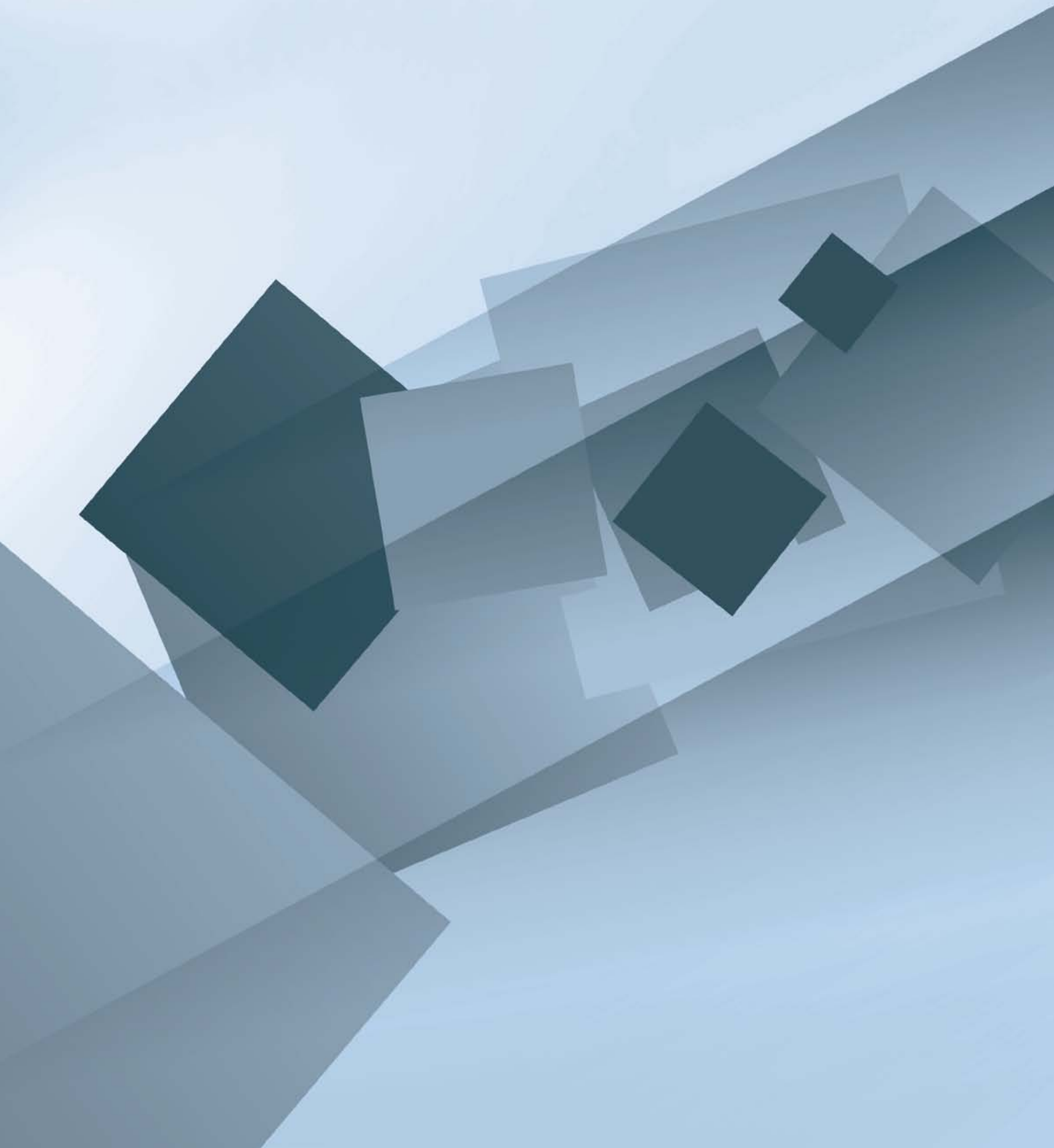




CNMV BULLETIN
Quarter III
2011



CNMV Bulletin

**Quarter III
2011**

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

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Table of contents

I	Securities markets and their agents: situation and outlook	9
II	Reports and Analyses	65
	Return on Spanish investment funds: an analysis of its determinants	67
	M ^a Isabel Cambón Murcia	
	The use of ratings in financial regulation: measures and proposals	85
	Ramiro Losada López	
III	Regulatory Novelties	99
	Modifications to the securities market as a result of the Sustainable Economy Act	101
	Adela Aguilar, Fernando Ibáñez and Ángel Domínguez	
	European Securities and Markets Authority	121
	Josefina Munuera Cebrián and Ángeles Martín de Diego	
IV	Legislative Annex	145
V	Statistics Annex	153

Abbreviations

ABS	Asset Backed Securities
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 Organisation 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	Mercado Español de Futuros y Opciones Financieros (Spanish financial futures and options market)
MFAO	Mercado de Futuros del Aceite de Oliva y Opciones Financieros (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 capital variable (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 Tradable 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	32
3	Spanish markets	33
	3.1 Equity markets	33
	3.2 Fixed-income markets	41
4	Market agents	48
	4.1 Investment vehicles	48
	4.2 Investment firms	57
	4.3 UCITS management companies	61
	4.4 Other intermediaries: venture capital	63

List of exhibits

Exhibit 1:	“Dark liquidity: the new IOSCO principles”	22
Exhibit 2:	“The stockmarket flotation of Spanish savings banks”	27
Exhibit 3:	“The temporary ban on short selling”	35
Exhibit 4:	“Green Paper on the EU Corporate Governance Framework”	40
Exhibit 5:	“Asset Securitisation Markets: Joint Forum Recommendations”	44
Exhibit 6:	“Circular 3/2011 of 9 June modifying UCITS investment policies”	51
Exhibit 7:	“ESMA technical advice to the European Commission on level 2 implementing measures for the Alternative Investment Fund Managers Directive”	54

1 Executive summary

- The pace of the world economy slowed appreciably in the year's middle months in contrast to the 4.5% growth of the opening quarter, with some advanced economies among the weaker performers. Emerging market economies kept up a comfortable growth lead although they too experienced some loss of steam. Against this backdrop, evidence of the U.S.'s struggle to get its public finances under control, coupled with persistent concerns about Greece's public debt, brought renewed turbulence to international financial markets which reached its height during the first half of August. The downside risks for world economic growth, which augur a renewed downturn in the coming quarters, have been increasing over the past two months.
- Financial market stress bore down heavily on equity prices, with European banks particularly affected, and was also responsible for an upswing in volatility. Third-quarter losses on main stock markets ranged from 6.6% in the case of the Nasdaq to 25% in some European indices. In parallel, the rush into "safe-haven" assets intensified, with U.S., UK and German debt among the beneficiaries, alongside assets denominated in Swiss francs and, also, non-financial assets such as gold. The sovereign credit spreads of a growing list of European countries were pushed to historic highs, and were only restored to stability by the ECB's decision to buy European government bonds on secondary markets, and the adoption of new, national measures. At the closing date for this report,¹ market volatility was still running high.
- The Spanish economy expanded 0.2% in the year's second quarter, for a year-on-year rate of 0.7% – in both cases two points below the result posted in the previous quarter. The slowdown in domestic activity was less marked than in other European countries, though year-on-year growth again trailed the average for the euro area (1.6%). Unemployment rates stayed stuck above 20%, while Spanish inflation abated to 2.7% in August from the 3.5% peak of April, narrowing its differential versus the euro area to 0.2 percentage points. Figures for central government budgetary execution to the month of July square with the 2011 deficit reduction target, though the latest round of financial market turmoil unquestionably poses an upside risk for the public deficit and a downside risk for economic activity.
- The business environment for Spanish financial institutions remains complex in the extreme, given the prevailing weakness of domestic activity and the disruption suffered by wholesale markets, which has caused funding conditions to deteriorate sharply.

¹ 20 September.

- Non-financial listed companies increased their aggregate profits by 8% in the first-half period to 13.15 billion euros, while their aggregate debt dropped back 5.1%.
- Spanish stock markets' first-quarter gains gave way to a price correction that gained in intensity from end-July onwards. The Ibex 35, up by 7.3% to March, shed 2% of its value in the second quarter and a further 19% approximately in the third, a performance more or less mirroring that of indices elsewhere in Europe. Market volatility peaked at times above 65%, recalling the levels reached in May 2010 during the first wave of the Greek debt crisis. Here, as in the rest of Europe, the banks were hardest hit, though the temporary ban on short selling of financial shares, ordered last August by the CNMV in concert with other European supervisors, went some way to smoothing out price volatility. In this context, stock market turnover has contracted by 2.7% year-to-date, putting liquidity conditions under a degree of strain.
- Domestic fixed-income markets also moved on the turbulences afflicting European sovereign debt. These reached a new peak in early August, sending Spanish government yields and spreads back to highs. Following this, the ECB's secondary-market purchases of European bonds and the approval of other measures at national level restored a degree of calm that was to prove short-lived. In September, evidence of the weakness of world economic activity set the markets on edge once more and prompted a fresh ascent in Spanish bond yields and spreads, which by the deadline for this report were testing 360 bp over the German bond. Meantime, the volume of fixed-income issues registered with the CNMV shrank by 1.3% to 162 billion euros between January and September.
- Assets under management in investment funds dropped 2.5% in the first six months to just over 140 billion euros, as the redemption rush continued. Outflows were strongest in fixed-income funds albeit on a rather smaller scale than in previous semesters. Investment fund returns held in positive territory though here too investment policies marked the difference. The aggregate profits of UCITS management companies fell by 3.8% between January and June in consonance with the downtrend in industry assets. Strong competition from bank deposits continues to dull the sector's short-term recovery prospects and, furthermore, will likely persist in the foreseeable future.
- Investment firm business continued to labor under financial market turmoil throughout the first half of 2011, putting paid to hopes of a recovery in income flows from core industry services. The small advance in aggregate pre-tax profits (1.4% year-on-year) owed basically to extraordinary income coupled with operating cost containment. The number of loss-making firms rose slightly in the first-half period, though the volume of their losses tended to decrease. The sector's solvency conditions remained in the comfort zone.
- The report includes seven monographic exhibits:
 - The first runs through some of the issues raised by the recent trading boom in non-transparent securities market segments (dark liquidity) and the proposals made by IOSCO to mitigate its adverse impacts.

- The second describes the stockmarket flotation in July 2011 of Bankia and Banca Cívica as part of the restructuring of the Spanish financial system, setting out the criteria used by the CNMV in verifying both transactions.
- Exhibit three brings analytical considerations and empirical evidence to bear on the joint decision of 11 August by the securities market regulators of Spain, France, Italy and Belgium, under the coordinating aegis of ESMA, to impose a temporary ban on the creation or increase of short positions in certain financial shares.
- Exhibit four looks at the initiatives contained in the Green Paper on Corporate Governance published by the European Commission in April 2011, in order to improve the corporate governance of Europe's companies, focusing on those traded in regulated markets.
- The fifth exhibit reproduces the recently published recommendations of the Joint Forum to establish a regulatory framework that supports the re-establishment of a sustainable securitisation market.
- The sixth describes the main changes made by Circular 3/2011 modifying UCITS categories based on investment policy, in order to adapt the definition of money-market fund to the harmonised definition issued by the Committee of European Securities Regulators (CESR), now ESMA, and introduce certain technical improvements.
- Finally, the seventh exhibit describes the main thrust of ESMA's advice to the European Commission on the level 2 implementing measures of the Alternative Fund Managers Directive.

2 Macro-financial setting

2.1 International economic and financial developments

Since the latest edition of this report in the CNMV Quarterly Bulletin for the first quarter of 2011, the world macroeconomic and financial landscape has been perturbed by a new wave of European sovereign debt market tensions, extending this time to a larger number of euro-area nations, and anxieties about certain aspects of the U.S.'s federal debt management. All this in a context of faltering economic activity.

The international macro-financial setting is gripped by renewed turbulence.

So even though first-quarter figures showed world growth to be holding up well with rates close to 4.5%, the second quarter was characterised by a slowdown that was especially marked in the U.S. and some European economies, and will likely persist through the second half, according to the tenor of the latest indicators. The IMF is now projecting a 2011 advance of 4.0%, over one point less than in 2010, on account of the downturn in Japan (–0.5%), after the March earthquake, and the lesser growth momentum of emerging and certain advanced economies (see table 1).

World economic activity slows sharply in the year's middle months...

Gross domestic product (annual % change)

TABLE 1

	2007	2008	2009	2010	IMF(*)		OECD(*)	
					2011F	2012F	2011F	2012F
World	5.4	2.8	-0.7	5.1	4.0 (-0.3)	4.0 (-0.5)	-	-
United States	1.9	-0.3	-3.5	3.0	1.5 (-1.0)	1.8 (-0.9)	2.6 (+0.4)	3.1 (=)
Euro area	3.0	0.4	-4.3	1.8	1.6 (-0.4)	1.1 (-0.6)	2.0 (+0.3)	2.0 (=)
Germany	3.4	0.8	-5.1	3.6	2.7 (-0.5)	1.3 (-0.7)	3.4 (+0.9)	2.5 (+0.3)
France	2.2	-0.2	-2.6	1.4	1.7 (-0.4)	1.4 (-0.5)	2.2 (+0.6)	2.1 (+0.1)
Italy	1.5	-1.3	-5.2	1.3	0.6 (-0.4)	0.3 (-1.0)	1.1 (-0.2)	1.6 (=)
Spain	3.6	0.9	-3.7	-0.1	0.8 (=)	1.1 (-0.5)	0.9 (=)	1.6 (-0.2)
United Kingdom	2.7	-0.1	-4.9	1.4	1.1 (-0.4)	1.6 (-0.7)	1.4 (-0.3)	1.8 (-0.2)
Japan	2.4	-1.2	-6.3	4.0	-0.5 (+0.2)	2.3 (-0.6)	-0.9 (-2.6)	2.2 (+0.9)
Emerging	8.9	6.0	2.8	7.3	6.4 (-0.2)	6.1 (-0.3)	-	-

Source: IMF and OECD.

(*) Figures in brackets show the change over the previous published forecasts. IMF, forecasts published in September 2011 (versus June 2011). OECD, forecasts published May 2011 (versus November 2010).

...while inflation has tended to moderate, in Europe especially.

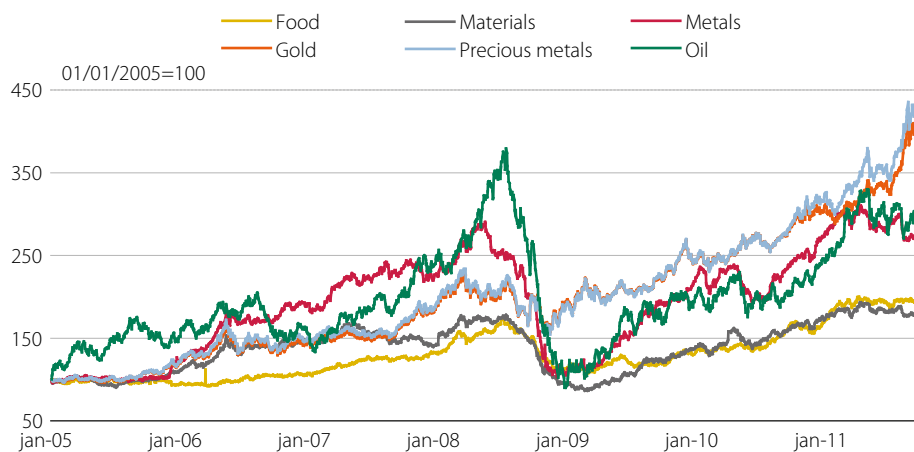
The world's main economies experienced a surge in inflation over the year's opening months, which tended to remit in the middle months, in some European countries at least. Commodity prices began to head gradually lower in the spring after two years of vigorous growth, the exception being precious metals (see figure 1). Inflationary pressures were strongest in the emerging economies on their greater output buoyancy, and were contested in many cases by hikes in official interest rates. Among the advanced economies, the big news was the ECB's decision to raise its benchmark rate by 25 bp on two occasions, to 1.25% in April and 1.5% in the month of July, after nearly two years without movement. Stateside, the Federal Reserve announced that it expected to keep rates at their current lows until 2013, in view of increasingly feeble domestic activity.

The upswing in uncertainty spells a new blow for world bond and equity markets...

Against this renewed backdrop of global macro-financial instability, stock markets began sinking rapidly, volatility surged to end-August highs in excess of 40% and a broad group of European countries saw their sovereign spreads escalate once more. Further, the rush into "safe-haven" assets, both financial as in the case of U.S., British and German bonds or instruments denominated in Swiss francs, or non-financial, as in the case of gold, continued to intensify. Approval of a new public spending ceiling in the United States, the adoption of additional consolidation measures in Europe's most vulnerable economies and the government bond purchases effected by the ECB from 8 August onwards, together with the joint decision by securities market regulators in Spain, France, Italy and Belgium to impose a temporary ban on the short selling of domestic financial sector shares, initially helped to drive down aggregate volatility. But come September, the confirmation of slowing world growth and fears of a restructuring of Greece's sovereign debt dealt a new blow to financial markets.

Commodity prices

FIGURE 1



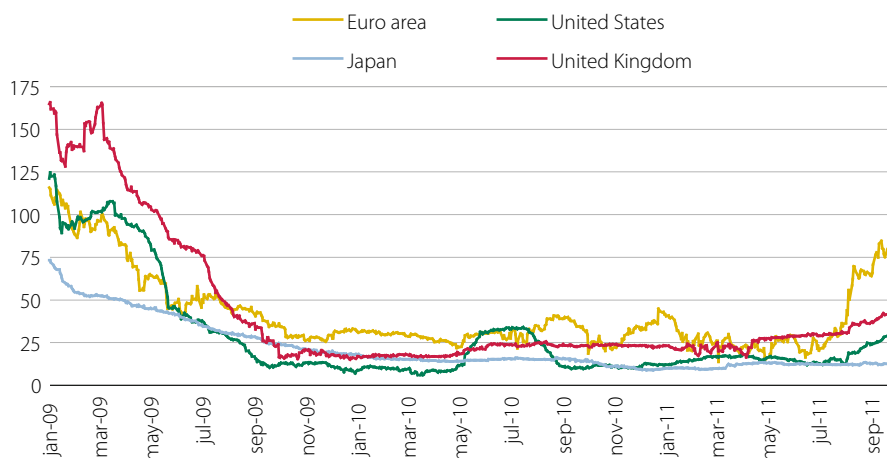
Source: Thomson Datastream. Data to 20 September.

The tensions gripping stock and bond market were also quick to drag in interbank trading. As we can see from figure 2, the three-month euro Libor-OIS spread widened significantly as of July from just under 25 basis points to mid-September highs testing 80 basis points, the highest level since spring 2009.

...and also European interbank markets.

Three-month Libor-OIS (basis points)

FIGURE 2



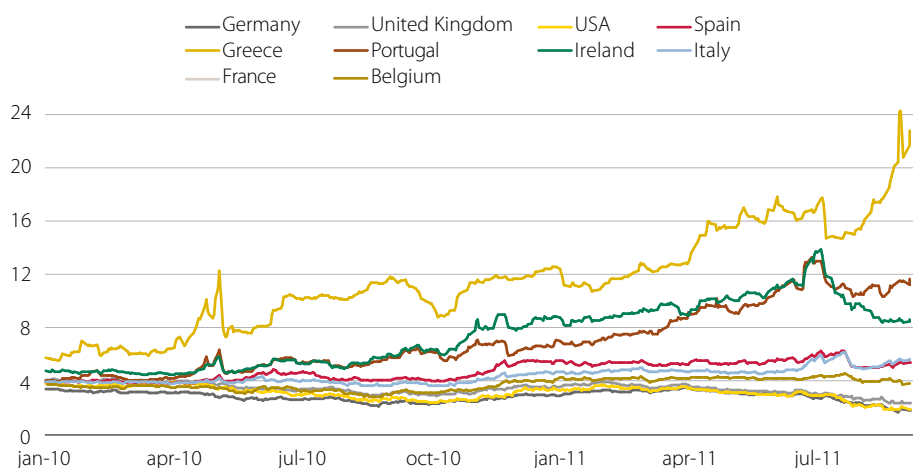
Source: Bloomberg. Data to 20 September.

Government bonds yields displayed similar behaviour to during the last bouts of volatility in certain euro-area sovereign debt markets; namely a significant run-down in the yields of U.S., German and UK treasuries on their reputation as safe-haven assets to historical lows of below 2% for the ten-year maturity. In contrast, the European economies in receipt of multilateral financial assistance saw their interest rates soar to peak levels of 24% for Greece and 14% in the cases of Ireland and Portugal. Meantime, interest rates on Spanish and Italian government paper pulled into line over the year's middle months with yields in both cases touching highs of over 6% (see figure 3). As figure 4 shows, these rising tensions progressively drew in other European economies like Belgium and France, which had not previously suffered major fluctuations in their sovereign risk indicators.

As in earlier rounds of market turmoil, investors have rushed in growing number into perceived safer assets...

Ten-year government bond yields (%)

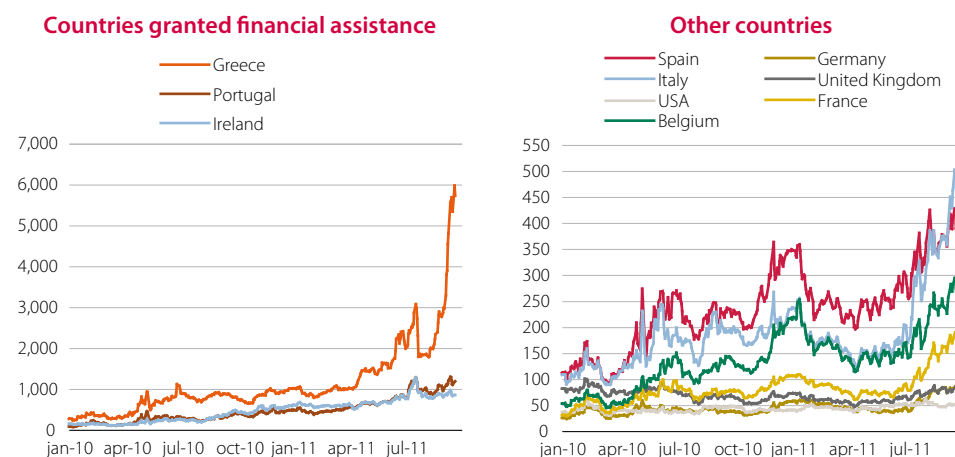
FIGURE 3



Source: Thomson Datastream. Data to 20 September.

Sovereign credit spreads, 5-year CDS (basis points)

FIGURE 4



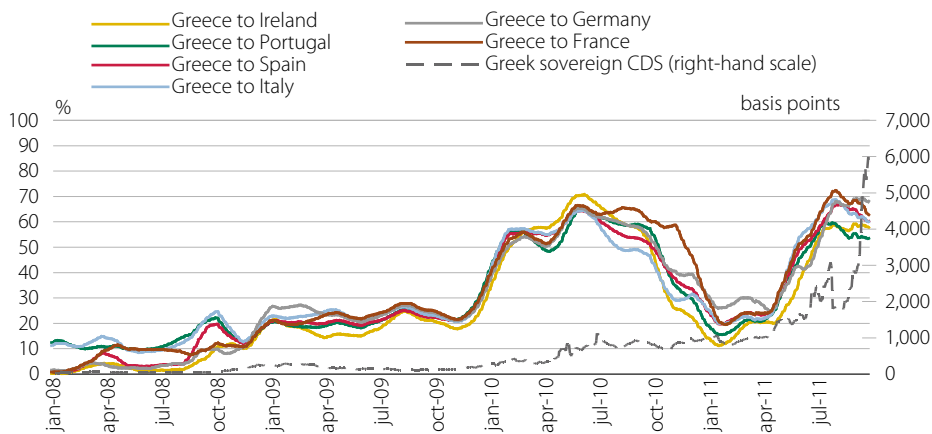
Source: Thomson Datastream. Data to 20 September.

...and rising sovereign spreads across a wide range of Europe's economies, victims of contagion.

Available indicators for the extent of sovereign risk contagion from more vulnerable economies to the rest of Europe, and the financial sector, show that the effect has been considerable. More specifically, indicators for sovereign credit risk contagion from Greece to other European economies have been running at highs since the start of August, peaking at just above the crisis levels of May 2010 (see figure 5). Further, dynamic estimates of credit risk transmission between Europe's financial and public sectors reveal that the public sector has been a contagion source of the first magnitude since early 2010, to increasingly damaging effect since the second quarter of this year (see figure 6).

Contagion of the Greek crisis to other European economies¹

FIGURE 5

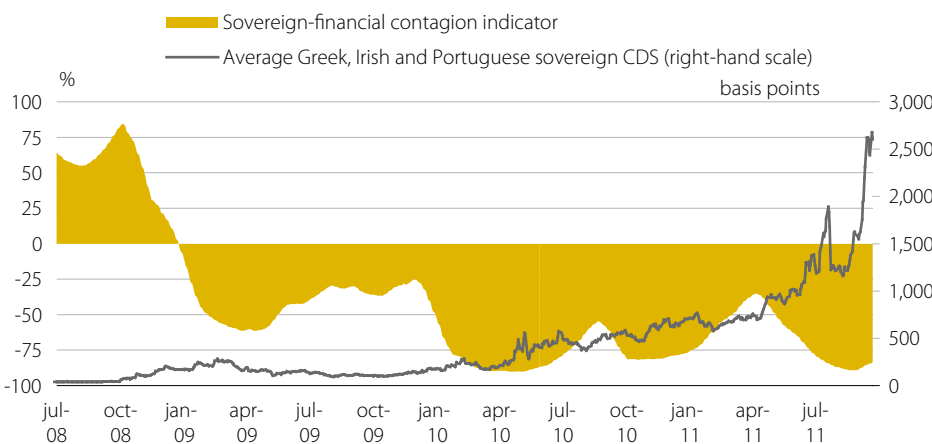


Source: CNMV.

- 1 The figure shows the percentage of variance in the CDS premiums of various European countries that is not ascribable to historical information but to contemporaneous shocks in Greece's credit risk. The resulting contagion indicator is increasing with the intensity of the effect produced by specific shocks in Greek sovereign spreads. The scale of contagion on a given day is calculated from available data for the 100 days preceding the current date, with the series also filtered by 30-day moving averages. Data to 20 September.

Sovereign-financial contagion in Europe¹

FIGURE 6



- 1 The figure shows the percentage of variance in the average CDS of the European banks sector and Greek, Portuguese and Irish sovereign bond that is not ascribable to their historical information but to contemporaneous return shocks. The resulting contagion indicator is decreasing with the increase in relative intensity of the impact of specific sovereign risk shocks on financial sector CDS. Positive values denote a net contagion effect from the European banking sector to the three countries' sovereign sector, while with negative values the source of the contagion is the sovereign risk of the study nations. Contagion on a given day is calculated from available data for the 60 days preceding the current date, with the series also filtered by 30-day moving averages. Data to 20 September.

Public debt market tensions also took their toll on the risk premiums of U.S. and European corporate issuers and, by extension, on their volumes of issuance. As figure 7 shows, the spreads of medium-to-low rated corporate issuers widened significantly in both the U.S. and euro area to not far short of the levels recorded in May 2010. Specifically, high-yield borrowers saw their spreads rise by around 315 and

Tensions in private fixed-income markets drive up the premiums of worse-rated issuers...

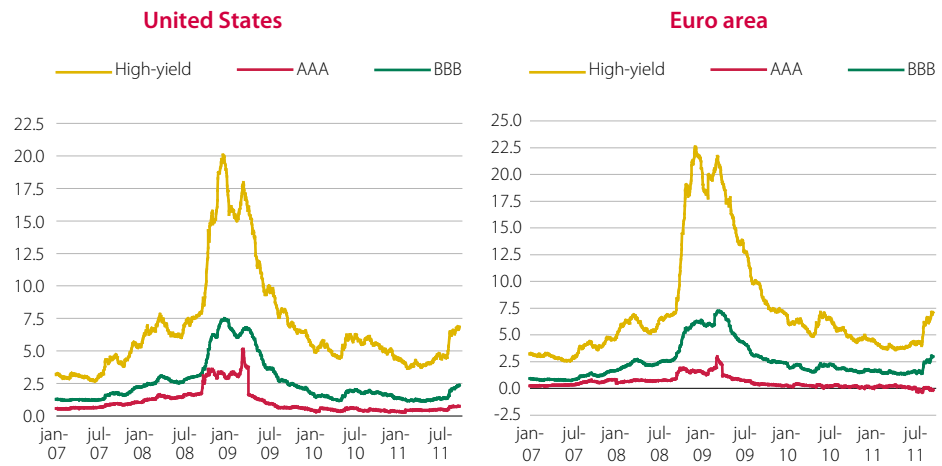
350 basis points in the United States and euro area respectively, from the lows of spring 2011 to the neighbourhood of 7%. Meantime, the spreads of medium-grade issuers (rated BBB or equivalent) climbed 125 bp in the U.S. and 165 bp in the euro area as far as 2.4% and 3.0% respectively.

