.31	0.32	0.30	0.32	-
Depository fee (%) ³	0.11	0.08	0.08	0.02	0.02	0.02	0.02	-

1 Available data: November 2012. Return refers to the period September-November.

2 % of monthly average total net assets.

3 % of daily average total net assets.

Management companies. Number of portfolios and assets under management¹

TABLE 3.13

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
NUMBER OF PORTFOLIOS								
Mutual funds	2,429	2,341	2,205	2,306	2,284	2,224	2,205	2,196
Investment companies	3,068	3,002	3,002	2,975	2,967	2,949	3,002	2,921
Funds of hedge funds	32	27	24	27	28	26	24	24
Hedge funds	31	35	35	35	35	35	35	33
Real estate investment fund	8	6	6	6	6	6	6	6
Real estate investment companies	8	8	8	8	8	8	8	9
ASSETS UNDER MANAGEMENT (million euro)								
Mutual funds	143,918.2	132,368.6	124,039.9	131,994.5	125,120.7	125,108.2	124,039.9	126,479.6
Investment companies	25,361.3	23,037.8	22,773.2	23,827.4	22,849.4	23,363.1	22,773.2	23,504.9
Funds of hedge funds ³	694.9	573.0	545.8	568.0	561.4	561.3	545.8	-
Hedge funds ³	643.5	694.7	799.6	739.8	738.0	791.0	799.6	-
Real estate investment fund	6,115.6	4,494.6	4,201.5	4,446.9	4,386.0	4,313.9	4,201.5	4,160.8
Real estate investment companies	321.9	312.5	284.1	310.8	305.1	294.7	284.1	830.3

1 It is considered as "assets under management" all the assets of the investment companies which are co-managed by management companies and other different companies.

2 Available data: January 2013.

3 Available data for III Quarter 2012: November 2012.

Foreign Collective Investment schemes marketed in Spain¹

TABLE 3.14

	2010	2011	2012	2011	2012	II	III	IV ²
				IV	I			
INVESTMENT VOLUME³ (million euro)								
Total	36,692.9	29,969.5	37,990.7	29,969.5	31,835.1	34,537.8	38,359.2	37,990.7
Mutual funds	8,535.9	6,382.9	6,248.7	6,382.9	6,583.3	7,188.4	7,571.7	6,248.7
Investment companies	28,156.9	23,586.6	31,742.0	23,586.6	25,251.9	27,349.4	30,787.5	31,742.0
INVESTORS/SHAREHOLDERS								
Total	865,767	761,380	816,417	761,380	768,467	788,852	819,014	816,417
Mutual funds	193,233	177,832	162,363	177,832	175,621	179,987	186,613	162,363
Investment companies	666,534	583,548	654,054	583,548	592,846	608,865	632,401	654,054
NUMBER OF SCHEMES								
Total	660	739	754	739	765	743	749	754
Mutual funds	379	426	421	426	443	421	418	421
Investment companies	281	313	333	313	322	322	331	333
COUNTRY								
Luxembourg	290	297	310	297	303	302	308	310
France	225	284	272	284	300	278	279	272
Ireland	75	87	90	87	90	89	90	90
Germany	20	20	31	20	20	22	23	31
UK	16	19	22	19	20	21	21	22
The Netherlands	1	1	1	1	1	1	1	1
Austria	27	25	23	25	25	24	20	23
Belgium	5	5	3	5	5	5	5	3
Malta	1	1	1	1	1	1	1	1
Denmark	0	0	1	0	0	0	1	1

1 Exchange traded funds (ETFs) data is not included.

2 Provisional data.

3 Investment volume: participations or shares owned by the investors/shareholders at the end of the period valued at that moment.

Real estate investment schemes¹

TABLE 3.15

	2010	2011	2012	2012				2013
				I	II	III	IV	I ²
REAL ESTATE MUTUAL FUNDS								
Number	7	6	6	6	6	6	6	6
Investors	75,280	29,735	25,218	29,754	27,716	27,587	25,218	25,226
Asset (million euro)	6,115.6	4,494.6	4,201.5	4,446.9	4,386.0	4,313.9	4,201.5	4,160.8
Return on assets (%)	-4.74	-3.23	-5.55	-0.85	-1.23	-1.64	-1.93	-1.00
REAL ESTATE INVESTMENT COMPANIES								
Number	8	8	8	8	8	8	8	9
Shareholders	943	943	937	939	939	935	937	921
Asset (million euro)	321.9	312.5	284.1	310.8	305.1	294.7	284.1	830.3

1 Real estate investment schemes which have sent reports to the CNMV, excluding those in process of dissolution or liquidation.

2 Available data: January 2013. In this case, return on assets is monthly.