...and cause an issuance slump that has proved especially intense in Europe.

But the single most visible effect of the tensions gnawing at the private corporate sector must be the relentlessly declining issue volumes on primary debt markets. As we can see from figure 8, net international debt issuance continued to shrink in the year's middle months due to lower government borrowing, the virtual drying-up of financial sector issuance, primarily in Europe, and the lull in borrowing by non-financial corporations. The tougher funding conditions faced by European financial institutions are not the only factor bearing down on issue volumes. Other regular funding sources, such as U.S. money-market funds, also thinned considerably in the summer period. In this respect, the recent coordinated decision by a number of banks, including the ECB, to provide liquidity in dollars to the commercial banking sector could help them steer clear of a funding crunch.

Corporate bond risk premiums¹ (percentage points)

FIGURE 7



Source: Thomson Datastream (Merrill Lynch, IBOXX indices). Data to 20 September.

Expressed as the yield spread between bonds of the same maturity and credit quality belonging to a given index and 10-year government bonds (a synthetic bond in the case of the euro area).

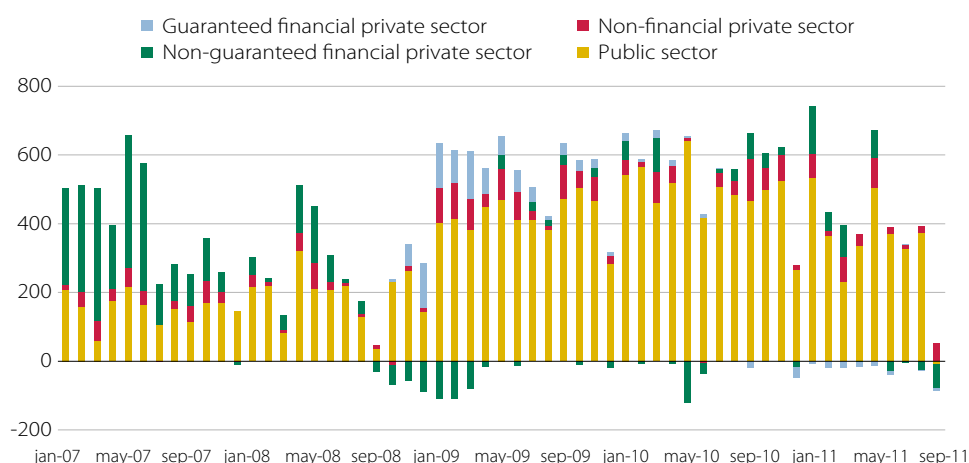
Key stock indices of advanced economies recede sharply in the third quarter, especially in Europe...

Meantime, the stock indices of leading advanced economies, which had generally held up well over the second quarter of 2011, plunged into losses in the third – by over 20% in the case of European indices and from 6.6% to 11% in the U.S. and Japan. Accompanying the fall was an upswing in volatility (as far as 40% in terms of historic volatility and, in some indices, to over 50% by the implied volatility measure). In most cases, however, the increase stopped short of the levels reached in May 2010, when the Greek crisis first erupted, or at end-2008 following the Lehman Brothers collapse. Falling share prices reduced the P/E (price-earnings) ratios of main world indices to around or below 10 times, compared to historical averages of 14 to 16 depending on the index.

Net international debt issuance, billion dollars

FIGURE 8

By type of issuer



Source: Dealogic. Monthly data. Data for September 2011 (to the 20th) are restated on a monthly basis.

Performance of main stock indices¹ (%)

TABLE 2

	2007	2008	2009	2010	3Q10	4Q10	1Q11	2Q11	3Q11 (to 20 September)			
									% prior qt.	% Dec	% y/y ²	
World												
MSCI World	7.1	-42.1	27.0	9.6	13.2	8.6	4.3	-0.3	-12.7	-9.2	-0.8	
Euro area												
Euro Stoxx 50	6.8	-44.4	21.1	-5.8	6.8	1.6	4.2	-2.1	-24.9	-23.4	-23.6	
Euronext 100	3.4	-45.2	25.5	1.0	7.5	2.8	3.2	-1.2	-19.9	-18.3	-17.2	
Dax 30	22.3	-40.4	23.8	16.1	4.4	11.0	1.8	4.8	-24.5	-19.4	-11.5	
Cac 40	1.3	-42.7	22.3	-3.3	7.9	2.4	4.8	-0.2	-25.1	-21.6	-21.2	
Mib 30	-8.0	-48.7	20.7	-8.7	6.2	1.1	6.4	-7.1	-25.5	-26.4	-25.7	
Ibex 35	7.3	-39.4	29.8	-17.4	13.5	-6.2	7.3	-2.0	-19.3	-15.2	-22.2	
United Kingdom												
FTSE 100	3.8	-31.3	22.1	9.0	12.8	6.3	0.1	0.6	-9.8	-9.1	-4.3	
United States												
Dow Jones	6.4	-33.8	18.8	11.0	10.4	7.3	6.4	0.8	-8.1	-1.5	6.1	
S&P 500	3.5	-38.5	23.5	12.8	10.7	10.2	5.4	-0.4	-9.0	-4.4	5.2	
Nasdaq-Cpte	9.8	-40.5	43.9	16.9	12.3	12.0	4.8	-0.3	-6.6	-2.4	10.0	
Japan												
Nikkei 225	-11.1	-42.1	19.0	-3.0	-0.1	9.2	-4.6	0.6	-11.2	-14.7	-9.4	
Topix	-12.2	-41.8	5.6	-1.0	-1.4	8.4	-3.3	-2.3	-11.1	-16.0	-11.4	

Source: Datastream.

1 In local currency.

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

...with the bear trend extending to the stock indices of emerging market economies.

European and Japanese stock indices have been the worst performers year-to-date (from -9.1% in the case of the FTSE 100 to -26.4% in the case of the Mib 30), while U.S. indices managed to contain their losses between the -1.5% of the Dow Jones and -4.4% of the S&P 500. Emerging market indices, with few exceptions, posted falls on a similar scale. By sector, financial shares took the biggest punishment, especially in Europe, where doubts persist about the strength of the banking sector and the extent of its exposure to European sovereign debt.

The euro loses ground against other leading currencies.

In currency markets, salient developments have been the euro's slide against the dollar, starting last May, which has taken exchange rates down from 1.49 to 1.37 dollars, and, above all, the appreciation of the yen and Swiss franc against the euro and the dollar, in tune with the safe-haven role they have exercised throughout the crisis.

Exhibit 1: "Dark liquidity: the new IOSCO principles"

For some years now, a growing part of securities market trading has taken place in dark venues or else has been instrumented through orders that are not subject to pre-trade transparency requirements. In both these cases, buy and sell orders are not disclosed to all market participants, while the liquidity they generate is not factored with remaining orders into the price formation process. This kind of trading is conducted on electronic platforms managed by multilateral trading facilities, broker-dealers and even regulated markets in specific trading segments. According to data from the European Securities and Markets Authority (ESMA), as many as 10% of the transactions closed on European regulated markets and multilateral facilities in 2010 did not meet conditions of pre-trade transparency.

In May 2011, IOSCO's Technical Committee approved a report¹ expressing regulators' concerns about the rapid development of these so-called dark pools. Specifically, IOSCO identifies three ways or areas in which trades not subject to pre-transparency requirements may impair market operation:

- Price formation, since dark liquidity does not contribute to price discovery.
- Potential fragmentation of liquidity and information, so buyers have to search for liquidity across a greater number of venues, pushing up their transaction costs.
- Fair access and market integrity, such that certain participants may be denied access to the market or order information selectively channelled towards some users at the expense of others.

IOSCO has accordingly developed a series of principles to mitigate the adverse effects of dark pool trading in these three domains. And its Technical Committee urges members to bear them in mind when preparing regulatory initiatives that address dark pools and dark orders:

- The first principle refers to the need to ensure timely access to information on the price and size of securities orders (pre-transparency) to mitigate the

potentially adverse effects of liquidity being fragmented across a multiplicity of trading venues, and to facilitate best execution and efficient price formation. The Technical Committee acknowledges the heterogeneous nature of trading platforms and orders themselves and that it may be appropriate to apply different levels of pre-trade transparency. Indeed it recognises that full disclosure requirements may need to be waived in the case of large orders with a potential impact on price formation.

- The second principle, turning on the dissemination of price and volume information on already executed trades (post-transparency), insists that all transactions should be disclosed on the same basis to all participants, including those executed in dark pools. Regarding the content of disclosure, the Technical Committee leaves it to regulators' discretion whether to specifically identify dark venues or the fact that a trade has resulted from a dark order.
- The third principle proposes that transparent orders should take priority over dark orders in the execution queue.
- The fourth principle stresses that regulators must be able to access information on orders and transactions effected in dark pools.
- The fifth principle insists that dark pools should provide market participants with sufficient information about the way orders are handled and executed.
- Finally, the sixth principle calls on regulators to periodically monitor developments in dark pools and dark orders to ensure that they are not impairing the efficiency of the price formation process, and, where necessary, to take appropriate preventive action.

1 *Principles for Dark Liquidity. Final Report.* May 2011, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD353.pdf>

2.2 National economic and financial developments

Quarterly National Accounts data for the second quarter of 2011 show that Spain's GDP grew 0.2% in quarterly and 0.7% in year-on-year terms, in both cases two decimal points below previous quarter's rate. Note that deceleration was rather less than in other European countries, though the economy's year-on-year advance still trailed behind the average for the euro area (1.6%).

Spanish GDP advances at a modest rate...

Year-on-year growth of Spain's GDP drew heavily on external demand, which doubled its contribution to aggregate growth as far as 2.6 points. Conversely, domestic demand detracted 1.9 points against the 1.5 points of one year before, with private consumption (-0.2% year-on-year), government consumption (-1%) and, particularly, gross fixed capital formation (-6%) also contributing on the downside. Meantime, imports dropped by 1.7% year-on-year after a steady advance spanning five consecutive quarters, while exports rose by 8.4% (12.1% in the first quarter).

...thanks to the strength of exports...

...and positive input from industry and, to a lesser extent, services.

On the supply side, deceleration extended to all branches of production except construction which, despite clawing back some ground, still registered the steepest decline (-4.1%) in year-on-year terms. The energy sector, meantime, slowed to 0.9% (3.4% in the first quarter) and industry to 3.2% (4.1% in the first quarter), while the services sector dropped one decimal point of growth as far as a year-on-year rate of 1.2%.

Spain: main macroeconomic variables (annual % change)

TABLE 3

	2007	2008	2009	2010	European Commission*	
					2011F	2012F
GDP	3.6	0.9	-3.7	-0.1	0.8 (+0.1)	1.5 (-0.2)
Private consumption	3.7	-0.6	-4.2	1.2	0.8 (-0.1)	1.1 (-0.5)
Government consumption	5.5	5.8	3.2	-0.7	-1.4 (-0.1)	-0.3 (=)
Gross fixed capital formation, of which:	4.5	-4.8	-16.0	-7.6	-3.4 (-0.3)	1.8 (-0.9)
Equipment	10.4	-2.5	-24.8	1.8	3.1 (-0.6)	4.4 (-1.6)
Exports	6.7	-1.1	-11.6	10.3	7.0 (+1.5)	5.8 (+0.2)
Imports	8.0	-5.3	-17.8	5.4	1.7 (+0.3)	3.8 (-0.7)
Net exports (growth contribution, pp)	-0.8	1.5	2.7	1.0	1.4 (+0.3)	0.5 (+0.2)
Employment	2.8	-0.5	-6.6	-2.4	-0.6 (-0.3)	0.9 (-0.2)
Unemployment rate¹	8.3	11.3	18.0	20.1	20.6 (+0.4)	20.2 (+1.0)
HICP	2.8	4.1	-0.2	2.0	3.0 (+1.5)	1.4 (=)
Current account (% GDP)	-10.0	-9.6	-5.5	-4.5	-4.1 (-0.3)	-4.1 (-0.5)
General government (% GDP)	1.9	-4.2	-11.1	-9.2	-6.3 (+0.1)	-5.3 (+0.2)

Source: Ministry of Economy and Finance, National Statistics Office (INE) and European Commission.

1 Eurostat definition.

* Forecasts published in spring 2011 (with respect to autumn 2010). In September 2011, the European Commission released interim European economic forecasts ahead of the autumn edition, which maintained its growth projection for the Spanish economy at 0.8% for 2011, and downward revised its inflation forecast by one decimal point to 2.9%.

Spanish inflation has abated since April, narrowing the gap versus the euro area...

Inflation in the EU, measured by the harmonised index of consumer prices, eased to 2.7% in August after the peak levels of April 2011 (3.5%), with the fall extending to most components. Spain's headline inflation moderated rather more steeply, narrowing the differential with the euro area to 0.2 points. Core inflation, meantime, dropped to 1.6% from the 2.1% high of April-May to stand four decimal points above the euro-area average.

...in a framework of labour market weakness...

Spanish labour market statistics offered little to celebrate, with around 1% fewer employed workers at the close of the second quarter (18.3 million) and unemployment rates stuck above 20%. Unit labour costs have receded by an average 2% since 2010 in contrast to the pre-crisis years, when they were advancing ahead of 4% annually driven by rising wage compensation per worker. The subsequent decline was the combined work of flat wage growth and higher labour productivity.

...and intense budgetary adjustment spearheaded by central government.

The latest data for central government budgetary execution reveal a 22.75 billion deficit on a national accounts basis over the first seven months of 2011 (2.1% of GDP), an 11.8% decrease with respect to the year-ago period. Non-financial revenues

grew by 1% while non-financial payments fell by 22.7% in year-on-year terms in tune with budgetary austerity. Meantime, the budgetary outcomes of the autonomous communities throw up a first-half deficit equivalent to 1.2% of national GDP (1% of GDP in the same period of 2010) on the back of a decline in non-financial revenues (-3.6%) and slightly higher spending (0.5%). The general government debt ratio moved up 4.8 points in the opening quarter to 65.2% of GDP. Of this volume, 49.4 points corresponded to central government, 12.4 to the autonomous communities and 3.5 to local authorities.

One move that may help alleviate the uncertainty surrounding the sustainability of Spain's public finances is Parliament's approval of a bill to limit the structural budget deficit by amending Article 135 of the Constitution. Under the recast provision, the structural deficit (discounting public revenues and expenditures derived from the normal fluctuations of the business cycle) may not exceed 0.40% of GDP across all sub-sectors of general government.²

The newly approved public deficit ceiling may help to dispel market uncertainty.

As well as conducting their business in the face of persistently weak domestic activity, Spanish credit institutions had to cope with both the challenges of sector restructuring and a resurgence in market tensions that has placed added pressure on their share prices and funding conditions.

Credit institutions have to negotiate a complex landscape, characterised by...

The income sheets of national deposit-taking entities held in positive territory over the first six months of 2011, with aggregate net profits topping 4.70 billion euros, 23% less than in the first half of 2010. Behind these lower numbers was a fall in net interest income (down 21%), originating in higher interest costs (up 30%), which could not be sufficiently offset by substantial improvement in the sector's impairment losses in financial assets.

...weak domestic activity...

Outstanding loans to the non-financial private sector (corporations and households) registered a year-on-year decline of 3% to the month of July, prolonging the downward trend that commenced in 2009. All lending modalities shared in the decrease led by household consumer credit (-5%) and business loans (-4.2%). Home purchase lending has contracted by around 1% since June after the small advance of full-year 2010, the likeliest cause being the increased tax pressure on home ownership.³ The contrast is provided by lending to public authorities, which expanded 15% in year-on-year terms. In the euro area, aggregate lending to the non-financial private sector rose at a year-on-year rate ahead of 2%. The advance extended to all modalities with home purchase loans strongly to the fore (5%). Finally, growth of household consumer credit cooled to 0.6%, while business lending kept up a steady but discreet recovery (1.4%).

...an ongoing contraction in lending to the non-financial private sector...

By July, the non-performing loans ratio of Spanish credit institutions was up to 6.9%, two decimal points higher than in June and almost one and a half points

...an NPL ratio fast approaching 7% on the deterioration of loans to construction and real estate...

2 This ceiling will be regulated by a future law to be approved before 30 June 2012 and implemented as of 2020. The limit will be set at 0.4% of GDP on a general government basis, 0.26% for central government and 0.14% for the autonomous communities, but may be subject to review in 2015 and 2018. Local authorities will be required to present a balanced budget.

3 Tax deductions for first home purchases will be discontinued in 2011. Also, the VAT on new housing purchases was raised from 7% to 8% in July 2010.

above its year-ago levels. The biggest culprits were again construction and real estate development, with a combined second-quarter ratio of 17% (13.5% in December 2010 and 10.9% in June 2010), while delinquent loans to households held at 3.2%, two decimal points less than at mid-year 2010.

...and tougher funding conditions amid renewed market stress.

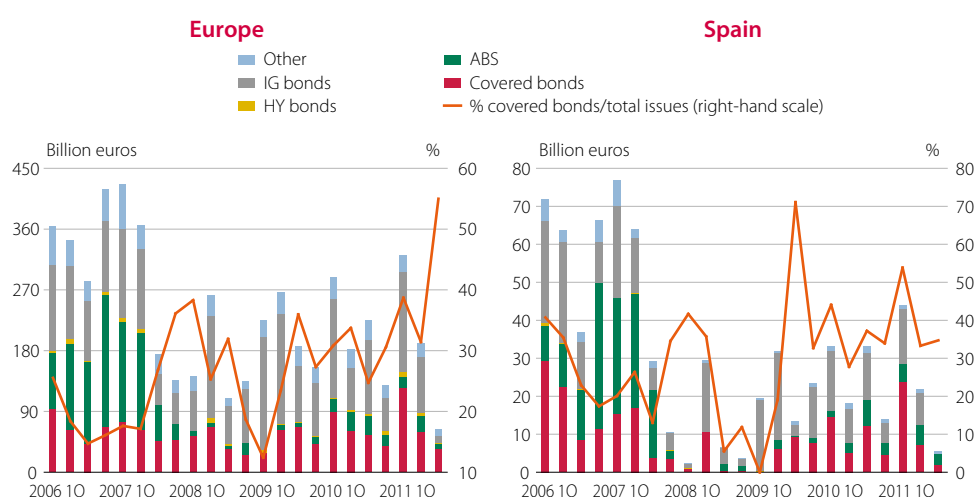
Spanish banks have faced increasing funding difficulties, with the summer months proving especially tough as market tensions flared once more. Since the start of the crisis, institutions have had to find alternative sources to the international wholesale markets they could comfortably draw on around the middle of the last decade. Hence their recourse to non-conventional means like government-backed bonds, whose issuance has nonetheless tapered off this year,⁴ or borrowing from the Eurosystem. Funds raised through this last channel peaked at over 130 billion euros in the middle months of 2010, then dropped back to around 40 billion in the first quarter of 2011 until renewed debt market tensions sent them heading back upwards to 70 billion euros in August last.

Entities respond by competing for deposits and centring their debt issuance in high-quality instruments.

The trends emerging over recent months in Spanish credit institution financing strategies combine: (i) a major drive to broaden their customer base and build their deposit volumes (deposits from the non-financial private sector have climbed by over 16 billion euros since the lows of April 2010); (ii) a gathering shift in the debt financing mix towards mortgage covered bonds; and (iii) a step-up in equity issuance. The above change in the debt mix mirrors developments elsewhere in Europe (see figure 9), where the across-the-board surge in investor risk aversion has persuaded banks to opt increasingly for products of perceived higher quality, like mortgage covered bonds (46% of Spanish entities' issue volume in the year and 38% that of their European peers). Finally, the recent upswing in the equity issuance of Spanish credit institutions traced mainly to the stockmarket listings of two entities arising from savings bank mergers (see exhibit 2 of this report).

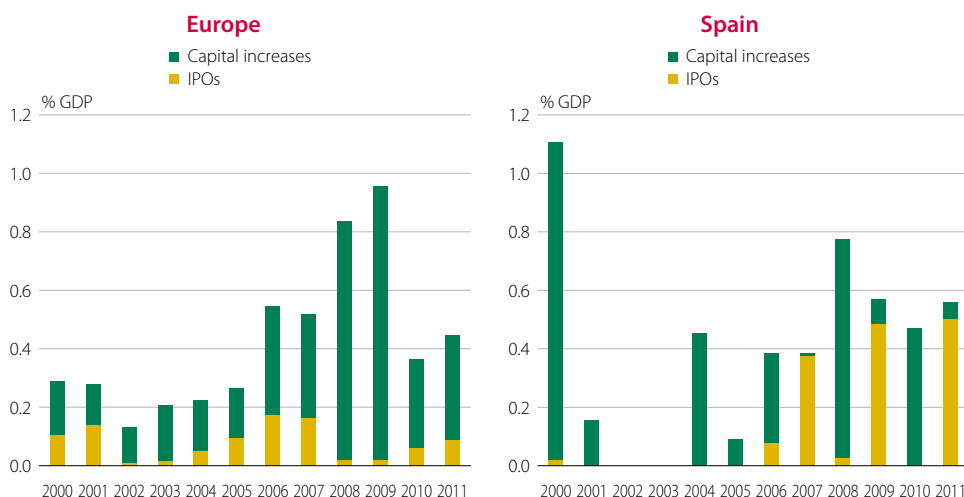
Gross medium- and long-term debt issuance by financial entities

FIGURE 9



Source: Dealogic. Data to 20 September 2011.

4 Issuance of government-backed bonds has faded to just four billion euros year-to-date compared to the 13 and 48 billion euros of 2009 and 2010 respectively.



Source: Dealogic. Data to 20 September 2011. Data for this last year restated on an annual basis.

Exhibit 2: “The stockmarket flotation of Spanish savings banks”

Royal Decree-Law 2/2011 of 18 February on the strengthening of the Spanish financial system, toughened the capital requirements of Spanish credit institutions by establishing a minimum core capital ratio of 8% of risk-weighted assets, rising to 10% for those institutions with less than 20% of their equity in the hands of private investors and, additionally, reliant on wholesale funding for over 20% of their net loans. In order to meet the condition of having a minimum percentage of equity under private investor ownership, some savings banks have opted to transfer their financial activities to a newly created commercial bank and apply for its shares to be admitted to stockmarket trading. By the deadline for this report, the first entities arising from this strategy, Bankia and Banca Cívica, had had their listing applications approved by the CNMV, on 20 and 21 July respectively.

The criteria utilised by the supervisor in verifying these operations are summarised below:

1. Ownership dispersion

Among the listing conditions stated in Royal Decree 1310/2005 is that shares admitted to trading should have a wide enough distribution to ensure them sufficient secondary market liquidity. This requirement is normally met through a public offer for sale or subscription before the entity begins trading. The RD establishes that ownership dispersion will be sufficiently wide if 25% of the shares for which admission is sought are distributed among the public. However this threshold can be lowered if the market can operate effectively due to the large number of the issuer’s shares outstanding and the extent of their distribution. At times, the CNMV has accepted an ownership dispersion below 25% (though never as low as 20%) for large-scale transactions involving a large number of shareholders, but always providing the issuer makes certain undertakings in return. In the case of

the stockmarket listings of Bankia and Banca Cívica, the regulator's view was that share distribution was sufficient, considering that Bankia and Banca Cívica had a free-float¹ on their admission dates of 43.3% and 44.7% respectively.

2. The listing price

As on any occasion when the public are asked to invest their savings in particularly complex market conditions, the CNMV was doubly vigilant with regard to the pricing procedures followed by issuers and their advisors. Normally, the most effective guarantee of fair, independent price formation is the existence of a large tranche of qualified investors participating in the bookbuilding² process. In this case, it was stipulated that the qualified investor tranche should equate to 40% of the offer volume before the exercise of the purchase or greenshoe option traditionally reserved for placing agents.

In savings bank placements, the CNMV has established that at least half of the qualified investors' tranche should be formed by the sub-category of institutional investors, that is, the investors envisaged in letters a), b), c) and d) of Article 78(2) of the Securities Markets Law, defining the different types of qualified investor.

Finally, the supervisor considered that to guarantee a diverse enough base of investor institutions contributing to efficient price formation, at least one hundred qualified investors should acquire a significant stake through the bidding process.

The following two tables show the breakdown of placements across subscriber categories.³

Results of BANKIA IPO			
Types of subscribers	No. of shares	% offering	No. of subscribers
Financial institutions	105,055,568	12,74	532
- Spanish market	80,208,378	9,73	511
- Foreign market	24,847,190	3,01	21
Insurance corporations	86,433,137	10,48	145
Public authorities	2,597	0,00	2
SUB TOTAL	191,491,302	23,22	679
Others (*)	633,080,951	76,78	270,484
TOTAL OFFERING	824,572,253	100	271,163
Pro memoria:			
Price per share (euros)	3,75		
Capital raised (million euros)	3,092		
(*) Non-financial corporations, households and private not-for-profit organisations.			

Results of BANCA CÍVICA IPO			
Types of subscribers	No. of shares	% offering	No. of subscribers
Financial institutions	46,371,203	20,87	89
- Spanish market	18,324,440	8,25	83
- Foreign market	28,046,763	12,63	6
Insurance corporations	12,304,399	5,54	30
Public authorities	13,330	0,01	5
SUB TOTAL	58,688,932	26,42	124
Others (*)	163,453,868	73,58	66,530
TOTAL OFFER	222,142,800	100	66,654
Pro memoria:			
Price per share (euros)	2,7		
Capital raised (million euros)	600		
(*) Non-financial corporations, households and private not-for-profit organisations.			
1 Percentage of the issuer's share capital that is available for purchase on the market.			
2 Bookbuilding is a price formation mechanism based on a demand prospection among potential investors assessing the quantities and price at which they would be willing to transact. Depending on the results, the placing agent and issuers arrive at a fixed price or discount rate for the placement.			
3 For a correct reading of these data, please bear in mind that a portion of institutional investment (corresponding to non-financial large corporations) appears under "Others".			

Non-financial listed companies reported aggregate net profits of 13.15 billion euros in the first half of 2011, 8% more than in the same period last year (see table 4). Profits growth extended to all sectors with the exception of energy, whose combined earnings dropped 10% approximately to 6.13 billion euros. The top performers were retail and services and industrial sector companies, with profits growth of over 10% to 5.24 billion and 818 million euros respectively. But perhaps the most newsworthy development was the return to profit of construction and real estate firms, who posted first-half earnings of 954 million euros after several years of heavy losses.

Non-financial listed companies grow their profits 8% in first half 2011...

Earnings by sector:¹ non-financial listed companies

TABLE 4

Million euros	EBITDA ²		EBIT ³		Net profit	
	1H10	1H11	1H10	1H11	1H10	1H11
Energy	16,044	15,545	10,767	10,265	6,796	6,129
Industry	2,161	2,217	1,328	1,394	741	818
Retail and services	14,583	15,777	8,333	8,917	4,660	5,240
Construction and real estate	3,616	4,340	2,004	2,722	-3	954
Adjustments	-102	-85	-28	-18	1	14
AGGREGATE TOTAL	36,302	37,794	22,404	23,280	12,195	13,155

Source: CNMV.

1 Year-to-date.

2 Earnings before interest, taxes, depreciation and amortisation.

3 Earnings before interest and taxes.

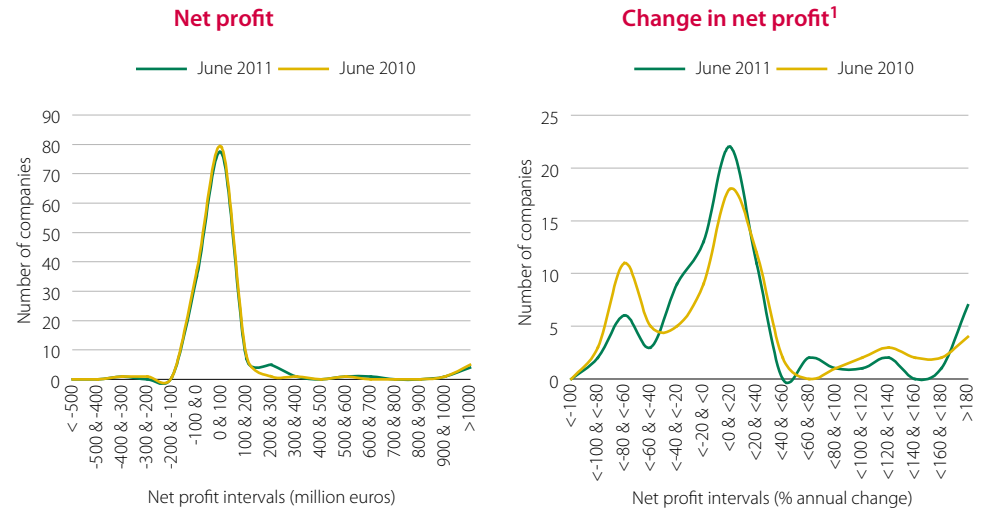
Breaking down listed companies in terms of their net profit for the year (see figure 11, left panel), we find a broadly similar pattern to the two preceding first-half periods. A majority of firms posted earnings of less than 100 million euros, though the number with profits between 200 and 300 million was higher than in the year-ago

...with little variation in the results of individual firms.

period. As occurred last year, no single firm suffered losses deeper than 400 million euros. Finally, among the listed companies in profit over first-half 2010 and 2011 (see figure 11, right panel), a larger number had reported moderate improvement or deterioration (an increase or decrease of less than 40%), while those with more pronounced swings in either direction were fewer overall.

Non-financial listed companies by:

FIGURE 11



Source: CNMV.

1 Number of entities distributed according to the change in their net profit, including only those with a positive net outcome in both years.

Non-financial listed companies pay down debt by 5.1% in the first half of 2011...

The combined debt of non-financial listed companies dropped by 5.1% to 310 billion euros between December 2010 and June 2011, in a break with the rising trend of previous years (see table 5). The contraction, however, was far from universal, with debt actually increasing in two (the industrial sector and construction and real estate) and falling in two others (energy and retail and services). More specifically, industrial firms grew their debt balance 19.2% to almost 18 billion euros, the cause being one firm's financing of its acquisition of a foreign competitor, while the total debt of construction and real estate operators rose by a more subdued 1.7% to 101 billion euros. Meantime, firms in the energy sector and retail and services cut their debt levels by 7.6% and 12.0% respectively. Note that the sectors reporting higher debt in the first half of 2011 were also those that had increased debt less or even decreased it in the course of the preceding years.

...though not all sectors share in the decrease.

Despite this aggregate reduction in indebtedness, financial leverage (the ratio between debt and net equity) ticked up from 1.4 at end-2010 to 1.5 in June 2011 due to a reduction on the equity side (see table 5). Meantime, the debt coverage ratio, measuring the years needed to repay existing debt assuming constant EBITDA, rose from 3.8 in December 2010 to 4.0 in June 2011. The biggest jump here (from 2.1 to 4) corresponded to industry, the source being the same large corporation remarked on above. Retail and services was the only sector that reduced its debt coverage ratio thanks to a strong earnings performance coupled with a decrease in aggregate indebtedness. Companies' interest coverage ratios deteriorated slightly, with EBIT/interest expenses down from 3.1 at end-2010 to 2.6 in June 2011, though not all sectors participated in the decline.

Gross debt by sector: listed companies

TABLE 5

Million euros		2007	2008	2009	2010	1H11
Energy	Debt	69,172	82,608	100,572	98,283	90,815
	Debt/ Equity	0.8	0.9	1.1	0.9	0.9
	Debt/ EBITDA ¹	2.5	2.8	3.5	2.8	2.9
	EBIT2/ Interest expenses	4.1	3.7	3.4	4.2	3.8
Industry	Debt	13,312	15,645	15,953	14,948	17,824
	Debt/ Equity	0.6	0.7	0.7	0.6	0.9
	Debt/ EBITDA	1.8	2.7	3.0	2.1	4.0
	EBIT/ Interest expenses	5.9	3.4	3.1	5.0	2.8
Construction and real estate	Debt	138,933	119,788	104,762	99,917	101,605
	Debt/ Equity	3.1	3.8	4.1	3.4	3.1
	Debt/ EBITDA	10.8	31.9	22.5	11.2	11.7
	EBIT/ Interest expenses	1.2	0.0	0.3	1.0	1.0
Retail and services	Debt	96,941	112,322	108,579	115,413	101,605
	Debt/ Equity	1.7	2.1	1.8	1.6	1.9
	Debt/ EBITDA	3.0	3.6	3.7	3.4	3.2
	EBIT/ Interest expenses	3.2	2.9	3.3	3.9	3.1
Adjustments ³	Debt	-17,391.0	-20,802.0	-1,908	-1,792	-1,670
AGGREGATE TOTAL⁴	Debt	300,967	309,561	327,958	326,769	310,179
	Debt/ Equity	1.5	1.6	1.6	1.4	1.5
	Debt/ EBITDA	4.0	4.6	4.8	3.8	4.0
	EBIT/ Interest expenses	3.0	2.0	2.4	3.1	2.6

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.

4 This table did not previously include any financial entities, comprising credit institutions, insurance companies and portfolio companies. However, as IPP (Periodic Public Information) forms are the same for portfolio companies as for non-financial companies starting in 2008, it has been decided to include them in the aggregate figure. Data for the 2007 close have been restated to factor the impact of Criteria Caixacorp.

Household asset indicators for the first quarter of 2011 reveal a further decline in savings rates to just over 12% of disposable income, remote from the highs recorded at the start of 2010 (18.1%). In the same period, household debt dropped below 125% of gross disposable income on a combination of stable income and lower liabilities, while net wealth contracted slightly as depreciating real estate cancelled out the small advance in financial asset prices.

Household savings shrink, along with indebtedness.

As to investment decisions, households' net financial asset purchases in the year's opening quarter came to 3.5% of GDP⁵ (4.4% in 2010). The acquisitions mix evidenced Spaniards' continuing preference for lower-risk instruments, with invest-

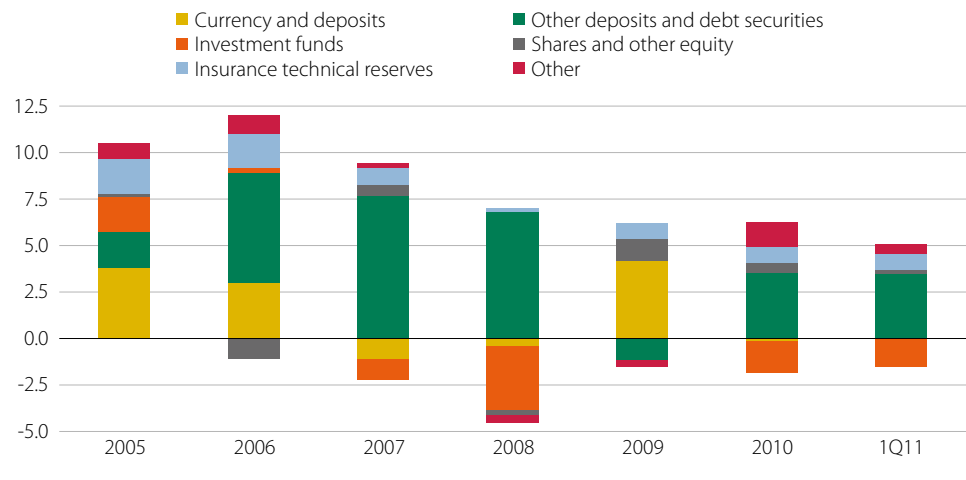
Homes continue gearing their investment to lower-risk instruments.

5 Cumulative four-quarter data.

ment in term deposits and insurance and pension plan products at 3.1% and 0.8% respectively of first-quarter GDP. The contrast was provided by the slump in equity investment (0.1% of GDP) versus the two previous years, and net outflows from investment funds approaching 1.5% of GDP (1.7% in 2010). Finally, the share of household liabilities receded five decimal points to 0.8% of GDP.

Households: financial asset acquisitions (% GDP)

FIGURE 12



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

2.3 Outlook

Forecasts by leading organisations auguring a global slowdown in the next few quarters...

The IMF's latest forecasts, published in September after the high point of the summer crisis, project a world growth slowdown from 2010 rates just topping 5% to nearer 4.0% in 2011 and 2012. These figures represent a cut of three and five decimal points respectively over the same organisation's June forecasts. Emerging market economies are expected to again spearhead the advance in world activity with growth rates of 6.4% in 2011 and 6.1% in 2012, compared to the considerably thinner 1.6% and 1.9% augured for the advanced economies, where the big talking-point was the substantial revise-down in the growth forecasts for the United States (by 0.9 points to 1.8%) and Germany (by 0.7 points to 1.3%).

...are surrounded by uncertainty since turbulence returned to world markets...

These forecasts are inevitably subject to considerable uncertainty after the latest flare-up in the European debt crisis and the weakening activity of the year's middle months. Indeed the heightened instability of financial markets observable since spring, and attributed primarily to European debt markets is being increasingly linked to mounting fears of a new worldwide recession.

...and estimate risk remains tilted to the downside.

As such, the main and, without doubt, growing downside risks for these baseline scenarios have to do with: (i) prolongation of the distrust affecting certain euro-area sovereign borrowers, pushing up the costs of funding and thereby depressing activity; (ii) a slowdown in growth and employment affecting leading advanced economies; (iii) the need to secure public finance sustainability across a wide range of economies and, finally; (iv) the resurgent liquidity and funding problems besetting the financial sector, especially in Europe, where doubts persist over the scale and effectiveness of the restructuring process.

The forecasters' consensus for the Spanish economy, after near zero growth in domestic activity in 2010, is just under 1% in 2011, then improving to 1.1-1.5% in 2012. The IMF's revision of its growth projections for Spain (unchanged in 2011 and a half-a-point revise-down in 2012) is less severe than the correction applied to other advanced economies. The main uncertainties hanging over this gradual recovery scenario stem from the aggregate risk induced by sovereign debt problems and, in particular, their possible contagion to other sectors of the economy, and the possible drag effect on domestic activity of a slowdown in the dynamic economies that constitute its main export markets.

Spain is expected to see moderate growth, with risks lurking mainly in debt market tensions and the projected deceleration of external demand.

3 Spanish markets

3.1 Stock markets

The deepening impact of the European sovereign debt crisis and the worsening outlook for world economic activity unleashed a new wave of volatility in the year's middle months, and sent prices tumbling in international markets for equity instruments. The shares of European financial institutions were among the hardest hit, reflecting their heightened exposure to the sovereign debt of the region's more vulnerable economies. Spanish stock markets too were caught up in the prevailing uncertainty in the form of increased volatility and a price slide mirroring that of other European bourses. It was in response to the unsettled state of some of these markets, due in part to manipulative rumour-mongering, that the securities regulators of Belgium, Spain,⁶ France and Italy, under the coordination of ESMA (European Securities and Markets Authority), decided on 11 August to impose a temporary ban on the creation or increase of short positions in financial sector shares in their respective jurisdictions (see exhibit 3 of this article).

The latest round of the European sovereign debt crisis and worsening prospects for world economic growth sent stock markets tumbling in a climate of growing instability...

Against this backdrop, the country's main stock market indices posted third-quarter losses approaching 20%,⁷ in line with other European benchmarks, in contrast to the mild falls of the second quarter and, more strikingly, the price rally of the opening months (in all but Latin American securities platforms, see table 6). The Ibex 35 shed 19.3% of its value in the third-quarter period on the heels of 2% losses in the second quarter and a 7.3% price gain in the first, resulting in a year-to-date fall of 15.2%. Smaller cap indices experienced similar fortunes with declines of over 18% in the third quarter, for year-to-date losses summing 19.4% in the case of the Ibex Medium Cap and 15.8% for the Ibex Small Cap. Finally, Latin American indices contained their third-quarter losses at 9% and 11%, to close the first nine months down by 19% and 23%.

...which led to a temporary ban on the creation or increase of short positions in financial shares, applied in various European countries including Spain.

6 On 11 August last, the CNMV approved a temporary ban on transactions involving the creation or increase of short positions in Spanish financial sector shares, pursuant to Article 85.2 j of Securities Markets Law 24/1988 of 28 July and with the sole exception of market maker trades. A short position is understood as one arising from a positive economic exposure to a fall in the share price. On 25 August 2011, the CNMV extended its prohibition to 30 September 2011, with the possibility of lifting it earlier if market conditions settle and otherwise prolonging it as an exceptional measure.

7 To 20 September.

Performance of Spanish stock market indices and sectors (%)

TABLE 6

Index	2007	2008	2009	2010	1Q11 ¹	2Q11 ¹	3Q11 (to 20 September)		
							% prior qt.	% Dec	% y/y
Ibex 35	7.3	-39.4	29.8	-17.4	7.3	-2.0	-19.3	-15.2	-22.2
Madrid	5.6	-40.6	27.2	-19.2	7.5	-2.7	-19.7	-16.0	-23.9
Ibex Medium Cap	-10.4	-46.5	13.8	-5.6	6.3	-6.9	-18.6	-19.4	-19.3
Ibex Small Cap	-5.4	-57.3	17.6	-18.3	17.4	-8.2	-21.9	-15.8	-18.5
FTSE Latibex All-Share	57.8	-51.8	97.2	9.0	-3.2	-9.9	-11.2	-22.6	-15.5
FTSE Latibex Top	33.7	-44.7	79.3	9.7	-3.9	-8.1	-8.6	-19.2	-16.5
Sector²									
Oil and gas	1.8	-30.8	-20.1	0.3	22.5	-2.2	-12.5	4.9	15.0
Chemicals	-58.4	-67.8	3.4	-60.0	30.4	5.8	-19.6	10.8	0.0
Basic materials	-17.2	-45.4	23.1	-5.6	9.0	-6.6	-26.3	-25.0	-25.0
Construction mat. and construction	-12.0	-51.0	25.5	-14.4	13.8	-5.7	-17.5	-11.4	-11.7
Industrial goods and services	6.9	-41.9	29.3	-1.9	4.6	-1.4	-14.1	-11.3	-11.8
Health	19.2	-45.0	17.7	-22.2	14.1	0.3	-10.8	2.0	-8.8
Utilities	18.5	-31.0	-7.8	-14.3	10.8	3.3	-22.4	-11.2	-9.7
Banks	-4.5	-47.9	46.3	-32.3	7.3	-4.4	-25.5	-23.6	-38.5
Insurance	-13.3	-25.0	19.8	-26.8	26.6	-1.3	-12.2	9.7	-0.7
Real estate	-42.6	-58.6	-43.8	-53.2	24.2	-20.8	-32.9	-34.0	-51.6
Financial services	-35.6	-44.3	20.8	12.8	22.6	-3.6	-13.0	2.8	4.4
Telecommunications and media	26.3	-31.4	23.5	-13.4	4.3	-5.4	-17.7	-18.8	-24.1
Discretionary consumption	-7.7	-39.2	37.0	20.6	2.9	5.9	-5.6	2.8	0.4
Basic consumption	6.9	-22.5	-8.4	15.8	0.8	-5.4	-17.5	-21.3	-14.6

Source: Thomson Datastream.

1 Change versus previous quarter.

2 Classification according to Thomson Datastream.

The third-quarter price slide extends to all sectors, with the banks among the worst affected.

All sectors shared in the third-quarter price slump in national equity markets, with losses ranging from the 7% of consumer goods (discretionary and basic) to the 33% of the real estate sector. Among the big cap players the steepest slide corresponded to the banks (-25%), telecommunications and media (-18%) and utilities (-22%), while those in the middle capitalisation bracket, like construction and materials, oil and gas and industrial goods and services, posted falls in the interval of 12% to 17%. Year-to-date, the worst performers have been real estate (-34%), basic materials (-25%), banking (-24%), basic consumption (-21%) and telecommunications and media (-19%), while the firms that have best withstood the financial market stress are those in chemicals (cumulative 2011 gain of 11%), insurance (10%) and, to a lesser degree, oil and gas (5%), non-bank providers of financial services (3%), discretionary consumption (3%) and health and related services (2%).

Exhibit 3: “The temporary ban on short selling”

On 11 August last, the securities regulators of Belgium, France, Italy and Spain, under the coordination of ESMA, jointly decided a temporary ban on the creation or increase of short positions in financial sector shares. On 28 September, the CNMV agreed to extend this measure for the second time (the first was on 25 August) until market conditions accompany.

The precautionary ban on short selling owes to the risks posed for the stability and orderly functioning of markets by the extreme volatility which for the past few months has gripped European stock markets and, particularly, financial sector shares. This situation, it is feared, could lead to disorderly markets and provoke downward price spirals in determined shares driven by investor panics or, even, manipulative rumours or information.¹ Financial institutions have been singled out for their importance in the preservation of financial stability and the containment of systemic risk. In particular, their need to raise funds continuously makes them vulnerable to the destructive dynamics of the “self-fulfilling prophecy” whereby a falling share price pushes up their cost of funding.

But despite these pretendedly preventive or stabilising effects, there is no denying that this kind of ban can impede the action of certain indicators of the quality of market functioning. Indeed numerous studies conducted in the past few years have found that restrictions on short sales curtail market efficiency and liquidity.² And certainly in their absence, market participants have a narrower transactional range to choose from (lower liquidity) and can extract less reliable information from market prices (lower efficiency).

The experience of the Spanish market since the short selling ban was imposed last August is illuminating with regard to these effects. As we can see from the upper panel in the figure below, the average bid-ask spread of banks has widened in comparison with that of Ibx 35 shares unaffected by the ban, evidencing some deterioration in the formers’ liquidity.³ But the mid panel shows that the prohibition has allowed bank shares as a whole to outperform the rest of the market, though this boost effect appears to fade with time.⁴ The lower panel, finally, confirms that the ban has done much to reduce the high volatility that had plagued bank shares, particularly in the days before its application.

The empirical evidence therefore suggests that disallowing short sales has helped reduce the volatility of target shares, although its apparently lasting consequences for their liquidity endorse the wisdom of lifting the ban as soon as market conditions so allow. In this respect, the CNMV stated in its 28 September communication that the ban would be maintained for as short a time as possible, and that it would continue to coordinate its work, though ESMA, with that of other European regulators operating similar restrictions, in order to make regular assessments of the market situation.



The upper panel tracks the bid-ask spread of a wide range of companies subject or otherwise to the prohibition. The affected companies are in this case the banks (our analysis excludes two financial services providers and two insurance firms for the sake of a homogeneous sample). The companies unaffected are all those listed on the Ibex 35 when the ban was imposed. Liquidity is defined by reference to relative bid-ask spread. The central panel shows the cumulative outperformance of target shares since the prohibition date, defined as the difference in each share's return relative to the return of the Ibex 35. The lower panel charts the volatility gap between target and non-target companies, based on data for the 22 trading days prior to the prohibition date. In all three panels, the value 0 on the Y-axis corresponds to 11 August 2011, while negative and positive values indicate the number of trading days before and after the ban respectively.

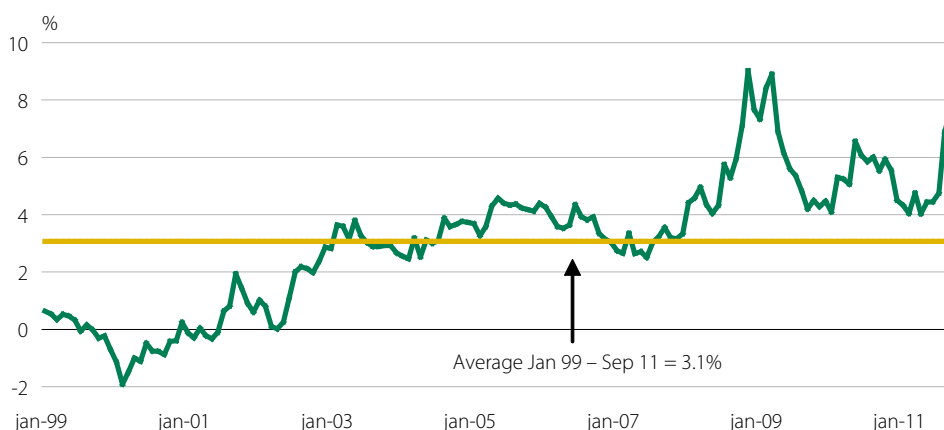
- 1 See I. Goldstein and A. Guembel (2008), "Manipulation and the allocational role of prices", in *Review of Economic Studies*, vol. 75, pp. 133-164, discussing how certain manipulation strategies involving short sales can have a lasting adverse impact on a company's earnings (damage to client, supplier and investor perceptions, costlier access to external finance, etc.).
- 2 See for instance 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; D. Abreu and M. Brunnermeier (2003), "Bubbles and crashes", in *Econometrica*, vol. 71, pp. 173-204; and H. Hong and J. Stein (2003), "Differences of opinion, short-sales constraints, and market crashes", in *Review of Financial Studies*, vol. 16, pp. 487-525.
- 3 This analysis confines itself to the shares of the banking institutions targeted by the ban, and therefore excludes four non-banking financial companies. The full list of issuers whose shares comes under the prohibition can be consulted on <http://www.cnmv.es/>
- 4 The first two results concur with the international evidence gathered by A. Beber and M. Pagano (2011), "Short-selling bans around the world: evidence from the 2007-09 crisis", to be published shortly in the *Journal of Finance*. The authors, however, make no assessment of bans' impact on share price volatility.

The P/E of the Ibox 35 prolonged its descent as far as 8 times approximately in the third quarter, below the level of year-end 2010 (around 10) and in line with other European indices. The earnings yield gap, which reflects the return premium required to be invested in equity versus long-term government bonds, turned up sharply in August, after charting an even course for most of the year, and by mid-September was running at 7.7% (4.3% in early August), at a distance from both its start-out level (4.9%) and its average since 1999 (3.1%).

The P/E of the Ibox 35 contracts sharply in the third quarter...

Earnings yield gap¹ of the Ibox 35

FIGURE 13

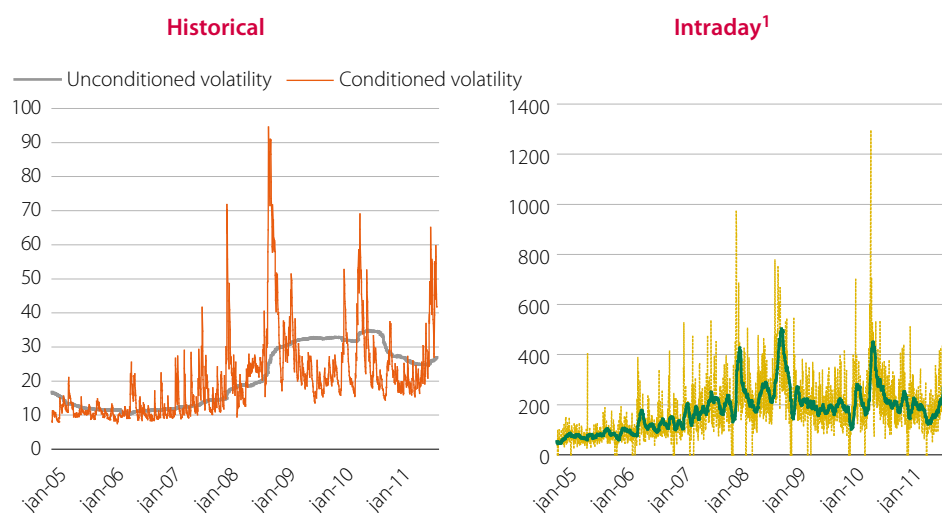


Source: Thomson Datastream and CNMV.

- 1 Difference between stock market yield, taken as earnings/price and ten-year Spanish government yields. Monthly data to 20 September 2011.

As figure 14 shows, both historical and intraday volatility moved up a gear in the third quarter. Ibox 35 historical volatility peaked at 65% in August, close to the heights reached during the first outbreak of the European debt crisis in May 2010 but still far short of the levels observed in the fourth quarter of 2008. By mid-September, readings had eased back to 40%. Meantime, intraday volatility, taken as the difference between the index's high and low prices in each trading session, peaked at 700 points in the thick of market disruption and has since cooled considerably.

...against a backdrop of fast-rising volatility...

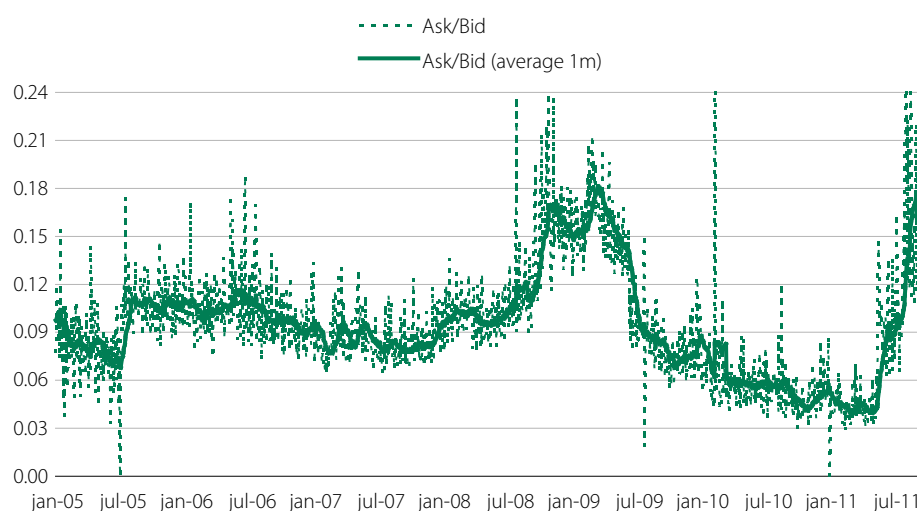


Source: Thomson Datastream and CNMV. Data to 20 September.

1 Depicting the difference between the daily price highs and lows of the Ibex 35 and the average of the last month.

...deteriorating liquidity conditions,...

This heightened volatility put the liquidity conditions of domestic equity markets under a growing strain in the second quarter which only intensified as the months progressed, with third-quarter readings resembling those of the first quarter of 2009. Specifically, the average bid-ask spread of the Ibex 35 was up to 0.14%, well above the 0.05% of the first-half period and the 0.09% average of the past six years.



Source: Thomson Datastream and CNMV. Data to 20 September.

...and a conjunctural upswing in market turnover.

Turnover on the Spanish stock market exceeded 699 billion euros in the first three quarters of 2011 (to 20 September), 2.7% less than in the same period last year. Average daily volume in the third quarter was 3.69 billion, after a year-on-year increase of 13%, just slightly below the average levels of full-year 2010 (4.05 billion euros).

The strong comeback in equity issuance over the second and the third quarter was all about the stockmarket listing of various savings banks (see table 2), as part of the restructuring of the Spanish financial system, and capital increases at already listed banks ahead of the new capital requirements to be introduced by Basel III. Issue volumes in these two quarters exceeded 11 billion euros, of which 67% corresponded to the above transactions. Between January and September, funds raised on domestic equity markets came to nearly 14.40 billion euros, rivalling the 16 billion raised in full-year 2010.

Savings banks IPOs explain the recent surge in equity issuance.

Turnover on the Spanish stock market

TABLE 7

Million euros

	2007	2008	2009	2010	1Q11	2Q11	3Q11 ¹
Electronic market	1,658,019	1,235,330	880,544	1,032,447	245,990	236,897	212,868
Open outcry	1,154	207	73	165	20	11	4
of which SICAVs ²	362	25	20	8	2	3	1
MAB ³	6,985	7,060	5,080	4,145	880	1,134	1,000
Second Market	193	31,50255	3	3	1	0	0
Latibex	868	757,88857	435	521	102	89	82
All exchanges	1,667,219	1,243,387	886,135	1,037,282	246,992	238,131	213,953
Pro-memoria: non resident trading (% all exchanges)							
	61.6	66.0	64.6	75.3	77.6	n.d.	n.d.

Source: CNMV and Dirección General de Comercio e Inversiones.

1 Cumulate data from 1 July to 20 September.

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.

Equity issues and public offerings¹

TABLE 8

	2007	2008	2009	2010	1Q11	2Q11	3Q11 ²
CASH AMOUNTS³ (million euros)	69,955	16,349	11,391	16,013	3,237	4,797.6	6,323.4
Capital increases	67,887	16,340	11,389	15,407	3,237	4,797.6	6,323.4
Of which, through POS	8,503	292	17	959	0	3,696.4	8,4
National tranche	4,821	292	15	62	0	3,696.3	8,4
International tranche	3,681	0	2	897	0	0.1	0.0
Public offerings	2,068	10	2	606	0	0.0	0.0
National tranche	1,517	10	2	79	0	0.0	0.0
International tranche	551	0	0	527	0	0.0	0.0
NUMBER OF FILINGS⁴	100	54	53	69	17	23	24
Capital increases	91	53	53	67	17	22	24
Of which, through POS	8	2	2	12	0	3	3
Of which, bonus issues	19	18	11	15	2	5	6
Public offerings	12	2	1	3	0	1	0

Source: CNMV.

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

2 Data to 20 September 2011.

3 Excluding amounts recorded in respect of cancelled transactions.

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

Exhibit 4: “Green Paper on the EU Corporate Governance Framework”

The Green Paper on Corporate Governance published by the European Commission in April 2011 puts forward a series of initiatives to improve the corporate governance of European companies, particularly those listed on regulated markets. These initiatives are spread over the four chapters into which the paper is organised:

1. General: the report raises the ideas of creating a specific corporate governance regime tailored to small and medium-sized companies and encouraging good governance codes for unlisted firms.
2. Boards of directors: it may be necessary, the Commission says, to strengthen the diversity of non-executive members, to ensure selection is based on professional qualifications, skills, and technical expertise and to require a higher level of dedication. Attention should also go to promoting greater gender diversity and a clear separation between the board chairperson and chief executive officer. Finally, it proposes introducing mandatory disclosure requirements for directors’ remuneration and remuneration policy, which should also be put to the vote of the shareholders’ meeting.
3. Shareholders: the Commission acknowledges that the current corporate governance framework rests on the assumption that shareholders feel engaged with companies and actively concerned about the quality of their management performance. Yet it has been widely observed that most shareholders take a passive, short-termist approach. For this reason, the Commission proposes a debate on ways to overcome this disinterest, increase institutional investors’ involvement in corporate governance and convince shareholders to adopt a longer-term outlook and investment strategy. It also looks at ways to strengthen minority shareholder protection vis à vis controlling shareholders in cases like related-party transactions.
4. Application of the “comply or explain” framework: the Commission expresses its concern about the shortcomings detected in the application of “comply or explain”. This occurs basically because companies’ explanations for departures from their respective codes are of poor informative quality, and because mechanisms are lacking for effective compliance monitoring. To this end, the Green Paper proposes more stringent requirements and tighter quality monitoring and analysis of the information companies supply in their corporate governance statements, over and above that performed by shareholders. The Commission refrains from comment regarding the proper functions or legal status of the authority charged with such monitoring, but solicits stakeholders’ views on what these functions should be.

The consultation round concluded on 22 July, and the European Commission will now review its proposals in the light of stakeholder responses and decide on future action at the Community level.

3.2 Fixed-income markets

The climate on domestic fixed-income markets was again dominated by the ongoing crisis in European sovereign debt markets, which gained new intensity in early August, sending Spanish government bond yields and spreads to record highs. The decision by the European Central Bank to purchase euro-area bonds on the secondary market plus other measures taken nationally helped contain the upward spiral in sovereign spreads that over the course of August had sucked in a fair proportion of Europe's economies. But nor did spreads abate to any meaningful extent. In September, both debt markets and sovereign risk premiums tensed once more amid gathering fears of a slowdown in the world economy.

In domestic fixed-income markets, government bond yields and spreads scale new heights in early August.

In this context, treasury bill rates, which had headed significantly lower in the opening quarter, began rising again to early August before falling once more in the weeks that followed. Between March and September, rates on three-, six- and twelve-month bills gained an average of 43, 92 and 100 basis points to 1.4%, 2.3% and 3.1% respectively (see table 9) – still well below the rates of late 2010 in the thick of the Irish debt crisis.

Short-term interest rates also rise on both government...

Short-term interest rates¹ (%)

TABLE 9

	Dec 08	Dec 09	Dec 10	Mar 11	Jun 11	Sep 11
Treasury bills						
3 month		0.44	1.63	0.96	1.46	1.39
6 month		0.61	2.76	1.40	1.84	2.32
12 month		0.88	3.26	2.10	2.63	3.10
Commercial paper²						
3 month	3.09	0.76	1.37	1.29	1.57	1.67
6 month	3.63	1.25	2.52	2.03	2.12	2.50
12 month	3.74	1.63	3.04	2.66	2.73	2.94

Source: Banco de España and CNMV.

1 Average daily data. September data to 20/09.

2 Interest rates at issue.

In private fixed-income markets, short-term rates dropped rather less than their public debt equivalents in the first quarter of 2011,⁸ and also rose more gently in the second and the third quarters. Hence the interest rate on three-, six- and twelve-month commercial paper climbed by 38, 47 and 28 basis points on average to 1.7%, 2.5% and 2.9% respectively.

...and corporate paper.

After an opening stretch in which rates were flat, or even falling in the case of three- and five-year maturities, long government bond yields initiated an upward trajectory in April that intensified throughout July. By the first days of August, the 10-year bond was trading at highs ahead of 6%, a reading not seen since November 1997. Thanks to the ECB's government bond purchases on the secondary market, Spanish

Long-term government yields are stabilised by ECB bond buying after reaching their highest levels since 1997.

8 In fact, average interest rates on three-month commercial paper rose slightly between December 2010 and March 2011.

government yields and those of other European economies like Italy, Portugal, Ireland and Belgium came down sharply in just a few days (by over 130 bp in Spain's case). But by early September, they were rising again as far as 3.8%, 4.5% and 5.2% at three, five and ten years respectively on the closing date for this report.

Corporate bond yields keep on rising into September.

Long-term corporate bonds performed broadly similarly over the first six months of the year, with initially falling yields giving way to a renewed increase in the second quarter. Unlike with public debt, however, the run-up in yield persisted through the third quarter. Between March and September, corporate bond yields climbed 111 bp, 83 bp and 98 bp in three-, five- and ten-year maturities respectively as far as 4.9%, 5.6% and 7.0%.

Medium and long government and corporate bond yields¹

TABLE 10

%	Dec 08	Dec 09	Dec 10	Mar 11	Jun 10	Sep 11
Government bonds						
3 year	3.05	1.95	3.87	3.41	4.07	3.82
5 year	3.41	2.67	4.65	4.30	4.70	4.45
10 year	3.86	3.75	5.38	5.25	5.48	5.22
Corporate bonds						
3 year	5.45	3.14	4.31	3.79	4.51	4.90
5 year	5.99	4.30	5.44	4.75	5.40	5.58
10 year	6.08	4.88	6.42	5.98	6.90	6.96

Source: Reuters and CNMV.

¹ Monthly average of daily data. September data to 20/9.

The rise in sovereign risk affecting Spain and other European economies...

After opening with a downward run that bottomed at 174 bp,⁹ Spanish long-term bond spreads over the German benchmark were driven higher once more as doubts grew about the sustainability of Greece's public finances and investors turned distrustful eyes on other European economies. After an early August peak of 390 bp,¹⁰ Spanish sovereign spreads tightened to below 300 bp, until renewed uncertainty at the start of September sent them back above the 360 bp mark (see figure 16).

...was largely due to doubts surrounding the sustainability of Greece's public finances...

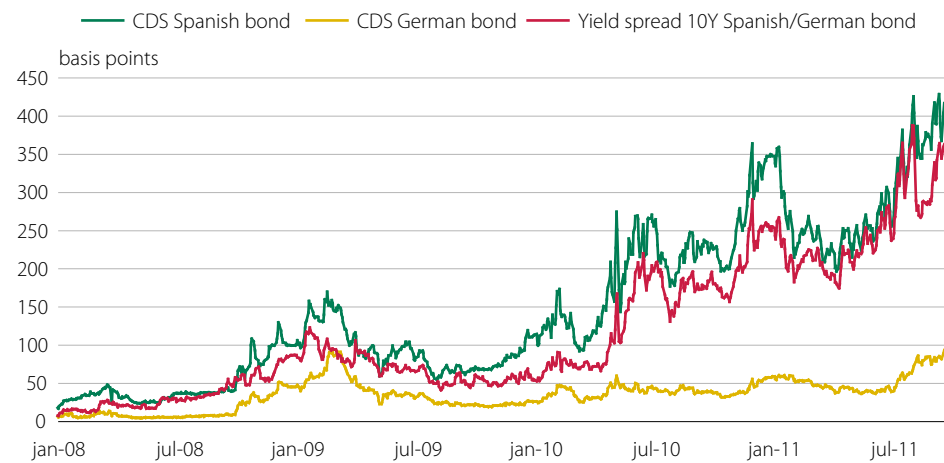
As in previous episodes of European debt market turmoil, sovereign risk contagion from more troubled economies to the rest was readily apparent. According to the estimates shown in figure 5 below, in Spain's case, over 65% of the variability in sovereign spread attributable to recent newsflow may have derived from contemporaneous shocks in Greek credit risk. This degree of contagion is consistent with the levels observed during the first Greek crisis, in May 2010, and also with estimates made for other European economies like Italy, France and Belgium.

⁹ 12 April.

¹⁰ In intraday terms, spreads at times exceeded 400 basis points.

Risk premium of Spanish government debt¹

FIGURE 16



Source: Thomson Datastream.

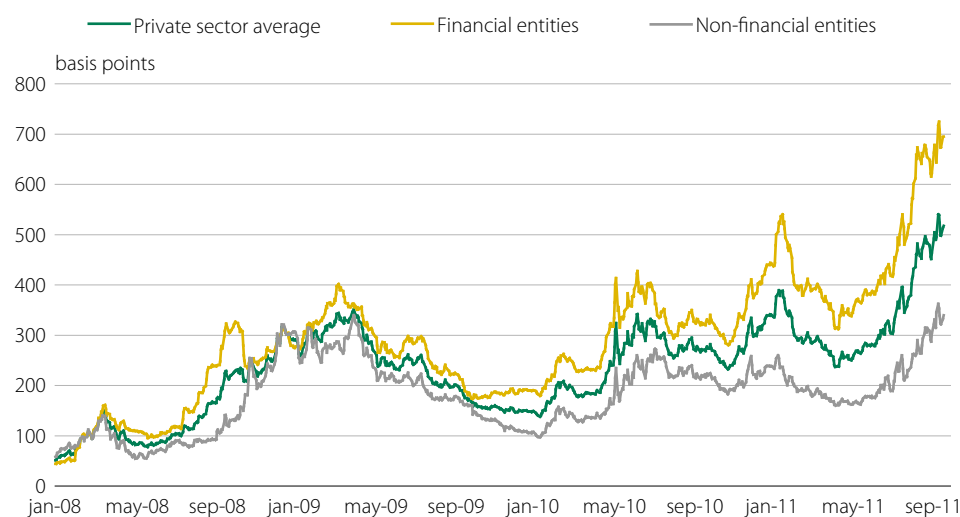
¹ Data to 20 September.

This contagion phenomenon not only shaped the risk premium movements of sovereign states but also those of a banking sector which, in Spain's case, was already immersed in an intense restructuring process. As we can see from figure 17, the average five-year CDS premiums of Spanish financial institutions climbed to highs approaching 700 bp against the average 340 bp approximately of non-financial issuers. According to the synthetic contagion indicator in figure 18, at times of maximum turbulence, a sizeable portion (around 65%) of the variability in Spanish banks' average CDS ascribable to recent newsflow may derive from contemporaneous shocks in the sovereign risk of Spanish government bonds.

...which also dragged in the area's banks.

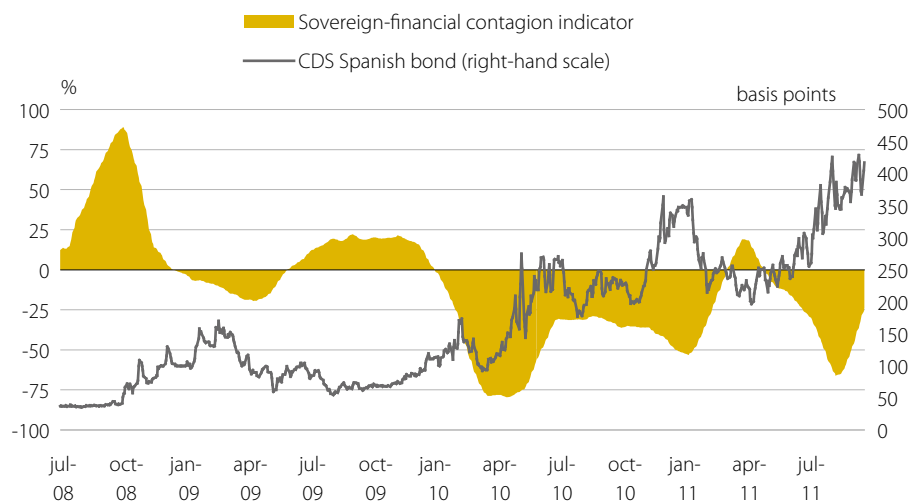
Aggregate risk premium¹ based on the five-year CDS of Spanish issuers

FIGURE 17



Source: Thomson Datastream and CNMV.

¹ Simple average. Data to 20 September.



- 1 This figure shows the percentage of variance in the average CDS indices of the Spanish banking sector and the CDS of the Spanish sovereign bond that is not attributable to their historical information but to contemporaneous return shocks. The resulting contagion indicator is decreasing with the increase in relative intensity of the impact of specific sovereign risk shocks on financial sector CDS. Positive values indicate a net contagion effect from the banking to the sovereign sector, while with negative values the source of the contagion is the sovereign risk carried by Spain. Contagion on a given day is calculated from available data for the 60 days preceding the current date, with the series also filtered by 30-day moving averages. Data to 20 September.

Exhibit 5: “Asset securitisation markets: Joint Forum recommendations”

In mid-2010, the Joint Forum received a mandate to advise its parent committees¹ and the Financial Stability Board (FSB) on developing a coordinated suite of policy responses to facilitate the regulation of sustainable securitisation markets.

In July 2011, the Joint Forum published a paper setting out the main conclusions of the work done under this mandate.² It describes the incentives which drove participation in the securitisation markets by originators, issuers, arrangers and investors before the financial crisis and analyses how those incentives have changed since then. It also reviews the academic literature on the subject and catalogues the main regulatory responses undertaken to date, considering both how they have been received by leading members of the international finance industry and how they might influence the future direction of securitisation markets.

While expressly acknowledging the potential benefits of securitisation, the Joint Forum paper also advocates reforms to correct the distortions and excesses brought to light by the financial crisis. And it is with this dual goal, of helping to stimulate securitisation markets while correcting their deficiencies, that the Joint Forum puts forward a series of recommendations directed at the competent authorities. One overarching need, it emphasises, is to develop rules that are mutually consistent, globally applicable, while allowing for local market circumstances, and implemented in a timely manner, so uncertainty about future regulation does not pose an impediment to market recovery.

The resulting recommendations are as summarised below:

1. Authorities should employ a broad tool kit to address misaligned incentives

The Joint Forum provides a checklist for action in this respect:

- Require originators or securitisers to retain an appropriate amount of risk in the securitisation transaction.
- Improve the quality of origination and underwriting practices or standards for assets eligible to be securitised.
- Provide guidance to investors on the analyses they should run to arrive at a fair valuation of securitisation products.
- Strengthen the warranties required of originators and issuers regarding the processes they have undertaken in relation to asset pools.
- Craft measures to discourage investors from relying automatically on credit ratings in reaching their decisions.
- Improve accompanying documentation to clarify the duties of advisors and service providers, including setting out obligations to manage conflicts of interest.
- Provide guidance on (or mandate) remuneration schemes which are linked to the long-term performance and quality of the assets.

2. Authorities should encourage the markets to improve transparency

The Joint Forum sees improving the quality and readability of the information available to investors and regulators as an important element of developing a sustainable securitisation market. The paper considers that this is not just a matter for the private sector, but that regulators should come actively on board by tightening up mandatory informative requirements.

3. Authorities should encourage a greater degree of document standardisation and a reduction of product complexity

The Joint Forum contends, furthermore, that the drive towards reduced product complexity and greater document standardisation should be co-led by financial institutions (in sponsoring and structuring securitisations), legal firms and investors, with the authorities providing support to their efforts. The hope is that advances on this front will reduce information asymmetries and create the foundation for a more liquid secondary market for structured products.

1 The Basel Committee on Banking Supervision (BCBS), the International Organisation of Securities Commissions (IOSCO) and the International Association of Insurance Supervisors (IAIS).

2 *Report on asset securitisation incentives*, available at <http://www.bis.org/publ/joint26.pdf>.

Sovereign debt market tensions also cut deeply into private debt issuance...

The stressed state of European sovereign debt markets also took its toll on primary bond market issuance. The volume of fixed-income issues registered with the CNMV plunged to just over 25 billion euros in the third quarter, 54% down versus the year-ago period, after a 26% advance in the first six months to 137 billion euros. This left year-to-date issuance at 162 billion, 1.3% less than in 2010 (see table 11). Financial institutions again had the fixed-income market virtually to themselves, and accounted for no less than 99% of funds captured in the period. Commercial paper remained the most popular financing instrument, with the 10.37 billion euros sold amounting to 41% of issue volumes. Next in importance were asset-backed securities (29% of the total) and covered bonds in their mortgage (17%) and territorial (10%) variants.

...with the contraction extending to all debt instruments (except covered bonds).

Covered bonds were the only instruments to escape the third-quarter stall in issuance. The biggest slide corresponded to non-convertible bonds and debentures, whose third-quarter issuance dropped to 733 million euros (-43%) for a year-to-date total of 6.63 billion (-61%).

Issuance of non-convertible bonds and debentures is down 61% year-to-date against the -3.3% of asset-backed securities...

After running ahead of last year's figures for the first six months of 2011, issuance of asset-backed securities tailed off in the third quarter to 7.45 billion euros (28.19 billion in third quarter 2010), giving a year-to-date decline of 3.3%. Note that the assets issued in securitisation deals were retained in their totality by the originators of the securitised loans, primarily for use as collateral in Eurosystem credit operations.

...while covered bonds are increasingly the debt instrument of choice.

Financial institutions retained their preference for mortgage bonds. Though third-quarter issuance of these instruments was on a rather more modest scale, the year-to-date figure is already ahead of 42 billion euros, eight thousand more than the full-year total for 2010. Also coming up fast are territorial covered bonds, with a positive change in issuance over the third quarter and year-to-date.

Foreign issuance was again a much-used resource for Spanish firms.

Foreign debt financing, again a much-used resource, conserved its relative weight in Spanish issuance at just over a third of the year-to-date total, albeit with some slippage in straight-number terms (see table 11). To 31 July, Spanish firms raised 88.39 billion euros on international markets, breaking down 50.59 billion via commercial paper and the rest via bonds and debentures.

4 Market agents

4.1 Investment vehicles

Financial UCITS¹¹

Redemptions take a further 2.5% slice from investment fund assets...

Assets under management in investment funds fell by 2.5% to just over 140 billion euros in the first six months of 2011 (see table 13), prolonging the trend initiated in 2008. The cause, once more, was net redemptions, which summed almost five billion euros in the period – nonetheless a small improvement on previous semesters. The instruments carried in investment fund portfolios appreciated slightly in the first two quarters, albeit with considerable cross-category heterogeneity. Thus, while fixed-income funds kept up positive returns throughout the first-half period, equity funds saw their first-quarter gains turn to second-quarter losses, in line with the overall performance of stock markets.

Investment fund subscriptions and redemptions (million euros)¹

TABLE 12

Category	Subscriptions				Redemptions			
	3Q10	4Q10	1Q11	2Q11	3Q10	4Q10	1Q11	2Q11
Fixed income ²	6,207	6,603	7,890	6,478	12,006	13,908	13,298	8,737
Balanced fixed income ³	572	641	358	517	812	1,384	1,138	892
Balanced equity ⁴	119	255	270	346	168	317	267	446
Euro equity ⁵	291	335	575	524	452	534	595	454
Intern. equity ⁶	779	1,227	2,489	721	626	982	2,521	801
Fixed-income guaranteed	3,404	2,506	7,424	2,595	1,414	1,719	2,008	2,224
Equity guaranteed ⁷	727	1,247	829	622	1,400	2,550	1,625	1,717
Global funds	265	1,767	1,534	836	383	1,581	507	598
Passively managed ⁸	74	96	221	149	142	254	237	108
Absolute return ⁸	959	1,334	1,166	382	1,039	1,350	1,332	1,290
Hedge funds	21	31	30	–	72	41	24	–
Funds of hedge funds	14	10	2	–	24	57	-30	–
Total	13,432	16,052	22,788	13,170	18,538	24,677	23,522	17,267

Source: CNMV.

- 1 Estimate only.
- 2 Includes: Euro and international fixed income and money market funds.
- 3 Includes: Balanced euro fixed income and balanced international fixed income.
- 4 Includes: Balanced euro equity and balanced international equity.
- 5 Includes: Euro equity.
- 6 Includes: International equity.
- 7 Includes: Guaranteed and partially guaranteed equity.
- 8 New categories as of 2Q09. All absolute return funds were previously classed as global funds.

¹¹ 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.

As we can see from table 12, fixed-income funds suffered the largest outflows – more than 7.60 billion euros – especially during the first quarter. Equity guaranteed funds were the other big losers (net redemption of almost 1.90 billion euros), while fixed-income guaranteed funds bucked the trend with net inflows of nearly 5.80 billion euros. Global funds also did well with net subscriptions exceeding 1.25 billion in the first six months of 2011. The result was a decline in the relative weight of the standard fixed-income segment in favour of fixed-income guaranteed funds. The former group saw their share drop from over 50% of total fund assets to 35% in the month of June, while fixed-income guaranteed funds rose from relative obscurity to take an industry share of 23%.

...especially in fixed-income categories.

Fund numbers dropped in the six-month period after a brief revival in the opening quarter, although the scale of decline was less than in preceding years. Finally nineteen funds ceased operation for a new total of 2,389. The main contributing factor was again fund mergers, which were nonetheless fewer than in previous quarters. Unitholder numbers too shrank by 2.3% to just over five million between end-2010 and June 2011. All categories shared in the decline except global and fixed-income guaranteed funds, where the number of participating investors rose by 17.4% and 25.4% respectively.

Both fund and unitholder totals fall once more between December 2010 and June 2011.

The latest analyses of the liquidity conditions of funds' private fixed-income holdings reveal a significant fall in the volume of less-liquid assets during the first and second quarters of 2011, from 10.64 billion at the year's outset to 9.19 billion at the end of June (see table 14). Their weight in industry assets likewise declined from the 7.4% of December 2010 to 6.6% in June, prolonging the trend initiated in 2009. This lower exposure to less-liquid instruments held true for all asset categories except high-grade financial fixed income (rated AAA/AA), which registered a slight increase. Moreover 70% of the reduction in exposure assets traced to lower holdings of less-liquid asset-backed securities; down from 3.26 billion euros at end-2010 to 2.25 billion in June 2011.

The sum of less-liquid assets drops from 7.4% of total fund assets in December 2010 to 6.6% in June 2011.

Main investment fund variables*

TABLE 13

Number	2008	2009	2010	2010		2011	
				3Q	4Q	1Q	2Q
Total investment funds inversión	2,912	2,536	2,408	2,421	2,408	2,417	2,389
Fixed income ¹	629	582	537	540	537	543	530
Balanced fixed income ²	195	169	160	162	160	158	152
Balanced equity ³	202	165	138	140	138	136	132
Euro equity ⁴	237	182	172	174	172	171	157
International equity ⁵	330	242	232	233	232	222	222
Fixed income guaranteed	260	233	276	261	276	303	324
Equity guaranteed ⁶	590	561	499	518	499	485	470
Global funds	469	187	192	189	192	197	203
Passively managed ⁷		69	61	61	61	61	57
Absolute return ⁷		146	141	143	141	141	142
Assets (million euros)							
Total investment funds	175,865.3	170,547.7	143,918.2	152,646.5	143,918.2	144,428.0	140,351.3
Fixed income ¹	92,813.1	84,657.2	56,614.6	64,102.1	56,614.6	51,565.6	49,449.9
Balanced fixed income ²	5,803.0	8,695.5	7,319.0	8,109.9	7,319.0	6,570.0	6,251.9
Balanced equity ³	3,958.8	3,879.6	3,470.5	3,520.2	3,470.5	3,484.5	3,345.6
Euro equity ⁴	5,938.9	6,321.6	5,356.8	5,504.4	5,356.8	5,656.3	5,687.2
International equity ⁵	4,254.7	5,902.4	8,037.3	7,203.6	8,037.3	7,896.1	7,751.6
Fixed income guaranteed	21,150.3	21,033.4	26,180.2	25,795.6	26,180.2	32,084.4	32,742.1
Equity guaranteed ⁶	30,873.7	25,665.8	22,046.5	23,600.0	22,046.5	21,181.6	19,827.6
Global funds	11,072.8	3,872.5	4,440.3	4,093.9	4,440.3	5,481.7	5,718.1
Passively managed ⁷		3,216.6	2,104.8	2,323.6	2,104.8	2,193.0	2,172.2
Absolute return ⁷		7,303.0	8,348.1	8,393.2	8,348.1	8,314.8	7,405.1
Unitholders							
Total investment funds	5,923,346	5,475,403	5,160,888	5,348,482	5,160,888	5,160,482	5,044,106
Fixed income ¹	2,204,652	2,041,487	1,622,664	1,745,366	1,622,664	1,525,292	1,466,938
Balanced fixed income ²	277,629	290,151	270,341	280,230	270,341	251,992	238,275
Balanced equity ³	209,782	182,542	171,336	182,860	171,336	162,861	156,631
Euro equity ⁴	377,545	299,353	266,395	280,566	266,395	253,365	248,355
International equity ⁵	467,691	458,097	501,138	502,463	501,138	493,052	493,057
Fixed income guaranteed	538,799	570,963	790,081	762,369	790,081	967,561	990,997
Equity guaranteed ⁶	1,402,948	1,188,304	1,065,426	1,115,180	1,065,426	1,027,392	981,572
Global funds	444,300	88,337	105,719	110,538	105,719	114,244	124,088
Passively managed ⁷		85,403	90,343	93,049	90,343	85,254	82,371
Absolute return ⁷		270,766	277,445	275,861	277,445	279,469	261,822
Return⁸ (%)							
Total investment funds	-4.21	5.73	0.35	1.64	-0.04	0.95	0.03
Fixed income ¹	2.06	1.91	0.11	0.63	-0.35	0.63	0.33
Balanced fixed income ²	-7.14	6.85	-0.54	1.82	-0.56	0.9	0.09
Balanced equity ³	-22.21	16.47	-0.98	4.67	0.78	2.23	-0.31
Euro equity ⁴	-39.78	32.41	-2.94	10.11	1.27	6.11	-0.45
International equity ⁵	-41.71	37.28	14.22	5.35	8.01	-0.49	-1.15
Fixed income guaranteed	3.29	3.81	-0.67	0.89	-1.28	0.89	0.36
Equity guaranteed ⁶	-2.61	3.56	-1.79	1.20	-1.45	0.71	-0.48
Global funds	-8.64	10.90	3.22	2.80	1.87	0.98	-0.14
Passively managed ⁷		-	-2.36	6.32	0.31	3.74	-0.30
Absolute return ⁷		-	1.53	1.17	0.58	0.28	-0.35

Source: CNMV. As a result of the reclassifying of investment fund objectives, in force from 1 April 2009, some changes have taken place in the variables of this table.

* Data for funds that 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.

2 Includes: Balanced euro fixed income and balanced international fixed income.

3 Includes: Balanced euro equity and balanced international equity.

4 Includes: Euro equity.

5 Includes: International equity

6 Includes: Guaranteed and partially guaranteed equity.

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

8 Annual return for 2008, 2009 and 2010. Quarterly data comprise non-annualised quarterly returns.

Type of asset	Less-liquid investments					
	Million euros			% total portfolio		
	Dec 10	Mar 11	Jun 11	Dec 10	Mar 11	Jun 11
Financial fixed income rated AAA/AA	4,374	4,335	4,391	22.4	22.5	22.8
Financial fixed income rated below AAA/AA	2,798	2,702	2,384	23.7	23.3	20.6
Non-financial fixed income	218	190	171	3.8	4.7	4.2
Securitisations	3,260	2,567	2,246	61.0	56.8	49.7
AAA-rated securitisations	1,429	919	609	62.8	74.3	49.3
Other securitisations	1,831	1,648	1,636	59.7	50.2	49.8
Total	10,651	9,794	9,192	29.2	28.1	26.0
% of investment fund assets	7.4	6.8	6.6			

Source: CNMV.

Exhibit 6: “Circular 3/2011 of 9 June modifying UCITS investment policies”

Circular 3/2011 of 9 June (BOE 27 June) partially amends CNMV Circular 1/2009 of 4 February on UCITS categories based on investment policy. The new text, which came into force two months after its publication in the *Boletín Oficial del Estado* (BOE), aims to align the definition of money market funds with the common definition issued by the Committee of European Securities Regulators (CESR), replaced in early 2011 by the European Securities and Markets Authority (ESMA), while introducing a series of technical improvements.

One of the big novelties of the amended Circular refers to the common definition of money market funds developed by the CESR (see document CESR/10-049). As a result of this new definition, the money market policy described in Circular 1/2009 is replaced by two new policies titled “short-term money market” and “money market”. This change is in order to avoid conflicting definitions circulating around Europe and thereby to ensure investors standard protection as well as clearer information about the product they are investing in.

Although short-term money market funds must meet stricter duration and maturity requirements than their money market counterparts, both products share certain core features: namely, zero exposure to equity instruments, exchange rate risk or commodities; the goal of preserving capital while providing returns in line with money market rates; subscription and redemptions on a daily basis; and investment in money market instruments and deposits complying with the terms of Article 36.1 a), e) and h) of the Regulation on Collective Investment Undertakings and Article 16 of Order EHA/888/2008 on derivative products. All instruments should be of high quality in the judgement of the management company, which should consider, at least, their credit rating (as the case may be), the asset class they represent, counterparty and operational risk in the case of structured financial products, and, finally, their liquidity profile. Regarding credit quality, the minimum requirement is to hold a short-term credit rating of at least A2 (according to the scale used by Standard & Poor’s) or equivalent from all the

agencies that have rated the instrument. If the asset has no specific rating, it should nonetheless be of an equivalent quality as determined by the management company.

The specific features of each fund category are as follows:

- Short-term money market funds: authorised to invest in other UCITS fitting the definition of short-term money market funds, average portfolio duration of less than or equal to 60 days, average portfolio maturity of less than or equal to 120 days and residual maturity to the legal redemption date of less than or equal to 397 days.
- Money market funds: authorised to invest in other UCITS fitting the definition of either short-term money market funds or money market funds, average portfolio duration of less than or equal to six months, average portfolio maturity of less than or equal to two years and residual maturity to the legal redemption date of less than or equal to 397 days. Money market funds may hold sovereign debt with a minimum rating of BBB- (on the Standard & Poor's scale) or equivalent, awarded by one or more recognised credit rating agencies.

The Circular also introduces a series of technical improvements for calculating the percentage of fixed-income and equity investment of each type of fund. For instance, it is now funds' total exposure that counts in defining its investment policy, i.e. the sum of its investments in spot and derivative instruments. Also computing for this purpose will be currency risk and investment in equity securities issued by entities from outside the euro area.

Finally, no additional exposure will be considered to arise if a fund's investments in spot or derivative financial instruments are materialised, among others, in public debt instruments issued by a state meeting the requirements set out in Article 38.2 b) of the UCITS Regulation or repos on the same, subject in both cases to maturity being of under three months and the issuer being of high credit quality.

Real estate investment schemes

The real estate investment sector loses mass in the face of manifold difficulties...

Real estate schemes continue to operate in a troubled environment, characterised by the prolonged downturn in Spanish real estate and a gathering outflow of investors since the year 2008. Latest data (for July 2011) put the number of real estate funds at seven, the same figure as in December 2010.¹² But only five of these funds were actually in operation, one of which had resumed business in March after lifting its suspension of redemptions. In four out of the five active funds, a large proportion of assets (ranging from 45% to 98%) were held by investors from the manager's financial group. All five also had at least one liquidity window in the year's first half which went ahead without incident.

¹² Although eight funds figured on the register at end-2010, one had been effectively liquidated in December. This fund finally left the register in July 2011.

As we can see from table 15, assets under management in real estate funds contracted in the first six months, though less so than in the three preceding years, especially 2008. By July 2011, funds had 5.98 billion euros assets in their charge, 2.2% less than at end-2010, while unitholder numbers had tumbled 58% to 31,591. Note, however, that most of the slump owed to one particular fund, where the manager's financial group invited investors so wishing to exit the scheme after its redemptions embargo came to end, subscribing for a sufficient amount to fill the resulting redemption orders. Meantime, fund returns continued to sink, though not quite as deeply as in the preceding quarters.

...leaving just five funds in active operation.

Real estate investment companies fared similarly to funds in the January to July period, though with a rather gentler decline that skimmed over three million euros off their total assets to 317 million. Shareholder numbers were unchanged at 943 while a total of eight companies remained on the register.

Real estate investment companies have a slightly smoother ride.

Main real estate scheme variables

TABLE 15

	2007	2008	2009	2010		2011		3Q ²
				2010	4Q	1Q	2Q	
FUNDS								
Number ¹	9	9	8	7	7	7	7	7
Unitholders	145,510	97,390	83,583	75,280	75,280	33,747	31,963	31,591
Assets (million euros)	8,609	7,407	6,465	6,116	6,116	6,083	5,995	5,983
Return (%)	1.3	0.7	-8.3	-4.7	-0.9	-0.67	-0.65	-0.23
COMPANIES								
Number	9	9	8	8	8	8	8	8
Shareholders	843	937	928	943	943	943	943	943
Assets (million euros)	513	372	309	322	322	320	318	317

Source: CNMV.

¹ Funds filing financial statements.

² Data for July 2011. In this case, the stated return corresponds to the month of July.

Hedge funds

Hedge funds have performed unevenly throughout the crisis, with funds of hedge funds coming out worse. This sub-sector's key variables have been deteriorating steadily since the peak levels of 2008. The number of schemes has fallen away from 40 in 2008 to just 27 in mid-2011,¹³ assets under management are down from 1.02 billion to 650 million euros and unitholder numbers have just about halved (from 8,151 in 2008 to 4,181 in May 2011). And their aggregate returns have fared no better, declining from 7.8% in 2009 to 3.1% in 2010 and close to zero in 2011.

Funds of hedge funds continue to underperform pure hedge funds...

13 A total of seven funds of hedge funds were in liquidation at the closing date for this report (with five more having advised the CNMV of their intention to liquidate).

Main hedge fund and fund of hedge fund variables

TABLE 16

	2007	2008	2009	2010		2011		
				2010	3Q	4Q	1Q	
FUNDS OF HEDGE FUNDS								
Number ¹	31	40	38	28	33	28	28	27
Unitholders	3,950	8,151	5,321	4,404	4,901	4,404	4,240	4,181
Assets (million euros)	1,000.6	1,021.3	810.2	694.9	726.8	694.9	667.2	650.3
Return (%)	-0.43	-17.8	7.85	3.15	-0.1	2.13	-0.01	-0.03
HEDGE FUNDS								
Number ¹	21	24	29	33	33	33	33	35
Unitholders	1,127	1,589	1,917	1,852	1,925	1,852	1,958	1,984
Assets (million euros)	445.8	539.4	652.0	646.2	639.3	646.2	693.5	719.0
Return (%)	0.84	-4.82	14.94	5.37	2.97	3.11	1.79	1.18

Source: CNMV.

1 Schemes that have filed financial statements.

2 Data to May. The return stated corresponds to April and May.

...which have even entered a tentative expansion phase.

Hedge funds, meantime, have seemingly pulled out of the crisis downturn and entered a new expansion phase, to judge by the year-to-date resurgence in funds in operation, unitholder numbers and managed assets. Fund returns have consistently outperformed those of the fund of hedge funds sub-sector. As table 16 shows, the number of schemes has grown each year since they were first authorised. By mid-2011, a total of 35 hedge funds were registered with the CNMV, two more than at end-2010 and six more than in 2009. Assets under management resumed solid growth in the first two quarters of 2011 after dipping slightly in 2010, while unitholder numbers traced a similar pattern. The upshot was that by mid-year 2011, hedge funds had 719 million euros under management (646 million at end-2010) and a total of 1,984 investors on the books (1,852 at end-2010).

Exhibit 7: “ESMA technical advice to the European Commission on level 2 implementing measures for the Alternative Investment Fund Managers Directive”

At end-2010, the European Commission called on ESMA to assist in preparing the level 2 measures envisaged in the Alternative Investment Fund Managers Directive or AIFMD. After due examination, ESMA published a consultation paper last summer setting out its draft advisory document and inviting feedback from external stakeholders. The definitive advice will be submitted to the European Commission on 15 November 2011. The Commission will then use its contents to draw up proposed AIFMD level 2 measures in the course of 2012 and the full legislative package will foreseeably come into force around mid-year 2013.

ESMA’s draft technical advice develops the Directive’s provisions on its scope of application, the organisational requirements of alternative fund managers,

depository appointment and duties, and transparency and leverage, as well as filling out its varied precepts on relations with third countries and supervisory cooperation. Set out below are the main contents of the draft advisory document.

Scope of application of the Directive

In fulfilment of the Commission's mandate, the document makes proposals on calculating the value of assets under management to determine where managers stand in relation to the threshold for full compliance with the Directive (100 million euros or 500 million in the case of non-leveraged closed-ended funds). On this score, the draft proposes that assets under management be calculated annually at least on the basis of the latest net asset value, including any assets acquired through leverage. It also advises a course of action for cases where managers with fewer assets and therefore subject only to registration and reporting requirements move above the full compliance threshold (the situation should not be seen as of a temporary nature if it persists for more than three months). Finally, it specifies the registration requirements binding on managers below the threshold and the procedure they should follow if they choose to seek authorisation under the AIFMD (opt-in procedure).

Organisational requirements

Regarding the organisation of alternative investment fund managers, the draft advice draws on the rules laid down in UCITS and MiFID directives, adjusted as necessary to the specifics of the alternative management sector (and the diversity of alternative investment funds in operation). It accordingly puts forward ideas for general organisational arrangements, and for the management of risk, liquidity and conflicts of interest.

Further to the level 1 obligation for alternative fund managers to maintain additional funds to cover the potential risks arising from professional negligence, the two options posed acknowledge the particularities of the alternative investment sector rather than directly applying the Capital Requirements Directive regime, which allow for no such distinctions. These options are: 0.01% of the value of assets under management, or else 0.0015% of the value assets under management plus 2% of income from management activities.

Finally, the text makes proposals on valuation (general guidelines and the recommendation that non-financial assets should be valued at least once a year), on alternative fund investments in securitisations (for compliance by both originator and manager whenever managed funds take securitisation positions – a requisite also to be applied to UCITS) and on delegation (two cases are envisaged that serve as justification for delegating tasks: when the manager can demonstrate that delegation will improve the fund's management or administration, or when certain set preconditions are met).

Depositaries

The text specifies the oversight and monitoring functions to be discharged by depositaries as well as their depository duties per se (asset custody or record-keeping in the case of assets not covered by custody, and the monitoring of cash

positions held at third-party entities). Regarding cash monitoring, two options are identified: one which requires the depositary to have a full overview of all movements in these cash accounts, and their reconciliations, and another which only requires it to verify reconciliation procedures. A similar two options are put forward for assets not covered by custody.

The depositary liability regime established in the Directive is filled out in some detail (depositaries to be obliged to replace assets under custody except when they are “lost” as a consequence of an external event beyond the reasonable control of the depositary, the consequences of which were unavoidable despite all reasonable efforts to the contrary), with attention to demarcating internal and external events for the purposes of determining such liability.

Transparency and leverage

Three methods are put forward for calculating leverage: one that measures gross leverage, another based on the commitment method employed by UCITS and a third, advanced method chosen by the manager subject to proof of its greater suitability. The text also sets out managers’ periodic reporting requirements with the authorities and investors. Specifically, a quarterly report should be provided to the authorities so ESMA can fulfil its own disclosure obligations on alternative investment funds with the European Systemic Risk Board (ESRB).

Foreign UCITS marketed in Spain

Investment by foreign UCITS marketed in Spain recedes by 3% in the first-half period...

The investment of foreign UCITS marketed in Spain advanced 2.6% in the first quarter then fell back by 5.5% for a first-half decline of 3% (as far as 35.58 billion euros). In straight-number terms, the outflow of assets (1.10 billion euros) equated to a third of the total first-half decline of assets under management in Spanish UCITS. Meantime, the number of schemes being marketed rose from 660 at end-2010 to 695 in June 2011.

...suggesting some attenuation of their substitute role versus Spanish UCITS.

We can perhaps deduce from this setback in the asset share of foreign UCITS that the trend among investors to shift out of riskier Spanish into less risky foreign schemes has attenuated in 2011.

Outlook

Competition from bank deposits will continue to set the industry pace.

The prospects for the domestic collective investment industry remain clouded by uncertainties as investors continue to withdraw on the back of heightened risk aversion. Symptomatically, the cash redeemed from fixed-income funds is being diverted, in part at least, to perceived safer instruments such as fixed-income guaranteed funds and bank deposits, which have gone on competing strongly for investor funds. Banks’ liquidity needs have led them to offer increasingly attractive deposit rates, and this situation seems likely to persist in the short-term at least. In the sector’s favour are the competitiveness gains harnessed from the numerous fund mergers of recent years and the increased efficiency brought by operating cost containment at fund management companies.

4.2 Investment firms

Financial market instability continued to bear down heavily on investment firm business over the first half of 2011, barring the way to a recovery based on core service revenues. The small advance in the sector's aggregate profits (1.4%) was basically a product of positive extraordinaires and operating cost containment. The sector's solvency conditions remained sound.

Financial market stress continues to weigh on investment firm business.

Broker-dealers' aggregate pre-tax profits amounted to 151 million euros in the first half of 2011, 1.7% more than in the year-ago period. The profits advance had its main origin in extraordinary items, while more recurrent income streams (fees and commissions) continued to thin out against a backdrop of rising costs, particularly depreciation and other charges (see table 17). A sharp jump (over 82%) in corporate income tax liabilities was the other factor that sent net income falling by 8.2% to 121 million euros.

Broker-dealers grow their aggregate profits 1.7% in first half 2011, thanks mainly to extraordinaires...

Net fee income dropped by 1% in the first six months to 419 million euros. Fees from order processing and execution fell by 7% to 285 million euros reflecting lower turnover in equity markets. This item, nonetheless retained its primacy among broker-dealer revenue streams, accounting for almost 70% of fee income in the period. Fees from investment advisory services managed a creditable advance of 51% to 37 million euros, while portfolio management fees rose by 24% to 7.9 million. Finally, fees from UCITS marketing were down 2.8% year-on-year at 31.3 million euros.

...while fee income slips back further.

The aggregate gross income of broker-dealers held more or less flat versus end-2010, with a small fall of 0.5% to 362 million euros. This stability resulted from the offsetting effect of movements under its component captions, with falling fee income and results from financial investments countered by higher net interest income and a substantial fall in exchange losses. Further down the income sheet, net operating income dropped 4.4% to 142.7 million, due to rising operating costs (1.5%) and, above all, heftier charges for depreciation and other provisions.

Broker-dealer gross margin holds at 2010 levels.

Brokers managed to grow their pre-tax profits by 7% over the year-ago period to 5.8 million euros. Improvement, as in previous years, was sourced from sharply falling operating costs, which moved down 15% in year-on-year terms to 43 million euros. These cost savings did enough to offset deterioration at the gross income line (a fall of 12% to 50.2 million euros) and permitted a 14% advance in net operating income to 5.6 million euros. The fee income contributing most of gross margin sank by over 11% in the reference period, with most investment services sharing in the fall.

Broker pre-tax profits advance 7% from January to June on operating cost containment.

Finally, the aggregate profits of **portfolio management companies** plunged over 50% in the first six months to 677,000 euros, due mainly to the disappearance of one of the sector's bigger players. This means only six firms remain in the market, two fewer than twelve months back. The approximately 28% fall in aggregate gross margin to 4.3 million euros (six million in 2010) was almost entirely a consequence of falling fee revenues, which are currently confined to portfolio management and financial advisory fees. Both net interest income and the results of financial investments moved up strongly, by 78% and 258% respectively, though their weight in earnings is minor only. Operating expenses fell by 20.4% to 3.6 million euros.

The fall in aggregate earnings of portfolio management companies is due to more firms leaving the market.

Thousand euros	Broker-dealers			Brokers			Portfolio managers		
	Jun 10	Jun 11	% var.	Jun 10	Jun 11	% var.	Jun 10	Jun 11	% var.
1. Net interest income	43,915	52,973	20.6	732	1,144	56.2	165	293	77.7
2. Net fee income	279,871	275,520	-1.6	56,876	50,423	-11.4	5,967	3,840	-35.6
2.1. Fee income	423,657	419,375	-1.0	65,412	57,899	-11.5	11,440	9,123	-20.3
2.1.1. Order processing and execution	306,583	285,047	-7.0	21,791	19,345	-11.2	-	-	-
2.1.2. Distribution and underwriting	2,906	2,830	-2.6	610	1,181	93.5	-	-	-
2.1.3. Securities custody and administration	11,218	10,887	-3.0	186	191	2.5	-	-	-
2.1.4. Portfolio management	6,366	7,911	24.3	8,808	6,760	-23.3	9,218	8,323	-9.7
2.1.5. Design and advising	24,477	37,047	51.4	1,291	2,634	104.1	719	800	11.2
2.1.6. Search and placement	7	184	2,722.1	115	538	367.8	-	-	-
2.1.7. Margin trading	5	4	-15.2	10	13	30.5	-	-	-
2.1.8. UCITS marketing	32,261	31,359	-2.8	12,004	11,097	-7.6	26	0	-100.0
2.1.9. Others	39,834	44,104	10.7	20,596	16,141	-21.6	1,477	0	-100.0
2.2. Fee expense	143,785	143,855	0.1	8,536	7,476	-12.4	5,473	5,283	-3.5
3. Result of financial investments	76,990	38,782	-49.6	-104	-54	48.1	65	233	257.6
4. Net exchange income	-38,210	-5,344	86.0	278	-225	-	16	-14	-189.1
5. Other operating income and expense	1,437	171	-88.1	-654	-1,081	-65.3	-173	-5	97.1
GROSS INCOME	364,004	362,102	-0.5	57,128	50,207	-12.1	6,040	4,347	-28.0
6. Operating expenses	209,760	212,791	1.5	50,836	43,433	-14.6	4,543	3,616	-20.4
7. Depreciation and other charges	1,776	6,538	268.2	1,430	1,209	-15.4	86	54	-37.2
8. Impairment losses	3,159	-1	-	-32	-3	90.7	0	0	-
NET OPERATING INCOME	149,310	142,774	-4.4	4,894	5,568	13.8	1,411	677	-52.0
9. Other profit and loss	-929	8,100	-	551	275	-50.1	-6	0	100.0
PROFITS BEFORE TAXES	148,381	150,874	1.7	5,445	5,843	7.3	1,405	677	-51.8
10. Corporate income tax	16,200	29,472	81.9	1,003	554	-44.8	234	187	-20.2
PROFITS FROM ONGOING ACTIVITIES	132,181	121,402	-8.2	4,443	5,289	19.1	1,170	490	-58.1
11. Profits from discontinued activities	0	0	-	0	0	-	0	0	-
NET PROFIT FOR THE YEAR	132,181	121,402	-8.2	4,443	5,289	19.1	1,170	490	-58.1

Source: CNMV.

Sectoral ROE holds at 15%...

In keeping with the year-to-date figures to June 2011, the sector's pre-tax return on equity¹⁴ (ROE) stayed flat versus the year-ago period at 15%. Disaggregating, we find that the 15.4% ROE of broker-dealers was on a par with the year-ago outcome,

14 ROE is calculated as:

$$ROE = \frac{\text{Profit before taxes (annualised)}}{\text{Equity}}$$

In which:

Equity = Capital + Share premium + Reserves – Treasury shares + Retained earnings and prior-year profit/loss – dividends and other entitlements.

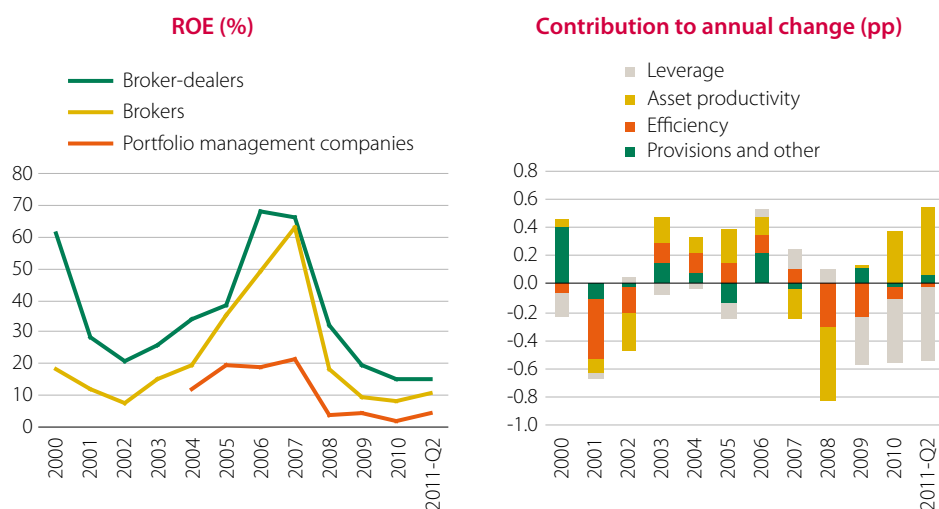
while brokers grew their ratio from last year's 9% to 10.7% in 2011. Portfolio management companies traced the opposite course with ROE down from 7.2% to 4.2%.

A look at the change factors¹⁵ for ROE in broker-dealers and broker contingents compared to 2009 and 2010 shows that the same forces were operating but with a rather different intensity. As we can see from figure 19 (right-hand panel), ROE held stable over first-half 2011 because the positive contribution of asset productivity balanced out the negative impact of lower leverage, while remaining components performed broadly as before.

...with gains from asset productivity wiped out by lower leverage.

Pre-tax ROE of investment firms

FIGURE 19



Source: CNMV.

As figure 20 shows, the number of firms reporting losses rose from 23 at end-2010 to 30 in mid-June 2011 (13 broker-dealers, 16 brokers and 1 portfolio management company). Comparing with June 2010, we find that of the 34 entities then in losses (15 broker-dealers, 16 brokers and 3 portfolio managers), 21 were in the same situation one year later (9 broker-dealers, 11 brokers and 1 portfolio management company). Despite the higher number of loss-making entities, the amount of their losses was 26% lower at 9 million euros.

Smaller losses at a larger number of firms...

Sector firms remained comfortably compliant with capital standards in the first half of 2011, hinting at a pain-free adaptation to the stricter requirements imposed under the 2009 solvency rules. As we can see from figure 21, the own funds of broker-dealers were 3.9 times above the minimum requirement at mid-year 2011

...while the sector remains comfortably in line with capital requirements.

15 The following equation allows us to isolate the effects of changes in each factor contributing to investment firm ROE:

$$ROE = \frac{PBT}{Equity} = \frac{PBT}{Net\ operating\ inc.} (1) \times \frac{Net\ operating\ inc.}{Gross\ income} (2) \times \frac{Gross\ income}{Assets} (3) \times \frac{Assets}{Equity} (4)$$

in which the numbered elements serve as indicators of: (1) extraordinary items in the income statement, (2) efficiency, (3) asset productivity and (4) leverage. For a fuller description of how to interpret the elements in this equation, see the exhibit "ROE breakdown" in *Securities markets and their agents: situation and outlook* in the CNMV Bulletin for first quarter 2008.

(3.7 times in June 2010), similar to the levels reported before the new regime came into force. Brokers too increased their surplus to two times the minimum (1.8 times in June 2010), albeit without matching the levels of broker-dealers. The contrast was marked by the portfolio management companies, whose own funds edged down slightly in first-half 2011 to just above the minimum standard. At the first half close, as in mid-2010, no single entity had an own funds deficit.

Number of investment firms in losses

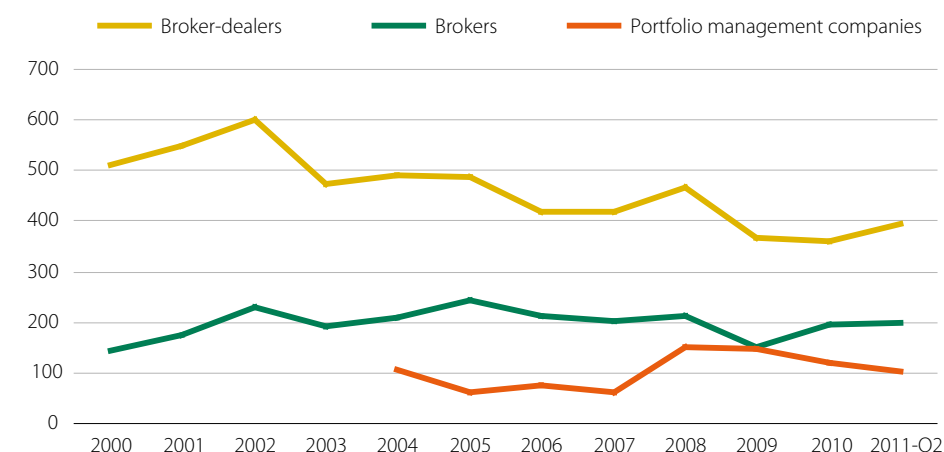
FIGURE 20



Source: CNMV.

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

FIGURE 21



Source: CNMV.

Investment advisory firms continue their push.

Investment advisory firms (IAFs), whose activity is legally confined to dispensing investment advice and guidance, have been operating in Spain since 2009 and the transposition of the Directive on Markets in Financial Instruments (MiFID). By mid-2011 a total of 64 such firms were registered with the CNMV (see table 18), twelve more than at end-2010 and double the number of twelve months before. Sector expansion is apparent in both the growing number of contracts signed (3,278 in June 2011 against 2,430 in December) and the volume of assets under advice, which advanced 5.2% in the first-half period to 17 billion euros. Professional clients account-

ed for 3.3% of contracts signed but 87% of assets advised (an average 136 million euros compared to the 700,000 per contract of retail customers). Finally, the fees earned by IAFs stood at over 14 million euros against the 7.7 million of first-half 2010.

The small improvement in investment firms' earnings has already been remarked upon in previous reports. Unfortunately recovery is for the moment no more than tentative and insufficiently supported on core business growth. Given the renewed downturn in financial market turnover, the prolonged drought in primary market issuance and the fragile state of the collective investment industry, providers have increasingly turned their attention to other business lines, like investment advice or portfolio management, which nonetheless bring in only a small part of their total income. So although the sector is adequately capitalised and firms are doing what they can to strengthen income statements through operating cost containment, at brokers especially, or the reduction of financial leverage, the fact is that unless financial markets conditions normalise and more headway is made in sector restructuring, the outlook is none too favourable. That said, we are unlikely to see a repeat of the profits slump experienced in the first throes of the crisis.

Although sector earnings have risen slightly, recovery drivers remain weak.

Main investment advisory firm variables

TABLE 18

Million euros			2009	2010	2011	
	2009	2010	2Q	1Q	2Q	1Q
NO. OF ENTITIES	16	52	16	36	52	64
ASSETS UNDER ADVICE¹	1,411	16,122	1,411	11,930	16,122	16,968
1. Retail customers	364	1,709	364	1,164	1,709	2,091
2. Professional customers	1,047	14,321	1,047	10,746	14,321	14,787
3. Others	0	92	0	19	92	91
NO. OF CONTRACTS	317	2,430	317	1,789	2,430	3,278
1. Retail customers	293	2,343	293	1,732	2,343	3,161
2. Professional customers	24	80	24	53	80	109
3. Others	0	7	0	4	7	8

¹ Data at period end. Periodicity of six months.

4.3 UCITS management companies

The managed assets of UCITS management companies fell by 1.2% to 175.5 billion euros in the first half of 2011. The was much less severe a decline than in previous years¹⁶ – just two billion euros in absolute terms – but still meant industry volumes stayed stuck at the level of the late 1990s (see figure 22 and table 19).

Assets under management in UCITS management companies drop by 1.2% in the year's first half...

This decline in managed assets was reflected in a 3.8% slide in UCITS managers' first-half profits as far as 282 million euros.¹⁷ Management fees too receded slightly to 0.87% of assets in June 2011 (see table 19), while aggregate return on equity held more

...translating as a 3.8% fall in the sector's aggregate earnings.

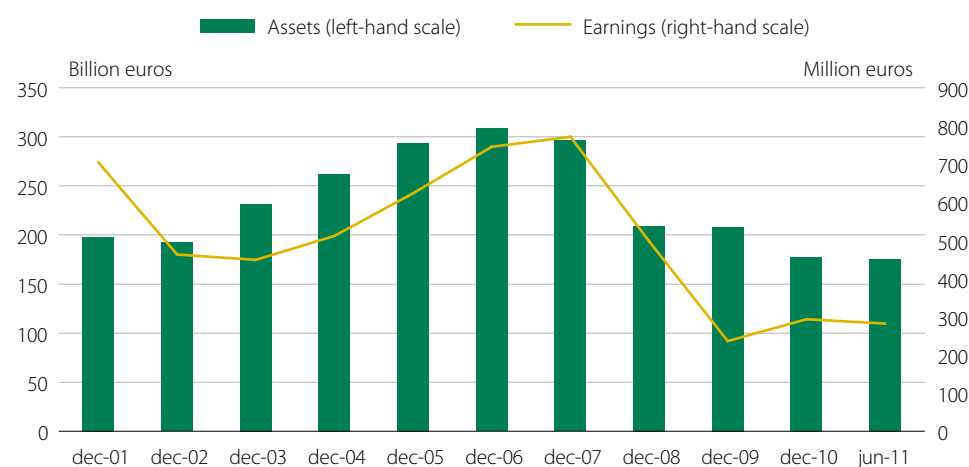
¹⁶ The steepest fall since the onset of crisis was in 2008, when the industry lost over 87 billion euros with respect to 2007.

¹⁷ Annualised profits.

or less flat at around 20%. Finally, although the number of loss-making companies was up to 35, one more than in December 2010, their combined losses fell to around half (ten million euros in annual terms), repeating the pattern of the previous year.

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

FIGURE 22



Source: CNMV. The profits figure to June 2011 has been restated on an annual basis.

The impact of financial sector restructuring is making itself felt.

In the first half of 2011, UCITS management companies pressed on with the task of streamlining their investment fund offerings by means of multiple inter-product mergers. At the same time, financial sector restructuring has meant the reorganisation of certain companies. Indeed of the five managers that ceased operation in the first half of 2011, three did so as the result of the wider restructuring process.

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

TABLE 19

Year	Assets under management	UCITS management fee income ²	Average UCITS management fee (%)	Fee ratio (%) ¹
2002	192,099	2,259	1.18	72.7
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	203,379	1,702	0.84	68.6
2010	177,676	1,622	0.91	68.1
2011 (June ²)	175,458	1,532	0.87	67.0

Source: CNMV.

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

2 Data for fee income and average management fees are restated on an annual basis.

4.4 Other intermediaries: venture capital

The register of venture capital entities (VCEs) has recorded 13 new entrants and 10 retirements since year-end 2010. The number of venture capital funds and venture capital management companies in operation rose by three and four in net terms in the first three quarters of 2011, taking their respective totals to 111 and 79. Conversely, the number of venture capital companies dropped from 150 at end-2010 to 146 in September 2011 after a run of retirements (nine).

Movements in the VCE register in 2011

TABLE 20

	Situation at 31/12/2010	Entries	Retirements	Situation at 20/09/2011
Entities	333	13	10	336
Venture capital funds	108	4	1	111
Venture capital companies	150	5	9	146
Venture capital management companies	75	4	0	79

Source: CNMV.

The annual statistics kept at the CNMV put the end-2010 assets of venture capital funds at a total of 3.75 billion euros, an 18.2% increase with respect to 2009 (see table 21). A breakdown of assets by holder shows that institutional investors were again the majority force. In all, legal entities commanded a 95% share of total fund assets in 2010, practically the same proportion as in 2009 (95.6%), while the share corresponding to individuals fell to 5%. Savings banks and non-financial corporations maintained significant positions, with around 15% each of the fund assets held by legal persons, ahead of public authorities (13%), pension funds (11%) and foreign entities. Proportionally, investor holdings varied little between 2009 and 2010.

Venture capital funds expand their assets 18% in 2010...

The share capital of venture capital companies came to 3.95 billion euros at the 2010 close, 4.2% less than at end-2009. Ownership was more tightly concentrated than in the venture capital fund segment. Specifically, non-financial corporations were the largest holders with 38.4% of capital at the 2010 close compared to 34.8% in 2009, ahead of the savings banks with 23.5% (19.9% in 2009), other financial companies with 16.6% (17.4% in 2009) and, finally, the banks, with 10.2%. Note that this last group withdrew significantly from capital in 2010 in both absolute and relative terms.

...while the share capital of venture capital firms shrinks by 4.2%.

According to data furnished by the Asociación Española de Entidades de Capital Riesgo (ASCRI) for the first half of 2011, the sector is experiencing something of an upturn. Venture capital firms invested 1.93 billion euros over the first six months of the year, comparable to the pre-crisis levels of first-half 2007 and 66% more than in first-half 2010. International funds were again prime movers in the period, with pan-European investment accounting for 65% of the total. Sixty per cent of all transactions, whose numbers (387) varied little with respect to 2010, corresponded to expansion capital, 34% to venture capital and 4% to leveraged operations. The sectors receiving most of this investment were medicine and health (24%), other services (23%), industrial products and services (17%) and consumer goods (14%).

Venture capital entities: assets by type of investor

TABLE 21

Million euros	Venture capital funds		Venture capital companies	
	2009	2010	2009	2010
Natural persons				
Residents	139.34	183.89	79.07	81.81
Non-residents	1.80	2.54	0.39	0.59
Legal persons				
Banks	207.38	226.40	551.92	402.42
Savings banks	490.57	547.46	819.37	929.81
Pension funds	357.41	413.29	25.23	10.35
Insurance undertakings	77.39	95.02	15.83	16.20
Broker-dealers and brokers	0.00	0.00	0.89	0.00
Collective investment schemes	22.39	26.02	8.20	8.28
Domestic venture capital entities	49.46	68.46	64.39	25.42
Foreign venture capital entities	247.67	296.70	50.53	44.87
Public authorities	372.65	494.53	132.44	133.80
Sovereign funds	26.02	33.17	0.00	0.00
Other financial companies	263.84	292.51	717.45	657.82
Non-financial companies	460.91	538.34	1,436.89	1,520.16
Foreign entities	347.26	395.53	36.34	44.45
Others	108.15	137.22	187.13	78.46
TOTAL	3,172.24	3,751.08	4,126.07	3,954.44

Source: CNMV.

...but bank lending constraints continue to hamper recovery.

The latest news on the sector hints at a return to a more dynamic market. But despite a sturdy advance in sector investment over these past months and the tentative resumption of large-scale transactions, persistent difficulties of access to bank finance are hampering what could and should be a stronger recovery.

II Reports and Analyses

Return on Spanish investment funds: an analysis of its determinants

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(*) M^a Isabel Cambón Murcia is a member of the Studies, Statistics and Publications Department of the CNMV. This article is based on Working Document No. 48 of the CNMV, written by the same author and with the same title.

1 Introduction

The investment fund (IF) industry plays an important role within the financial system, since it makes it possible to channel the savings of different kinds of investors towards financial instruments of various markets and to access professional management. There is a recurring debate, the subject of many academic papers, regarding the capacity of this sector to generate above-market returns to its customers. A significant part of this literature attempting to evaluate the return on investment funds has used some type of market reference, either to make a direct comparison with the return on funds, or to construct some kind of performance metric from which to draw conclusions. The evidence found by these works at both an international and a domestic level has been indicative insofar as investment funds (especially equity income funds) do not seem to be able to better the performance of the chosen market.¹ However, notwithstanding these results, the truth is that the industry has experienced a period of great expansion both at home and abroad in recent decades, which would be hard to understand if the returns on these funds were not, in general, reasonable (see figure 1). This apparent paradox has given rise to a great many works which have looked into the factors explaining the return on investment funds and have identified certain investment-related behaviours which are not solely driven by considerations of return/risk in a strict sense.

The analysis presented in this article takes the above mentioned paradox as its starting point, but rather than compare the return on Spanish investment funds against any benchmark, this paper attempts to explain the return on those funds on the basis of a number of variables which are important to investment institutions, such as volatility, past returns, fees charged, the size of the fund or of the fund manager, the orientation of the fund, the age, etc. The empirical model used enables some of

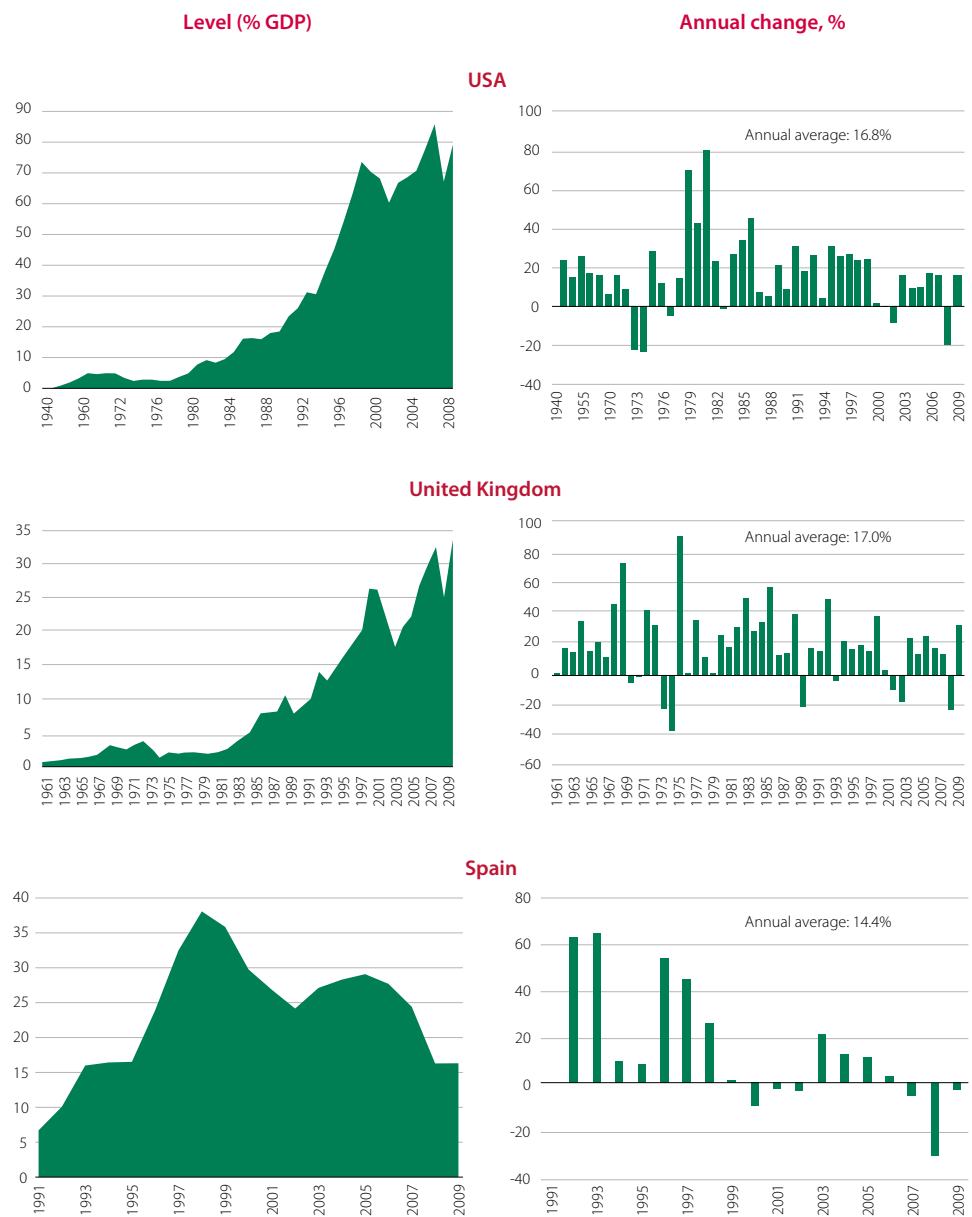
1 See Sharpe (1996), "Mutual fund performance", in *Journal of Business*, 39, pp. 119-138; Jensen (1968), "The performance of mutual funds in the period 1945-1964", in *Journal of Finance*, 23, No. 2, pp. 389-416; and Grinblatt and Titman (1989), "Performance measurement without benchmarks: An examination of mutual fund returns", in *Journal of Business*, 66, pp. 47-68; or, more recently, Malkiel (1995), "Returns from investing in equity mutual funds 1971-1991", in *Journal of Finance*, 50, pp. 549-572; Detzler (1999), "The performance of global bond mutual funds", in *Journal of Banking and Finance*, 23, pp. 1195-1217; and Edelen (1999), "Investor flows and the assessed performance of open-end mutual funds", in *Journal of Financial Economics*, 53, pp. 439-466. On the domestic front, we would highlight the papers of Ferrando and Lassala (1998), "Evaluación de la gestión de los FIAMM y de los FIM de renta fija en España en el periodo 1993-1995", in *Revista Española de Financiación y Contabilidad*, 94, pp. 197-231; Basarrate and Rubio (1999), "Non-simultaneous prices and the evaluation of management portfolios in Spain", in *Applied Financial Economics*, 9, pp. 273-281; Martínez (2001), "El puzzle de los fondos de inversión en España: un enfoque de demanda", in *Moneda y Crédito*, 213, pp. 129-154; Fernández et al. (2007), *Rentabilidad de los fondos de inversión de renta variable nacional en España 1991-2006*; and Palacios (2010), *A vueltas con los fondos de inversión españoles: nuevas sorpresas en la década 2000-2009*, IESE, Research Document DI-849.

the more recurrent hypotheses in previous literature (for example, persistence of return, or the relationship between return and the fees charged), and others of a relatively novel nature, such as the relationship between the return on the fund and its retail or institutional focus, among others, to be compared.

The article is structured in the following manner. The second section describes the data sample used in the study and the model to be estimated. The third section presents the results of the estimation for both investment funds as a whole and for the different segments of funds. Finally, in the fourth section the main conclusions are presented.

Assets of the investment fund industry

FIGURE 1



Source: 2010 Investment Company Fact Book (USA), Investment Management Association (United Kingdom), CNMV (Spain) and Thomson Datastream.

2 Data and methodology

In the last decade, 2000-2009, the aggregate annual return in net terms (i.e. excluding expenses) of Spanish investment funds as a whole has ranged from -4.2% to 5.7% (see table 1). There are substantial differences between the returns of the various categories of funds as a result of the different degree of risk assumed by each one. Fixed income funds have shown a more stable return, ranging from 1.5% to 3.7%. Conversely, returns on equity funds suffered from truly significant fluctuations in the last decade, with years in which losses were close to 40%, at the critical moments of the crisis, or gains were over 30%, depending on the state of the stock market at the time. Returns on mixed funds (fixed income and equity) are somewhere in the middle, depending on the relative importance of the investments made in fixed income or equity securities. Finally, the return on guaranteed funds, depending on their composition, has ranged from 0.8% to 4.5% in the fixed income category and from -2.6 to 4.7% in the equity income category.

Annual return on investment funds (%)

TABLE 1

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Total¹	-1.9	-1.6	-3.6	4.2	3.4	5.0	5.6	2.7	-4.2	5.7
Fixed income ²	3.3	3.7	2.7	1.8	1.7	1.5	2.0	2.7	2.1	1.9
Mixed fixed income ³	-0.1	-1.0	-3.6	3.7	3.8	5.0	4.2	1.9	-7.1	6.9
Mixed equity income ⁴	-6.9	-7.3	-17.0	10.1	6.2	11.9	10.3	2.7	-22.2	16.5
Euro equity income ⁵	-11.0	-13.8	-30.1	23.8	15.3	21.4	27.3	6.1	-39.8	32.4
International equity income ⁶	-15.8	-20.6	-33.2	12.8	7.0	25.6	13.4	1.5	-41.7	37.3
Guar. fixed income	3.8	4.4	4.5	2.4	2.6	1.7	0.8	2.8	3.3	3.8
Guar. equity income ⁷	-1.2	0.1	1.1	3.3	4.1	4.0	4.7	2.4	-2.6	3.6
Global funds	-6.1	-11.8	-12.7	4.8	2.2	6.2	4.1	1.5	-8.6	10.9
For comparison purposes:⁸										
Ibex 35	-21.7	-7.8	-28.1	28.2	17.4	18.2	31.8	7.3	-39.4	29.8
Eurostoxx 50	-2.7	-20.2	-37.3	15.7	6.9	21.3	15.1	6.8	-44.4	21.1
Treasury Bills (1-3 m)	4.7	3.1	2.7	2.0	2.0	2.5	3.5	3.9	1.8	0.4
Treasury Bills (12 m)	4.5	3.2	2.6	2.2	2.2	2.8	3.8	4.1	1.9	0.9
Govt. Debt (10 y)	5.2	5.1	4.3	4.3	3.6	3.3	4.0	4.4	3.9	4.0
Private fixed income (12 m)	4.8	3.4	2.9	2.4	2.5	3.0	4.1	4.8	3.3	1.4

Source: Thomson Datastream, Bank of Spain and CNMV.

- 1 Neither passive management funds nor absolute return funds, created in 2009, are included, since not even one full year of data is available.
- 2 Up to 1Q09 includes: short-term fixed income, long-term fixed income, international fixed income, monetary funds and FIAMM (the latter until 2006). Since 2Q09 includes: Euro fixed income, international fixed income and monetary funds.
- 3 Up to 1Q09 includes: mixed fixed income and mixed international fixed income. Since 2Q09 includes: mixed Euro fixed income and mixed international fixed income.
- 4 Up to 1Q09 includes: mixed equity income and mixed international equity income. Since 2Q09 includes: mixed Euro equity income and mixed international equity income.
- 5 Up to 1Q09 includes: domestic equity income and Euro equity income. Since 2Q09 includes Euro equity income (which already includes domestic equity income).
- 6 Up to 1Q09 includes: international equity income Europe, international equity income Japan, international equity income USA, international equity income emergings, and international equity income others. Since 2Q09: international equity.
- 7 Up to 1Q09: guaranteed equity income. Since 2Q09: guaranteed and partially guaranteed equity income.
- 8 The annual rate of change of the equity indices (Ibex 35 and Euro Stoxx 50) are provided as are the interest rates as at 31 December of each year for fixed income instruments.

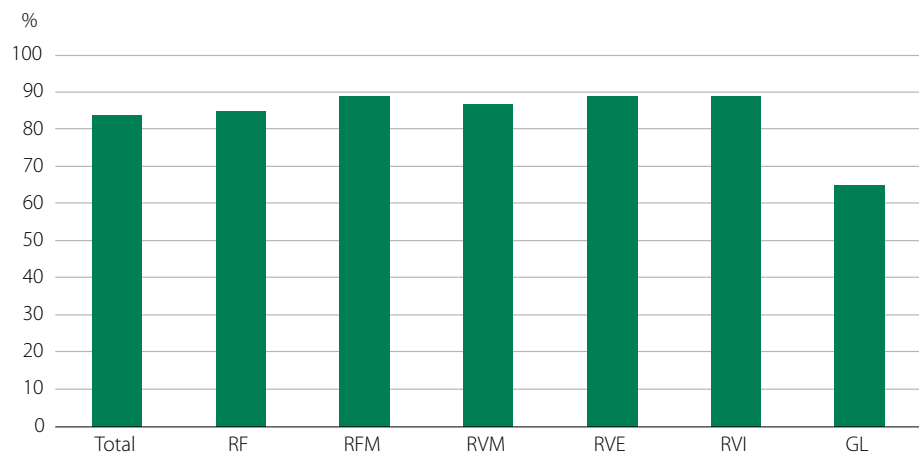
2.1 Data

The analysis presented below has been made on the basis of information that collective investment schemes (CIS) managers send regularly to the CNMV. We have taken annual data from the investment funds in existence between 2000 and 2009² for which we have a minimum of five years of observations. Fund merger processes and changes of focuses during the period under study are also incorporated into the study. Given the large number of focuses present in the investment fund industry, we decided to group them into the following categories: fixed income, mixed fixed income, mixed equity income, Euro equity income, international equity income, and global funds.³

The representativity of the final sample used by the study in terms of assets is high. As we can see in figure 2, the assets of the funds included in the sample represent around 84% of the total assets of the funds in average terms for the ten year period under study. Representativity is high in all fund categories, with assets representing between 85% and 89% of the total, save for the case of global funds where the percentage falls to 65% due to the relative youth of this category of funds.

Representativity of the sample in terms of assets¹ (%)

FIGURE 2



Source: CNMV.

1. Assets of the sample as a percentage of the total assets of the funds or of each category.

RF: fixed income, RFM: mixed fixed income, RVM: mixed equity income, RVE: Euro equity income, RVI: international equity income and GL: global funds.

2.2 Description of the empirical model

An empirical linear regression model was established⁴ in which the dependent variable is the net annual return on the fund, y_t , which is defined as the percentage

2 Except for guaranteed funds.

3 For a detailed description of the various focuses, see M.I. Cambón (2011), *Spanish mutual fund performance: an analysis of the determinants*, CNMV Working Paper Series, No. 48 (also in Spanish).

4 See Cambón (2011), *op. cit.*

variation of the net asset value of the unit between the close of one year and the close of the year before. The following were chosen as explanatory variables.

- Volatility (VOL_t), defined as the annualised typical deviation of the monthly yields of the fund in the previous twelve months.
- Net subscriptions (SN_t), defined as the quotient between the net flows of investment in the funds (net subscriptions for positive values and net redemptions for negative values) during the period under study and the assets of the fund at the beginning of that period.
- Explicit and implicit fees. We consider the two types of fees charged to investment funds: implicit fees (CGD_t), which comprise management fees (on assets or results) and custody fees, and the explicit fees, which are the subscription and redemption fees (CSR_t).
- Age of the fund ($EDAD_t$): number of years the fund has existed.
- Size of the fund ($PATF_t$): assets of the fund at the close of each year.
- Market share of the fund manager ($CUOTAG_t$): assets managed by the fund manager as a percentage of the total assets of the industry.
- Percentage of the assets of the fund in the hands of institutional investors ($INSTIT_PATRIM_t$): this variable aims to identify the focus of an investment fund with regard to the type of target client.
- Type of group to which the fund manager belongs, whether it belongs to a bank ($BANCO_t$), a savings bank ($CAJA_t$), or an independent financial group.
- Changes experienced by the investment funds during the period in question: mergers ($FUSIÓN_t$) and changes of investment focus ($CAMBIOVOC_t$).

The panels of figure 3 set out the averages of the most important variables. First of all it is important to note that the mean annual return on the funds in the sample in the reference period 2000-2009 is 1.3%. Pure and mixed fixed income funds, together with global funds beat this average. The turbulences in financial markets in the early years of the decade and at the end of it due to the financial crisis reduced the return on the riskier funds to extremely low figures, and even reached negative figures in the case of international equity income funds (-0.9%).

The average volatility of the return on the funds in the sample during the decade was 6.8%. The riskier funds showed a higher volatility (with a maximum of 12.2%), while the more conservative funds showed an average volatility of 2.7%.

For funds as a whole, average net annual subscriptions were negative during the decade. Market turbulences and competition from other financial instruments, such as high yield bank deposits, gave rise to a substantial volume of redemptions during this period. By investment focus we see that the highest relative volume of redemptions corresponds to global funds, a result which may be influenced by the sample's

smaller size due, in turn, to its relative youth. If we exclude this focus, we can see that the largest net redemptions in relative terms were in the fixed income categories.

The average custody and management fees of the funds amounted to 1.45%. All the equity income funds topped this average, with a maximum of 1.9% for international equity income funds, while the lowest management and custody fees were charged by pure fixed income funds, at 1.1%. The average subscription and redemption fees amount to 0.27%. Once again, the average is higher for equity income funds and lower for fixed income funds.

Averages of some variables of the sample

FIGURE 3



Source: CNMV.

RF: fixed income, RFM: mixed fixed income, RVM: mixed equity income, RVE: Euro equity income, RVI: international equity income and GL: global funds.

With regard to the age of funds, on average the age of fixed income funds tends to be higher than equity income funds and global funds. The size of fixed income funds is also higher on average than equity income funds, except for Euro equity income where the domestic funds raise the average. The fund manager market share variable shows that the larger fund managers are more active in pure fixed income funds, pure equity income funds, and global equity funds.

32% of the assets of the funds in the sample are in the hands of institutional investors. In this case, the equity income categories show a higher percentage of institu-

tional participation (nearly 38% in the case of international equity income funds), while for fixed income funds the average is under 30%.

With regard to which financial group the fund manager belongs to, it should be noted that 41% of the observations of the sample correspond to funds belonging to banks and nearly 36% to funds belonging to savings banks. The percentage of bank managed funds in each focus is more evenly distributed, while savings banks concentrate more on pure fixed income funds and pure equity income funds, with a much smaller share in global funds.

The percentage of funds which have undergone one or more merger processes in the period under study is 27% for the sample as a whole. By focus, the relative importance of mergers was greater for mixed fixed income funds and international equity income funds. Finally, between 2000 and 2009 a little over 19% of the funds underwent some change in focus while remaining within one of the six classifications considered in this work.

3 Results

We go on to describe the main results of the estimation of the regression equation in which the dependent variable is the net annual return on the fund and the explanatory variables are those defined in point 2.2.⁵ First of all the results for the industry as a whole are presented along with an initial comparison between the pure and mixed equity income and fixed income categories and between those and global funds (point 3.1), while in point 3.2, we do not take into account whether the funds are pure or mixed but rather their geographical focus (domestic or international).

3.1 Results for the industry as a whole and comparison between pure and mixed funds

In table 2 we present two estimations for investment funds as a whole, which differ only in the way the variable related to the fund manager's market share is presented. The first (reduced estimation) includes the variable as defined in point 2.2, while the second (broad estimation) makes a distinction between the type of group the fund manager belongs to (bank, savings bank or independent entity). Next we present the most interesting results of these estimations together with the results obtained for the categories of funds depending on whether they are pure or mixed (see table 3).

5 The estimation was made using the generalised method of moments (GMM) applied to panel data, following the methodology proposed by M. Arellano and S.R. Bond (1991), "Some tests of specification for panel data: Monte Carlo evidence and an application to employment equations", in *Review of Economic Studies*, 58, pp. 277-297; M. Arellano and O. Bover (1995), "Another look at the instrumental-variable estimation of error-component models", in *Journal of Econometrics*, 68, pp. 29-52; and D. Holtz-Eakin, W. Newey and H.S. Rosen (1998), "Estimating Vector Autoregressions with Panel Data", in *Econometrica*, 56, pp. 1371-1396.

Persistence. No evidence was found of persistence in the return on investment funds as a whole for either of the two specifications considered, neither was evidence found for any of the categories of funds considered. The majority of studies of Spanish investment funds detect a certain persistence in returns in the short term, especially in the case of equity income funds and extreme funds.⁶ If persistence is only detected under these conditions, it would seem reasonable for the coefficient related to persistence of return in our model for the universe of investment funds in the decade to be insignificant.

Volatility. Neither does the model find any positive and statistically significant effect of past volatility on the present return on the fund. However, the fact that in the course of the decade there have been several periods of turbulence of varying nature which have substantially impaired the performance of the riskier investment funds may be influencing the relationship observed between the two variables. For the funds as a whole, the relationship might possibly be more obvious if we looked at a sufficiently long period of time. By category, this positive relationship is detected in fixed income funds and in international equity income funds.

Net relative subscriptions. The rejection of the positive effect does not lend support to the smart money theory, whereby investors would demonstrate a certain skill in choosing investment funds. According to this theory, the funds which receive the highest volume of subscriptions in a given period of time tend to show a higher return in the following period.⁷ Some authors which have obtained this same result in other studies referring to the domestic fund market⁸ put it down to the tax treatment of the capital gains of the funds (something which changed in 2003 but does

6 See S. Menéndez and S. Álvarez (2000), "La rentabilidad y la persistencia de los resultados de los fondos de inversión de renta variable", in *Revista Española de Financiación y Contabilidad*, 103, pp. 15-36; J.C. Matallín and M.A. Fernández (2001), "La evaluación de los FIM de renta variable: un enfoque endógeno y multiperiodo", in *Revista Española de Financiación y Contabilidad*, 30 (107), pp. 67-102; L. Ferruz *et al.* (2003), "Analysis of performance persistence in Spanish Short Term Fixed Interest Investment Funds (1994-2002)", in *European Review of Economics and Finance*, 2 (3), pp. 1-75; A. Ciriaco and R. Santamaría (2005), "Persistencia de resultados en los fondos de inversión españoles", in *Investigaciones Económicas*, vol. XXIX (3), pp. 525-573; I. Toledo and R. Marco (2006), "¿Persisten las rentabilidades en el mercado de fondos de inversión español? Un análisis empírico para el periodo 1994-2001", in *Estadística Española*, vol. 48, No. 161, pp. 5-38; L. Ferruz *et al.* (2007), "Análisis de la persistencia en rentabilidad de los FIAMM y de los determinantes de sus comisiones", in *Revista española de financiación y contabilidad*, vol. XXXVI, No. 136, pp. 689-706; M. Ruiz (2007), *Los fondos de inversión: performance y persistencia*, Working Documento No. 26 of the CNMV; and R. Marco (2007), "Rentabilidad y crecimiento patrimonial en el mercado de fondos de inversión", in *Revista de Economía Aplicada*, No. 44 (vol. XV), pp. 41-84. At an international level, we would highlight the following papers: M. Grinblatt and S. Titman (1989), "Mutual fund performance: An analysis of quarterly portfolio holdings", in *Journal of Business*, 62, pp. 393-416; B. Malkiel (1995), "Returns from investing in equity mutual funds 1971-1991", in *Journal of Finance*, 50, pp. 549-572; S. Brown and W. Goetzman (1995), "Performance persistence", in *Journal of Finance*, 50, pp. 679-698; M. Carhart, J. Carpenter, A. Lynch and D. Musto (2000), "Mutual fund survivorship", in *Review of Financial Studies*, 15, pp. 1439-1463; and W.G. Droms and D.A. Walker (2001), "Determinants of variation in mutual fund returns", in *Applied Financial Economics*, 5, pp. 383-389.

7 The most important papers at an international level which touch upon the skill of investors when choosing funds are those of M.J. Gruber (1996), "Another puzzle, the growth in actively managed mutual funds", in *Journal of Finance*, 51, (3), pp. 783-810 and L. Zheng (1999), "Is money smart?: A study of mutual fund investors' fund selection ability", in *Journal of Finance*, 54 (3), pp. 901-933.

8 A. Ciriaco, C. Del Río and R. Santamaría (2002), "El inversor ante la elección de fondos de inversión. Algunos datos para la reflexión", in *Papeles de Economía Española*, No. 94, pp. 122-133 and Marco (2007), *op. cit.*

Estimation of the equation of the determinants of the return for the funds as a whole

TABLE 2

	Reduced estimation ¹	Broad estimation ¹
Return (t-1)	0.009 (0.941)	0.012 (0.929)
Volatility (t-1)	-0.488 (0.404)	-0.350 (0.585)
Net subscriptions (t-1)	0.010 (0.945)	0.088 (0.479)
Management and custody fees (t)	-0.137 (0.822)	0.029 (0.963)
Subscription and redemption fees (t)	2.112*** (0.004)	2.220*** (0.003)
Age of the fund (t)	-0.007 (0.910)	0.036 (0.520)
Assets of the fund (t)	-0.019 (0.906)	-0.068 (0.418)
Market share of the fund manager (t)	-0.149** (0.023)	
Market share of the fund manager (t) (BANCO)		-0.179** (0.015)
Market share of the fund manager (t) (CAJA)		-0.099 (0.352)
Market share of the fund manager (t) (INDEP)		3.214** (0.037)
Percentage of assets in the hands of institutional investors (t)	-0.413** (0.029)	-0.362* (0.066)
BANCO	7.851*** (0.000)	7.371*** (0.001)
CAJA	4.013*** (0.001)	4.817*** (0.005)
FUSIÓN	-0.180 (0.894)	0.083 (0.957)
CAMBIOVOC	-0.429 (0.542)	-0.260 (0.698)
Hypothesis tests		
m1	-2.19 (0.028)	-2.04 (0.042)
m2	-1.88 (0.060)	-1.66 (0.097)
Sargan	35.33 (0.105)	35.76 (0.121)

1 GMM estimation in orthogonal deviations that are robust to heteroscedasticity and serial correlation. As instrumental variables we use lags up to t-2 of the variable, net subscriptions and volatility variables. Estimated coefficients and p-value of the statistic t in parentheses. *. 10% significance level. **. 5% significance level. ***. 1% significance level.

m1 and m2 correspond to tests on the first- and second-order serial correlations, respectively, on first difference errors. The p-value is provided.

Sargan is a test which checks the validity of the instruments used. The p-value is provided. The null hypothesis tested is "the set of instruments used is valid", therefore a sufficiently high p-value (for example, over 0.05) would not reject the validity of the instruments.

not appear to have had a significant effect in this respect), high redemption fees, and the high level of concentration of the fund marketing channel, factors which may limit the mobility of participants between funds. By category, we can only see a significant and positive relationship between net subscriptions and the return on the funds in the mixed fixed income category.

Fees. In theory, the fact that one investment fund charges higher fees (mainly management fees) than another fund with a similar risk would be justified by the greater skill of the managers of the first fund, which ultimately would be reflected in a higher return (adjusted for risk). Generally speaking, this expected positive relationship between return and fees finds no empirical support in the most important studies.⁹ In our case, the relationship between the return on funds and management and custody fees is not significantly different from zero for investment funds as a whole (see table 2); i.e. in general terms it would seem that the funds which charge the highest fees of this type are able to obtain higher gross yields, but in a relatively similar amount to the increase in the fee.¹⁰ By focus, the estimated coefficient is positive for mixed equity income funds but negative for Euro equity income and global funds.

The negative relationship found between the performance of funds and the fees charged in the higher risk categories have also been found in other studies,¹¹ which put forward as an explanation the fact that the funds with a poorer historical or expected performance raise their fees strategically and target investors who are “less sensitive to performance” since they do not expect to be able to compete with the best funds in the market targeting more sophisticated investors. It cannot be ruled out that this mechanism may also be operating in the Spanish fund market, in which there is a high degree of concentration and in which the entities may be capable of distinguishing the sensitivity of investors to performance and, consequently, segment and optimally target their offer of funds.

Another possible explanation of this negative relationship which is found between the fees charged by funds and the return on the funds, one which is not wholly independent of the previous explanation and which may also be applicable to the Spanish funds industry, is related to the fixed marketing cost of the funds. The costs associated with the marketing of funds to participants who are going to make relatively small contributions are proportionally high for the management company of these funds. Consequently, these fund managers may have an incentive to increase the management and/or custody fee of the funds acquired by these participants in order to recoup, at least in part, the higher marketing cost.

Conversely, the coefficient estimated for subscription and redemption fees is positive and significantly different from zero; in other words, the management companies which set the highest fees for entering or leaving their funds do tend to

9 See Gruber (1996), *op. cit.* and M. Carhart (1997), “On persistence in mutual fund performance”, in *Journal of Finance*, 52, pp. 57-82.

10 Note that the return used for the estimation is expressed in net terms; i.e. discounting management and custody fees. Hence the interpretation of the result.

11 J. Gil-Bazo and P. Ruiz Verdú (2009), “The relation between price and performance in the mutual fund industry”, in *Journal of Finance*, 64 (5), pp. 2153-2183.

Estimation of the equation of the determinants of net return: single-focuses vs. mixed-focuses

TABLE 3

	TOTAL FI	RF	RFM	RVM	RVE	RVI	GL
Return (t-1)	0.009 (0.941)	-0.209 (0.372)	-0.144 (0.529)	-0.062 (0.788)	-0.006 (0.980)	0.029 (0.732)	-0.234 (0.101)
Volatility (t-1)	-0.488 (0.404)	2.079** (0.042)	3.153** (0.010)	1.622 (0.163)	2.199 (0.141)	1.729*** (0.000)	-0.125 (0.766)
Net subscriptions (t-1)	0.010 (0.945)	0.047 (0.479)	0.205** (0.043)	-0.027 (0.856)	0.043 (0.772)	0.065 (0.387)	-0.034 (0.688)
Management and custody fees (t)	-0.137 (0.822)	0.067 (0.557)	0.251 (0.168)	0.729* (0.081)	-1.168** (0.040)	0.379 (0.202)	-0.660* (0.099)
Subscription and redemption fees (t)	2.112*** (0.004)	0.004 (0.953)	-0.027 (0.641)	0.894* (0.087)	-0.029 (0.576)	0.265* (0.059)	-0.080 (0.631)
Age of the fund (t)	-0.007 (0.910)	-0.094** (0.028)	0.312 (0.229)	-1.062* (0.051)	-0.023 (0.476)	0.276 (0.174)	0.209 (0.275)
Assets of the fund (t)	-0.019 (0.906)	-0.010 (0.789)	-0.122* (0.062)	-0.070 (0.485)	0.058 (0.660)	-0.160*** (0.003)	-0.128* (0.069)
Market share of the fund manager (t)	-0.149** (0.023)	0.001 (0.897)	0.008 (0.618)	0.012 (0.741)	-0.024** (0.045)	-0.014** (0.018)	-0.004 (0.823)
Percentage of assets in the hands of institutional investors (t)	-0.413** (0.029)	-0.817* (0.099)	0.012 (0.962)	-2.403 (0.139)	-2.139* (0.052)	0.169 (0.172)	-0.111 (0.625)
BANCO	7.851*** (0.000)	4.218* (0.067)	0.158 (0.729)	1.872 (0.189)	2.860** (0.015)	1.632*** (0.009)	-0.341 (0.406)
CAJA	4.013*** (0.001)	1.992** (0.038)	-0.226 (0.565)	-0.592 (0.616)	1.414** (0.021)	0.784** (0.039)	0.122 (0.289)
FUSIÓN	-0.180 (0.894)	-0.493 (0.220)	0.249 (0.390)	0.091 (0.842)	0.085 (0.806)	1.476*** (0.001)	0.683* (0.097)
CAMBIOVOC	-0.429 (0.542)						
Hypothesis tests							
m1	-2.19 (0.028)	-2.08 (0.037)	-2.40 (0.016)	-2.04 (0.041)	-2.39 (0.017)	-4.70 (0.000)	-2.82 (0.005)
m2	-1.88 (0.060)	-0.71 (0.480)	0.22 (0.824)	-0.65 (0.517)	-1.38 (0.169)	-0.84 (0.400)	-1.87 (0.062)
Sargan	35.33 (0.105)	48.95 (0.073)	39.31 (0.175)	26.59 (0.227)	19.19 (0.158)	23.50 (0.172)	56.73 (0.078)
For comparison purposes:							
Number of funds	1,782	585	207	215	202	309	218
Number of observations	15,076	4,838	1,744	1,813	1,693	2,484	1,489

RF: fixed income, RFM: mixed fixed income, RVM: mixed equity income, RVE: Euro equity income, RVI: international equity income and GL: global funds.

GMM estimation in orthogonal deviations that are robust to heteroscedasticity and serial correlation. As instrumental variables we use lags up to t-2 of the return, net subscriptions, volatility and assets variables. Estimated coefficients and p-value of the statistic t in parentheses.

*. 10% significance level. **. 5% significance level. ***. 1% significance level.

m1 and m2 correspond to tests on the first- and second-order serial correlations, respectively, on first difference errors. The p-value is provided.

Sargan is a test which checks the validity of the instruments used. The p-value is provided. The null hypothesis tested is "the set of instruments used is valid", therefore a sufficiently high p-value (for example, over 0.05) would not reject the validity of the instruments.

compensate their participants with a higher net yield. Breaking down the results by focus, we find evidence of this in two categories of equity income (mixed equity income and international equity income), which is logical, since these types of fees are predominant in these categories of funds and practically non-existent in fixed income funds.

Age of the fund. The estimations do not detect any significant relationship between the variable related to the age of the fund and the return on that fund. That is to say, the more recent funds, which might be benefiting from more sophisticated management models, do not provide better yields. This result is consistent with other studies of the Spanish fund market, such as those of Lassala (1998)¹² and Marco (2007), and of international funds, in which even a negative relationship has been detected between the age of a fund and its return in the case of equity income funds of some European countries.

Size of the fund. The hypothesis whereby economies of scale might be exploited does not find support in the model's estimations. In this respect it is worth noting that the average size of Spanish funds is very small in comparison with European funds and even smaller compared with US funds, so it may be that Spanish funds may not be large enough for economies of scale to have any significant effect on their returns. The substantial increase in the number of mergers between funds in the last two years may lead to a more appropriate offer of funds in the future.

Some authors suggest that the negative relationship between size and return that they found is explained by the fact that larger funds tend to have a more diversified portfolio and, therefore, a lower risk and also a lower return.¹³ This hypothesis is partially compatible with some of the findings we obtain in this work in the estimations by focus, in which we find this positive relationship between volatility and return on funds and a negative relationship between size and return.

A final explanation for this negative relationship between size and return on funds may be linked to the characteristics of the firms which manage the larger funds. As we will see in the following paragraph, the estimated relationship between the size of the fund manager and the return on the fund is negative.

Size of the fund manager. The reduced estimation of the model identifies a negative relationship between the net return of the fund and the size of its fund manager (measured by market share). The results of a broad estimation for investment funds as a whole, in which we differentiate market share by the type of financial group the fund manager belongs to, show that the relationship between the return obtained by the fund and the size of the fund manager is statistically negative when the fund manager belongs to a bank, insignificant when the fund manager belongs to a savings bank, and positive in the case of independent entities. The results of both estimations suggest that large entities, mainly belonging to banks, are able to exercise considerable market power. Estimations by category find this relationship between

12 C. Lassala (1998), "Factores explicativos de las diferencias de rentabilidad financiera en los FIM de renta fija", in *Revista Española de Financiación y Contabilidad*, vol. XXVI, No. 97, pp. 1005-1031.

13 Droms and Walker, *op. cit.*

return and the market share of the fund manager to be negative in the case of pure equity income funds.

Participation of institutional investors. We find a negative relationship between the net return on funds and the percentage of their assets which are in the hands of institutional investors; i.e. those funds with a greater presence of institutional investors which, in theory, are somewhat more sophisticated and tend to show lower returns. This relationship is detected for pure fixed income funds and Euro equity income (see table 3). As far as fixed income focuses are concerned, we might expect this negative relationship to be explained in part by the fact that a substantial part of non-financial companies' cash surpluses are invested in short-term fixed income funds, about which they may not have carried out a reasonable evaluation of their return. More broadly, this negative relationship between institutional investment and the return on funds may also be due to the fact that there is a certain percentage of institutional investors whose investment in certain funds is not solely driven by considerations of the expected return/risk but pursues additional objectives.¹⁴

Type of financial group. The estimations show that fund managers belonging to banks and savings banks obtain higher returns than those belonging to other groups (independent groups). If we break the results down by focus we see that banks and savings banks obtain higher returns than the independent groups in the pure fixed income and pure equity income categories. This result coincides with the findings of Lassala (1998) and partially with those of Marco (2007).

Changes of focus and mergers. The strategic decisions taken by fund managers, such as the change of focus of the fund or its merger with another fund, generally speaking do not appear to have a significant effect on the return on the fund. By category, the estimations indicate that funds which have undergone one or more merger processes in the course of the period under study end up having higher returns in the international equity income and global funds categories.

3.2 Results based on the geographic focus of the fund

The most interesting results obtained when we segment the funds according to their geographic focus are as follows:

Persistence. Neither is evidence of persistence found in the returns of the funds if broken down by geographic focus.

Net subscriptions. We obtain a positive and significant coefficient between net subscriptions and the return on funds in categories of an international nature, either

14 The commitment of some institutional investors to investing in certain collective investment schemes, for example in socially responsible investment funds, or the institutional investor's link with the financial institution managing or marketing the fund are a couple of examples of factors other than the twin considerations of expected return and risk which may influence the investment decision of institutional investors. In this respect, we should also note the existence of significant investments of investment funds in other investment funds of the same CIS.

Estimation of the equation of the determinants of the return by geographic focus of the fund

TABLE 4

	TOTAL FI	RF	RF Int	RV	RV Int	GL
Return (t-1)	0.009 (0.941)	-0.230 (0.317)	-0.023 (0.840)	0.021 (0.918)	0.001 (0.993)	-0.234 (0.101)
Volatility (t-1)	-0.488 (0.404)	1.357* (0.094)	0.940* (0.091)	0.246 (0.738)	1.306* (0.052)	-0.125 (0.766)
Net subscriptions (t-1)	0.010 (0.945)	0.109 (0.219)	0.150* (0.072)	-0.288* (0.073)	0.260** (0.049)	-0.034 (0.688)
Management and custody fees (t)	-0.137 (0.822)	0.078 (0.574)	0.035 (0.504)	-1.599* (0.077)	0.184 (0.710)	-0.660* (0.099)
Subscription and redemption fees (t)	2.112*** (0.004)	-0.242 (0.116)	-0.158 (0.157)	-0.057 (0.359)	0.476* (0.052)	-0.080 (0.631)
Age of the fund (t)	-0.007 (0.910)	-0.075 (0.111)	-0.299** (0.026)	-0.472* (0.067)	0.338 (0.259)	0.209 (0.275)
Assets of the fund (t)	-0.019 (0.906)	-0.171* (0.057)	0.110*** (0.009)	0.237 (0.166)	0.004 (0.967)	-0.128* (0.069)
Market share of the fund manager (t)	-0.149** (0.023)	-0.031*** (0.003)	0.012* (0.058)	-0.025** (0.027)	-0.079** (0.012)	-0.004 (0.823)
Percentage of assets in the hands of institutional investors (t)	-0.413** (0.029)	-2.669** (0.013)	-0.150 (0.119)	-3.494*** (0.006)	0.156 (0.385)	-0.111 (0.625)
BANCO	7.851*** (0.000)	3.763** (0.021)	-0.099 (0.342)	3.291*** (0.006)	2.089* (0.060)	-0.341 (0.406)
CAJA	4.013*** (0.001)	1.469** (0.040)	-0.946 (0.261)	1.419*** (0.009)	1.807** (0.025)	0.122 (0.289)
FUSIÓN	-0.180 (0.894)	-0.609 (0.228)	0.012 (0.929)	-0.749 (0.192)	1.798** (0.033)	0.683* (0.097)
CAMBIOVOC	-0.429 (0.542)					
Hypothesis tests						
m1	-2.19 (0.028)	-2.72 (0.007)	-3.13 (0.002)	-2.32 (0.020)	-2.68 (0.007)	-2.82 (0.005)
m2	-1.88 (0.060)	-0.73 (0.463)	-1.27 (0.203)	-1.95 (0.052)	-0.78 (0.436)	-1.87 (0.062)
Sargan	35.33 (0.105)	42.60 (0.063)	46.46 (0.137)	16.77 (0.158)	23.44 (0.435)	56.73 (0.078)
For comparison purposes:						
Number of funds	1,782	674	116	351	374	218
Number of observations	15,076	5,609	903	2,968	2,979	1,489

RF: fixed income, RFM: mixed fixed income, RVM: mixed equity income, RVE: Euro equity income, RVI: international equity income and GL: global funds.

GMM estimation in orthogonal deviations that are robust to heteroscedasticity and serial correlation. As instrumental variables we use lags up to t-2 of the return, net subscriptions, volatility and assets variables. Estimated coefficients and p-value of the statistic t in parentheses.

*. 10% significance level. **. 5% significance level. ***. 1% significance level.

m1 and m2 correspond to tests on the first- and second-order serial correlations, respectively, on first difference errors. The p-value is provided.

Sargan is a test which checks the validity of the instruments used. The p-value is provided. The null hypothesis tested is "the set of instruments used is valid", therefore a sufficiently high p-value (for example, over 0.05) would not reject the validity of the instruments.

fixed income or equity income. Thus, in these focuses the investors seem to show a certain degree of skill in the selection of funds. However, we obtain a negative and significant coefficient between net subscriptions and the return on funds in the domestic equity income category.

Management and custody fees. The coefficient associated with this variable continues the trend of the previous section when focuses are analysed. Thus, we find a negative relationship between these fees and the return in the case of domestic equity income and global funds. Once again, for the riskier funds, those that charge higher fees of this type do not compensate the participants with higher net returns. For the rest of the categories, the coefficient is not significantly different from zero.

Subscription and redemption fees. We detect a positive relationship between explicit fees and the performance of international equity income funds. This result is similar to that of the estimations in the previous point.

Size of the fund manager. The negative relationship between the market share of the fund manager and the return on the funds which we found for the funds as a whole is maintained in the two equity income categories, while for fixed income the results are mixed. Thus, for domestic fixed income funds this relationship continues to be negative, while for international fixed income funds the relationship is significantly positive. This latter relationship can be explained by the fact that in this category the presence of fund managers belonging to savings banks or independent groups (where the relationship between market share and return is positive) is greater.

Participation of institutional investors in the fund. As has been mentioned previously, the model detects a negative relationship between the percentage of assets in the hands of institutional investors and the return on the fund in the domestic fixed income and equity income categories.

Type of financial group. We find that banks and savings banks obtain better returns than independent groups in the equity income categories and in domestic fixed income funds.

Mergers. According to estimations, funds which have undergone one or more merger processes during the period under study end up having better returns in the categories of international equity income and global funds.

4 Conclusions

In this article we present the main results of a recent study of the return on Spanish investment funds.¹⁵ This study is framed within the literature on investment funds which has attempted to find an answer to the apparent paradox arising on the one hand, from the relatively poor performance delivered by many of these products

15 See Cambón (2011), *op. cit.*

and, on the other, by their great popularity among investors. However, unlike other papers, this study does not evaluate the reasonableness of the return on investment funds, but provides an estimation of the influence of a number of different factors on that return during the period 2000-2009. The results obtained, based on the estimation of a panel data model, indicate that, for funds as a whole, current returns are not related to past returns. We also found that funds with higher management and custody fees do not always tend to compensate their participants with higher net returns.

The existence of funds which charge higher fees in the case of a certain level of returns suggests the presence of certain factors which may be limiting the mobility of investors when it comes to reassigning their savings among different funds, which gives the fund managers a certain degree of market power, especially the larger ones. In fact, the funds offered by these fund managers tend to show relatively lower returns. In this respect, it may be that, as has been suggested in previous literature, the fund managers offer products with a more modest expected return to investors who are less sensitive to performance, adjusting their fees strategically. Finally, the evidence presented in this article indicates that the age or size of the fund does not seem to have any significant influence on its performance, while the funds of fund managers belonging to banks and savings banks obtain higher net returns, particularly in the case of equity income funds.

The use of ratings in financial regulation: measures and proposals

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1 Introduction

Credit rating agencies enjoyed a sterling reputation in the financial markets until the early years of the 21st century when there was a wave of bankruptcies and accounting scandals affecting major corporations such as Enron in the United States or Parmalat in Italy.¹ The slow response of the rating agencies in these cases caused many to start to question their work and especially their independence from the issuers who contracted them and the quality of their ratings. The outbreak of these scandals prompted a wide-ranging debate in the United States and Europe on the need to review how agencies are regulated, which spawned a number of initiatives. Thus, in the United States it was decided to establish direct supervision of the agencies by the Securities and Exchange Commission (SEC), through the passing of the Credit Rating Agency Reform Act² in 2006. Europe, however, mostly opted for self-regulation by adopting the Code of Conduct published by IOSCO in 2004,³ consisting of a catalogue of best practices for rating agencies.

The current crisis has put the work of the rating agencies under the microscope once again. In particular, the quality of their work regarding the rating of securitisation assets during the years immediately prior to the outbreak of the financial crisis was called into question. In particular, the low quality of these ratings was evidenced by the successive downgrades which affected many products that had initially received the highest possible credit rating. This phenomenon was especially common in the United States (see figure 1). In fact, in the case of the United States, the considerable percentage of defaults in securitisation issues made in the period immediately prior to the crisis also suggests the existence of an upward bias of the initial ratings (see figure 2).

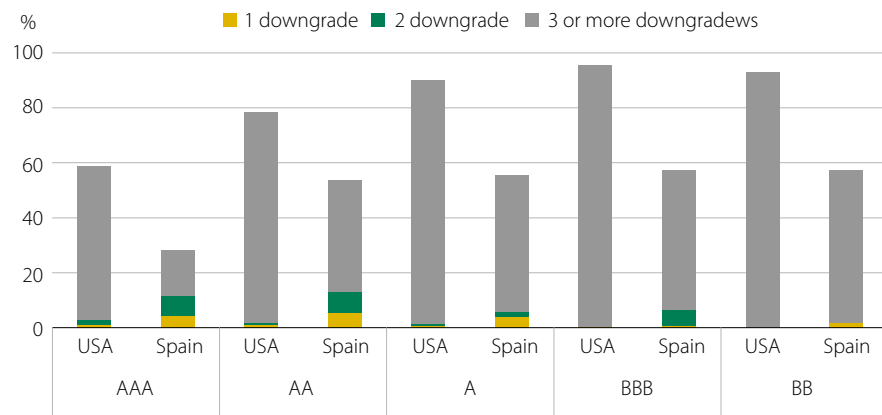
1 Enron filed for bankruptcy protection late in 2001, both in the United States and in Europe. Meanwhile, the Parmalat case became public in 2003.

2 See US Congress (2006), Credit Rating Agency Reform Act of 2006 (S. 3850).

3 See IOSCO (2004), *Code of Conduct Fundamentals for Credit Rating Agencies*, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD180.pdf>

Downgrades of mortgage-backed securities per issue rating¹

FIGURE 1

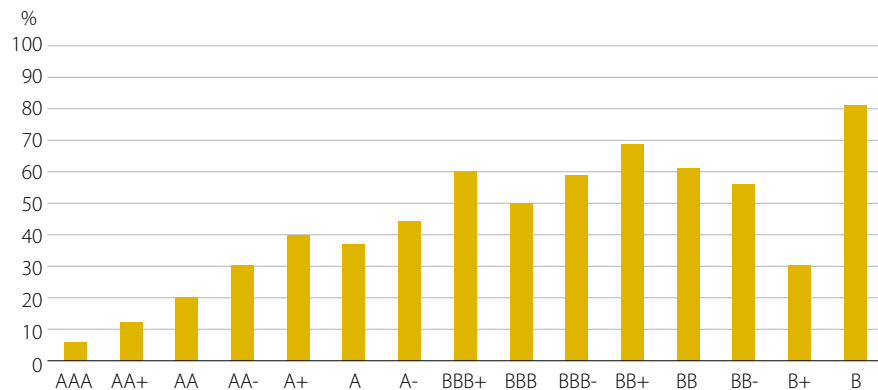


Source: Standard and Poor's and CNMV.

1 Percentage of securities suffering one, two and three or more downgrades of their credit rating after their issue, between the first quarter of 2005 and the third quarter of 2007. The + and – signs appended to the ratings are included in each category on the horizontal axis (for example, AA includes AA+, AA and AA-). Data as at 29 October 2009.

Percentage of US mortgage-backed securities in default, classified according to their issue rating¹

FIGURE 2



Source: Standard and Poor's.

1 Percentage of asset-backed securities issued from the first quarter of 2005 to the third quarter of 2007. Data as at 29 October 2009.

The reasons why the ratings assigned in the period prior to the crisis did not properly reflect the credit risk of securitisation issues are diverse and complex.⁴ Many highlight the use of ratings for the purpose of financial regulation among these reasons, pointing out that this circumstance may weaken the agencies' incentives to produce high quality ratings.

4 See, for example, P. Bolton, X. Freixas and J. Shapiro (2009), *The credit ratings game*, NBER Working Paper No. 14712; A. Ashcraft, P. Goldsmith-Pinkham and J. Vickery (2009), *The role of incentives in the rating of mortgage-backed securities*, Federal Reserve Bank of New York Working Paper; and R. Losada (2009), *Agencias de rating: hacia una nueva regulación* [Rating agencies: towards a new regulation] CNMV, Working Paper No. 34.

Thus, in principle, if the demand for ratings from the agencies only depended on the reputation of their ratings, the agencies would have a proper incentive to issue ratings of the highest possible quality. Under these conditions a drop in the quality of its ratings may not damage the agency initially, but it would later on, as soon as the investors became aware of this loss of quality. However, the situation could change substantially if the demand for a rating agency were not to depend only on its reputation but also on the regulatory value the ratings may have for those participating in the markets. In this case, many experts agree in pointing out that the intensive use of ratings in regulation weakens the role of reputation as a basic incentive to uphold the quality of ratings. With regard to securitisation issues, academic literature has shown how this weakening of the reputation mechanism significantly helped agencies to issue ratings of a less than desirable quality.⁵

The use of ratings for regulatory purposes is widespread at an international level. Among other significant examples we should mention the first version of the Capital Requirements Directive for Credit Institutions, through which Basel II was implemented in Europe, and the amendment made by the SEC in the United States to rule 15c3-1 on net capital requirements for brokers and dealers.⁶ In both regulations, the ratings of the instruments constituting the assets of financial institutions were used as basic information when determining the solvency of financial institutions. Another example which underlines the important role played by ratings in regulation is their use in the field of collective investment, specifically to limit the pool of assets in which monetary collective investment schemes can invest.⁷

In response to the perceived deterioration in the quality of ratings, several international authorities, including the Financial Stability Board and the European Commission,⁸ made recommendations and adopted measures intended to reduce the reliance of financial regulation on ratings from rating agencies. The purpose of this article is to present and provide an initial general analysis of the regulatory solutions that the various authorities have proposed for this purpose.

The article is structured as follows. In the second section we describe the use of ratings in financial regulation. In the third section we analyse the effect that ratings-based regulation has on the quality of ratings. In the fourth section we analyse recent proposals from international authorities aimed at reducing ratings-based regulation. Finally, in the fifth section we present our conclusions.

5 See D. Bongaerts, K.J. Cremers and W. Goetzmann (2009), *Multiple ratings and credit spreads*, NBER Working Paper No. 15331; A. Champsaur (2005), *The regulation of credit rating agencies in the U.S. and the E.U.: recent initiatives and proposals*, Working Paper, Harvard Law School; and J. Mason and J. Rosner (2007), *Where did the risk go? How misapplied bond ratings caused mortgage-backed securities and collateralized debt obligation market disruptions*, SSRN Working Paper No. 1027475.

6 The capital requirements directive is Directive 2006/48/EC of the European Parliament and of the Council, of 14 June 2006, on the capital adequacy of investment firms and credit institutions. Rule 15c3-1, on Net capital requirements for brokers and dealers, was reformed by the SEC on 24 November 1992 and entered into force on 1 January 1993.

7 Of particular interest, as we mention later, is the level 3 European regulation on monetary funds, see CESR (2010), *CESR's guidelines on a common definition of European Money market funds*, Document CESR/10-049).

8 See Financial Stability Board (2010), *Principles for reducing reliance on CRA ratings* (27 October) and European Commission (2010), *Public consultation on credit rating agencies* (5 November).

2 The use of ratings in financial regulation

Debt contracts typically generate a principal-agent relationship between the borrower (agent) and the lender (principal). The former tends to have more information than the latter about their own creditworthiness and, therefore, may have an incentive to provide the lender with inappropriate information. This is why lenders tend to distrust information provided by borrowers, which gives rise to a situation known in financial literature as “adverse selection”. In situations of this nature, the available information may not allow lenders to discriminate between borrowers on the basis of credit risk, which in turn may lead to borrowers with a low credit risk not finding funding at interest rates commensurate with their real situation.

In this context, rating agencies offer a service which provides an independent assessment of borrowers’ credit risks, aimed at mitigating the problems caused by asymmetric information. Their opinions, when they are of an appropriate quality, reduce the cost of accessing information for agents operating in debt markets, and help those markets to be more efficient, which is reflected in the fact that debt issuers pay margins on their debt which are better aligned with their credit risk.

As well as their role as assessors of the credit risk of issuers and issues, rating agencies are also entrusted by financial regulators to perform the important function of certification. Thus, financial regulation has been using ratings as important information for setting certain regulatory requirements. In recent decades ratings have been mainly used in three areas of regulation:

- Prudential regulation. In this area the use of ratings became appreciably more important as a result of the Basel II Capital Accord, introduced in 2004. The recommendations of this agreement considered the possibility of using the ratings issued by rating agencies to measure the credit risk associated with credit institutions’ portfolios. As mentioned earlier, the European regulation included this possibility in Directive 2006/48/EC, of the European Parliament and of the Council, relating to the taking up and pursuit of the business of credit institutions. In the United States there was also an adaptation of the rules along these same lines which, in the case of brokers in securities markets, was instrumented via a net capital rule drawn up by the SEC and included in Article 15c3-1 of the 1933 Securities Act.
- Regulation of the investment limits applicable to certain institutional investors. These restrictions particularly affect collective investment schemes and pension funds investing in high risk financial assets, normally assets with a rating lower than BBB-. In the United States one example of this type of regulation was the 1935 Banking Act, whereby national banks were obliged to buy investment grade assets. As has already been mentioned, another example, in this case in Europe, is the level 3 regulation published by the CESR in 2010, implementing Directive 2009/65/EC, of the European Parliament and of the Council, of 13 July 2009, on the coordination of laws, regulations, and administrative provisions relating to undertakings of collective investment in transferable securities (UCITS). In this level 3 regulation, short-term monetary

funds are obliged to invest in assets rated by one of the agencies operating under ESMA supervision. Also, investment of this type of funds is limited to assets whose ratings are equal to or better than the second highest rating category that the agency has on the short-term scale.

- Regulation of transparency. In some cases issuers with a high rating may benefit from a more flexible treatment in regulatory matters. Thus, for example, French legislation allows the Autorité des Marchés Financiers (AMF) to reduce the transparency requirements of issuers with higher ratings.

In addition to their use as input in various types of regulations, agencies also facilitate standardisation. The scales used by the agencies to classify their opinions on solvency enable investors to compare the risk of different debt issues, regardless of the sector, country or financial product they correspond to.

For agencies to properly carry out the three functions mentioned above (provision of information, certification and standardisation), the ratings they issue must be of an adequate quality. In fact, the idea underlying the use of ratings in regulation is that they are of high quality and faithfully reflect the credit risk of issuers and issues. However, as we will see later in this article, the intensive use of ratings for regulatory purposes may, on occasion, have had a negative impact on the quality of the ratings in the years prior to the crisis.

3 The effect of the use of ratings for regulatory purposes on the quality of those ratings

If rating agencies are to issue ratings of an appropriate quality, it is necessary for the reputation mechanism to function properly; that is to say, that the agencies must have an incentive to consistently maintain the high quality of their ratings. If the demand for rating agencies depended only on the informational value that investors ascribe to ratings, the reputation mechanism would ensure that the ratings were of the required quality. However, for certain investors with a significant weight in the market (credit institutions, institutional investors and other financial institutions), the call for credit ratings does not only depend on their informational value, but also on the usefulness of ratings when it comes to meeting certain regulatory requirements. If this component has a significant bearing on the demand for rating agencies, the incentive that the latter have to maintain their ratings at a high level may be adversely affected.

The regulators establish a number of requirements to be met before the ratings from rating agencies may be used for regulatory purposes. Thus, in the seventies, the SEC created a registration system for rating agencies wishing their ratings to be included in regulations (Nationally Recognized Statistical Rating Organisation, NRSRO). The designation of an agency as an NRSRO would require the SEC to issue a report stating that no action should be taken to prevent registration (no action letter). The designation criteria were generic and subject to a certain degree of discretion. Basically the agency's ratings had to be reliable, credible and widely used in the markets. This system was in force in the United States until 2008, the year a new NRSRO

system was introduced pursuant to the promulgation of the Credit Rating Agency Reform Act in 2006.⁹

The NRSRO designation system introduced new entry barriers in an industry which in many respects was already a natural oligopoly due to the importance of reputation, which encouraged a considerable concentration of market power in a small number of agencies. Bear in mind that if an agency is well-established in the market it will normally enjoy healthy profits. Also, if the number of potential newcomers tends to shrink, so will competitive pressure, particularly the pressure to innovate methods, with the consequent potential loss of quality of ratings in the long term.

In the literature on rating agencies, some authors provide evidence of the importance of regulatory objectives in the issue of ratings during the pre-crisis period and their impact on the quality of those ratings. In particular, Bongaerts *et al.* (2009)¹⁰ describe how in financial regulations, especially those in which investment grade issues are treated differently from speculative issues, ratings played an important role in the composition of the demand for agencies' services. In particular, these authors provide evidence that, in the corporate bond market, issuers assessed by the two main agencies only contracted a third one when there were doubts concerning whether the issuer was of investment grade. In other words, a third agency was only contracted with the purpose of ensuring that the issuer maintained or reached investment grade.

Other previous papers, such as Champsaur (2005) and Mason and Rosner (2007),¹¹ also link to a great extent the performance of rating agencies before the crisis with the regulation to which they are subject, mainly the NRSRO system of the United States. In particular, these articles show that the negative impact of the regulatory use of the ratings issued by rating agencies on their quality was especially significant in the case of securitisation issues, due to the fact that these types of issues were of great regulatory value for both issuers and investors.

In addition to their direct effect on the quality of the ratings, the use of ratings for regulatory purposes is a potential source of other negative consequences. In particular, Sy¹² describes how the use of ratings for regulatory purposes in the years prior to the current crisis caused a number of investors to base their investment on com-

9 In Europe there is also a mechanism for designating agencies whose ratings can be used for the purposes of regulation. This system is the result of Directive 2006/48/EC, of the European Parliament and of the Council, relating to the taking up and pursuit of the business of credit institutions. This directive establishes the rules that agencies must abide by for their ratings to be eligible for use in the calculation of entities' regulatory capital. The agencies which meet these requirements are called External Credit Assessment Institutions (ECAI). The requirements which an agency must meet to become an ECAI are of a diverse nature, but perhaps the most important of them is that their ratings must be recognised by the market and be considered to be credible and reliable by their users. As is the case with the NRSRO system, once an agency is designated as an ECAI it appears to be unlikely to be deprived of that status by the supervisors. Currently, in Europe, rating agencies need to be registered and come under the supervision of the European Securities and Markets Authority (ESMA) to be able to become an ECAI.

10 See note 5.

11 See note 5.

12 See A.N.R. Sy (2009), *The systemic regulation of credit rating agencies and rated markets*, IMF Working Paper 09/129.

plex products, such as asset-backed securities, without carrying out their own analysis of the advisability of such investments.

Apart from the poor quality of some of the asset-backed securities issued before the crisis, especially in the United States, it is interesting to look at the performance of the ratings of two of the main types of issues for which agencies provide ratings: corporate and sovereign issues. Various analysts and experts have pointed out that, since the outbreak of the crisis, ratings have been adjusted to reflect the credit impairment of the issuers, although the downgrades may not have been made quickly enough. These analysts and experts argue that ratings have been downgraded when the credit impairment has already been largely discounted by the market by means of the CDS market.¹³

One possible explanation of the apparent rigidity in the downgrading of ratings is the potential conflict of interest facing agencies due to the fact that it is the issuers who pay them to issue their ratings. Ratings-based regulation, mainly that which affects investors in debt, may also have contributed to this pattern in the adjustment of ratings. This type of regulation may mean that changes in ratings made by the agencies directly affect the solvency of the issuer at that moment. More specifically, a rating downgrade may cause the issuer to enter a downward spiral due to being penalised by regulations which use ratings as a reference.¹⁴ Thus, for example, regulations such as the one governing capital requirements for financial institutions, in which the credit ratings of the institutions' assets play an important role, or regulations which prevent certain collective investment schemes from investing in assets with a rating below a certain threshold, may penalise this type of institution if they invest in securities whose rating has been downgraded. As a result, such institutions will tend to avoid making investments of this kind. The degree of caution regarding this type of investment will be especially high at moments of great uncertainty in the market in respect of the solvency of the issuer. This regulatory effect may explain, at least in part, why there often tends to be a time lag between the appearance of information about the credit risk of the asset in question provided by market indicators, such as spreads in fixed income prices or CDS,¹⁵ and the agencies downgrading their ratings.

4 Regulatory proposals

The realisation that the ratings issued on asset-backed securities of the pre-crisis period were not of an adequate quality placed rating agencies at the heart of the

13 See, for example, J. Hull, M. Predescu and A. White (2004), "The relationship between credit default swap spreads, bond yields, and credit rating announcements, in *Journal of Banking and Finance*", vol. 28, pp. 2789-2811, and A. di Cesare (2006), "Do market-based indicators anticipate rating agencies? Evidence for international banks", in *Economic Notes*, vol. 35, pp. 121-150.

14 The best known regulatory effect is the *cliff effect*. This effect refers to when certain investors have to immediately dispose of part of their portfolio due to the rating of certain instruments falling below a given threshold.

15 See, for example, E. Altman and H. Rijken (2004), "How ratings agencies achieve rating stability, in *Journal of Banking and Finance*", pp. 2679-2714, and D. Lando and T. Skodeberg (2002), "Analyzing rating transitions and rating drift with continuous observations", in *Journal of Banking and Finance*, vol. 26, pp. 423-444.

debate over the causes of the financial crisis and the proposals for reform tabled by the G20. In April 2008, the Financial Stability Forum (FSF), soon to be replaced by the current FSB, made a number of recommendations aimed at improving the quality of ratings. These recommendations can be divided into two categories: in the first would be those which directly affect the performance of the agencies and in the second those which affect them indirectly.¹⁶

In the first category of measures, the FSF recommended IOSCO to review their Code of Conduct for the sector,¹⁷ which dated from 2004 and was non-binding, with a threefold purpose: to oblige agencies to take steps to avoid conflicts of interest, to allow investors to have access to the methodologies and criteria used to produce the ratings, and to increase competition in the rating agency sector. Following this recommendation, the code was reviewed that same year.¹⁸ However, both the European Union and the United States decided to take this recommendation-based approach a step further and introduced legislation to regulate and supervise the rating agencies. In the European Union, Regulation 1060/2009, of the European Parliament and of the Council, on credit rating agencies and its subsequent reform,¹⁹ called for the mandatory registration of these entities and their direct supervision by the European Securities and Markets Authority (ESMA). Similarly, in the United States, the 2006 Credit Rating Agency Reform Act, and its subsequent reform by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act, made mandatory the registration and direct supervision of rating agencies by the SEC.

In the second category of measures, as one of the main points of interest the FSF recommended that a study be made of the influence that the extensive use of ratings for regulatory purposes may have had on their quality. Subsequently, in November 2010, the FSB established a series of principles, later endorsed by the G20, in order to reduce the presence of ratings in financial regulation. The reduction proposal covered five fields: the financial supervision of banks, the investment policies of institutional investors, the operations of central banks, guarantee requirements in the trading of assets, and transparency requirements for issuers of securities. One of the main aims of these principles was to reduce the number of forced sales caused by rating changes, since such sales can exacerbate procyclicality and be a cause of systemic risk.

The FSB stated that the principles agreed upon should be implemented by means of: 1) the removal from the regulation of references to ratings issued by rating agencies and their replacement, whenever possible, by other alternative credit risk assessments and 2) the development by credit institutions, institutional investors, and

16 See Financial Stability Forum (2008), *Enhancing market and institutional resilience*, available at http://www.financialstabilityboard.org/publications/r_0904d.pdf. In this report a diagnosis is made and recommendations are presented with regard to how to improve the situation in the markets and in financial institutions. In particular, the report analysed the role of rating agencies during the crisis and proposed measures aimed at improving the quality of the ratings issued by those agencies.

17 See note 3.

18 See IOSCO (2008), *Code of Conduct Fundamentals for Credit Rating Agencies*, available at <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD271.pdf>.

19 See European Parliament and the Council of the European Union (2009), Regulation no. 1060/2009 of the European Parliament and of the Council of the European Union, of 16 September 2009, on credit rating agencies.

other participants of their own methods for assessing credit risk, so that these institutions no longer have to make investment decisions based solely on ratings issued by rating agencies.

The FSB's recommendations have already been taken into consideration, both by the Basel Committee on Banking Supervision in the production of the new capital framework for banks (known as Basel III), and in the regulatory reform carried out in the United States. In the latter country, the FSB's recommendations have already begun to be implemented. Thus, Section 939 of the aforementioned 2010 Dodd-Frank Act calls on federal agencies to review their regulations in order to replace references to ratings of issues or issuers. The US authorities call for the ratings to be replaced by other alternative credit risk measures, especially by internal models constructed by the market participants themselves. Pursuant to this mandate, the various agencies are currently discussing and proposing how to implement this measure. Specifically, the SEC has already proposed reforming the 1940 Investment Company Act to remove references to agency ratings, which particularly affects the determination of the assets eligible to form part of monetary funds. Therefore, in the near future, we can expect a considerable proportion of ratings-based regulations to disappear from financial regulation in the United States.

In the European Union, the debate as to whether there is a need to reduce ratings-based regulation is not at such an advanced stage. In November 2010, the European Commission launched a consultation document on rating agencies which was intended to cover unaddressed regulatory matters regarding these entities. One of the main issues addressed by the proposal is the reduction of the reliance on ratings by financial regulation and the manner in which such a reduction would be implemented. In particular, the document proposes reducing ratings-based regulation in three specific areas:

- In the calculation of the capital requirements of regulated entities.
- In the internal risk calculation systems of regulated financial institutions.
- In the calculation of the thresholds limiting the universe of assets in which certain institutional investors, especially UCITS and pension funds, can invest.

This reduction would be carried out by replacing credit ratings by internal models which would be designed by the entities themselves, following the general principles set out in the regulation. The measures proposed in the consultation document are expected to modify a number of European regulations. More specifically, the first objective to be set by the European Commission is to reform Directive 2006/48/EC on the capital adequacy of investment firms and credit institutions to bring it in line with Basel III rules in this matter.

In addition to the proposals of the European Commission, the Governing Council of the European Central Bank, as reported in the Annual Report for 2009, is studying the possibility of reducing reliance on ratings in Eurosystem funding operations.

As can be gathered from the arguments presented in the third section of this article, a reduction in ratings-based regulation is, on the whole, desirable, insofar as it may

help to increase the quality of ratings by strengthening the reputation mechanism in the rating agency sector. However, the replacement of ratings in financial regulation by other alternative indicators of credit risk level also has a cost attached. For example, if, as the FSB proposes, ratings-based regulation is to a large extent replaced by assessments originating from internal models developed by the entities under supervision, risk assessment costs may increase significantly for those entities, as will the cost of supervision for the public regulator.

Furthermore, there is no guarantee that entities can, as a rule, individually make better assessments of credit risk than the agencies can. In fact, even supposing that the entities made the assessments diligently, it is unlikely that all of them would have access to enough information about issuers and issues to make a proper analysis. For this reason, if the entities are to be able to make their own analyses, it would be necessary to increase the transparency of debt issuers and issues, especially in the case of securitisation issues.

In addition to the difficulty of accessing information, the fund managers of supervised entities will not always have the proper incentives to make an appropriate credit risk analysis. Generally speaking, fund managers receive a bonus when the firm makes a profit over and above a certain threshold, but their remuneration is not reduced in the same proportion when the firm makes a loss. This asymmetry may encourage the use of credit risk assessment models which allow entities to take excessive risks, as was demonstrated, for example, by the leading five US investment banks during the financial crisis. Regulation will oblige the models of supervised entities to meet certain general principles to offset these incentives, but they may not be enough to cancel them out.

Also, due to the costs involved in implementing the internal models proposed by the European Commission, especially for the smaller financial institutions, it may not be advisable to completely eliminate references to ratings. In fact, the mandatory nature of the models creates an entry barrier of a regulatory nature in the industry and, if no alternative is proposed for smaller firms, it may in the long term create a competition problem in the financial sector.

In any event, if it were decided to impose the use of internal models in supervised entities, it would be advisable not to remove other public measures of risk like ratings from the regulations. Since the incentives of fund managers are not always aligned with general interest, it would be advisable for there to be some kind of counterbalance, in this case alternative assessments, to the results delivered by internal models.

Another way to complement the information contained in ratings and reduce their role in regulation is the use of credit risk measurements based on the prices of the market instruments which contain that risk, such as the spreads of bonds or CDS.²⁰ To date, the main international authorities have been reluctant to use this type of

20 Loffler shows how measures based on market instruments were better than ratings in terms of risk, expected losses, and the measures of risk-return in a portfolio with instruments with credit risk in the years 1983 to 2002. See G. Loffler (2004), "Ratings versus market-based measures of default risk in portfolio governance", in *Journal of Banking and Finance*, vol. 28, pp. 2715-2746.

indicator in financial regulation, arguing that very often these types of instruments do not have sufficient liquidity and that their prices may be very volatile, especially at times of crisis. A high level of volatility could give rise to a procyclical effect on the capital requirements of credit institutions or an increase in forced sales in stressed scenarios, in the case of supervised entities. However, the problems associated with excess volatility could be mitigated if a monthly average or some other kind of statistic were taken as a reference to smooth out the daily price volatility of these instruments. That problem could also be minimised by taking ratings as a measurement of credit risk when the volatility of the reference market instruments exceeded a certain threshold.

5 Conclusions

The financial crisis which began in 2007 showed that the ratings which had been issued for some asset-backed securities, especially in the United States, had underestimated the credit risk which these products actually had. Although the reasons why the agencies issued ratings with a less than desirable quality are many and varied, one major factor to be taken into account is the influence of ratings-based regulation. Thus, the widespread use of ratings for reasons connected with the regulatory framework may have weakened the reputation mechanism by exposing the agencies to a demand which did not depend only on the informational value of their ratings.

In this context, a debate has recently been initiated among various authorities with responsibility for financial regulation concerning how to reduce the excessive reliance on ratings of financial regulation. In a first round of measures, the FSB recommended a review of the Code of Conduct, a voluntary code drawn up by IOSCO in 2004, with a dual objective: to make the agencies' activity more transparent and to minimise conflicts of interest between issuers and the agencies themselves. In the case of the United States and the European Union, the legislators took things a step further and amended the regulations, bringing the rating agencies' activity under the direct supervision of the SEC and the ESMA, respectively.

More recently, the FSB has shown its concern for the influence that ratings-based regulation may have had on the quality of the ratings assigned to securitisation issues prior to the crisis. Thus, in November 2010, the FSB approved a series of principles, which were endorsed by the G20, with the aim of reducing the use of ratings in financial regulation. Specifically, the FSB proposed that this reduction be effected as a general rule via the models constructed by financial market participants for their internal use.

The FSB's recommendations prompted a swift response in the United States in the form of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act which calls for a reduction in ratings-based regulation. This new law also provides for the replacement of ratings by internal models constructed by the entities participating in the market. In the case of the European Union, after a public consultation, the FSB's recommendations are expected to be implemented by means of the reform of several regulations, including, and as a priority, Directive 2006/48/EC on the capital adequacy of investment firms and credit institutions.

The aim of the measures proposed by the FSB for the reduction of the use of ratings in financial regulation is a desirable one, since it strengthens the reputation mechanism among rating agencies and, therefore, the quality of their ratings. However, the replacement of ratings by the use of internal models by the entities is not to be taken lightly. The extensive use of internal models would bring about a rise in the cost of credit risk assessment and of its supervision. In addition to these direct costs we would have to add the indirect costs resulting from increasing the transparency of issuers so that all entities would have access to the information required to make their measurements.

But perhaps the greatest drawback arising from the use of internal models is the incentives that the managers of these firms might have to make assessments underestimating the risks taken on by their entity. It is common for fund managers to receive a bonus when the firm makes a profit over and above a certain threshold, but their remuneration is not reduced in the same proportion when the firm makes a loss. Although the regulation may provide general principles for constructing these internal models, it is unlikely that they will be enough to counterbalance the managers' incentive to underestimate the risks. One way of mitigating these incentive-related problems might be to not totally eliminate the reference to ratings in the financial regulation, but rather complement them with information and analyses from internal sources and also with credit risk indicators based on market data, such as spreads in the prices of the bonds in question or in their CDS.

III Regulatory Novelties

Modifications to the securities market as a result of the Sustainable Economy Act

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1 Introduction

This article describes the main modifications introduced in the securities market by the Sustainable Economy Act 2/2011 of 4 March (hereinafter, SEA). In line with the guidelines adopted by the G-20 and the decisions of the European Union, Chapter III of the SEA includes reform measures for the financial market aimed at increasing transparency and the quality of corporate governance.

This article also describes the new aspects introduced by the SEA with regard to the powers of the CNMV. In order for the CNMV to be able to fulfil the tasks entrusted to it by the Law, the ongoing evolution of the securities market requires constant adaptation of the legal regime which regulates the supervision, inspection and disciplinary proceedings for natural and legal persons involved in the securities market.

In this regard, the Fifth, Seventh and Eighth final provisions of the SEA introduce a series of modifications aimed at strengthening and homogenising the supervision, inspection and disciplinary regime provided in the Securities Market Act 24/1988 of 28 July (hereinafter SMA), Act 35/2003 of 4 November on Collective Investment Schemes (hereinafter, CISA), and Act 25/2005 of 24 November regulating Venture Capital Firms (hereinafter, VCFA).

The article is structured into four sections: The second section analyses the new transparency requirements and corporate governance. The third section studies the modifications introduced in the supervision, inspection and disciplinary regime entrusted to the CNMV. The last section presents the final considerations.

2 Transparency and corporate governance

The SEA establishes as mandatory certain aspects relating to transparency of directors' remuneration which, until its entry into force, were recommendations of the Unified Code of Good Governance of Listed Companies.

The SEA therefore establishes that in the General Shareholders' Meetings held from 2012, listed public limited companies must submit to voting, on an advisory basis and as an item on the agenda, a report on the remuneration of their directors.

According to the Spanish legal framework, listed companies are free to follow or not the good governance recommendations, but on reporting whether they comply with them, they must respect the meaning of the items used to formulate the recommendations, especially the definitions of the type of directors.

The SEA strengthens the scope of these definitions by establishing that the information included in the Annual Corporate Governance Report¹ (hereinafter, ACGR) about the composition of the Board of Directors, its delegated committees and the classification of its directors, must be prepared in accordance with the definitions established by the Ministry of Economy and Finance or, with its express authorisation, the CNMV.

Another of the objectives of the SEA with regard to corporate governance is to improve the information which issuers publish about their internal control systems. To this end, it introduces a new heading in the ACGR in which companies must describe the characteristics of their internal control and risk management systems with regard to the process of issuing financial information.

All these new aspects are discussed in detail below.

2.1 Directors' Remuneration Report

In 2007, two reports from the European Commission were published about the level of incorporation of the Commission's recommendations published in 2004 and 2005.² The reports demonstrated that most Member States have adopted recommendations relating to the transparency of the remuneration policy into national legislation.

In Spain, these recommendations have not been established as mandatory through being included in Spanish legislation, but they have been incorporated into the Unified Code under the "comply or explain" principle.

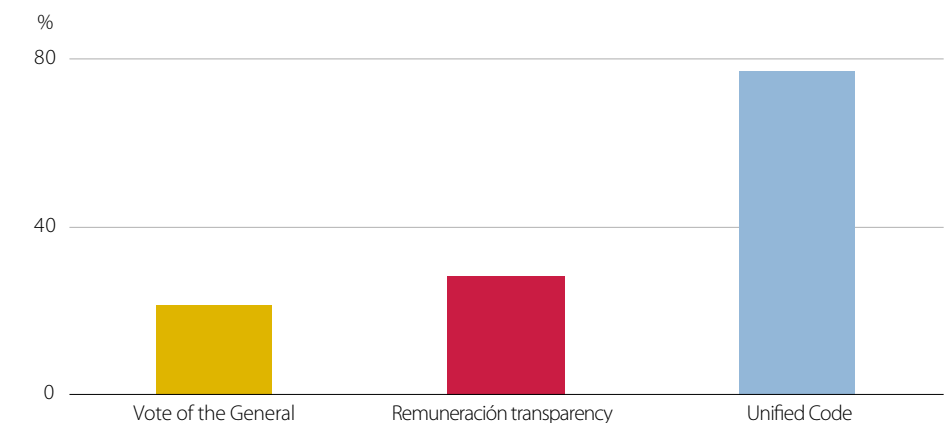
According to the declarations included in the ACGR from 2009, only two recommendations, both referring to the transparency of directors' remuneration were followed by less than one third of listed companies. Specifically these were recommendation 40 - that the Board submit a report on the directors' remuneration policy to the General Shareholders' Meeting, and number 41 - that the report breaks down individual remuneration. In the first case, compliance by listed companies amounted to 21.2% of the total and, in the second case, compliance stood at 28.2% of the total. As shown in figure 1, these compliance percentages were much lower than the average compliance with the 58 recommendations in the Unified Code.

According to the declarations included in the ACGR, in the three years that the Unified Code has been applied, there has been no significant improvement in the level of compliance with these two recommendations.

1 Listed companies must prepare an annual corporate governance report which details aspects such as the structure of ownership, the structure of the company's administration, related-party transactions, risk control systems, the General Shareholders' Meeting and the level of compliance with the corporate governance recommendations. The obligation to file this annual report is included in Article 61(2) of the SEA.

2 Recommendation 2004/913/EC fostering an appropriate regime for the remuneration of directors of listed companies, and Recommendation 2005/162/EC relating to committees of the Board.

Compliance with recommendations 40 and 41 of the Unified Code in 2009 FIGURE 1



Source: Companies' ACGR and CNMV.

The SEA has incorporated both recommendations into Spanish legislation by establishing that as from the General Shareholders' Meetings held in the first half of 2012 relating to the previous financial year, listed public limited companies must submit a report on directors' remuneration to a vote on an advisory nature and as an item on the agenda.

The report, the content of which is pending implementation by means of a ministerial order, will include full, clear and understandable information on the company's remuneration policy approved by the Board for the year in question and, where appropriate, that planned for future years.

It will also include an overall summary of how the remuneration policy was applied over the year, as well as a breakdown of the individual remuneration accrued by each one of the directors.

2.2 Update of the Unified Code

In June 2009, the European Commission published a new recommendation on the remuneration systems of directors of listed companies complementing certain aspects of those published in 2004 and 2005.

In this recommendation, the European Commission invited States to organise national consultations addressed to the interested parties and to report on the measures adopted to promote application of the recommendation so that the Commission may closely monitor and assess the need to adopt new provisions.

With the aim of complying with this European Commission recommendation, the CNMV drew up a draft update of the Unified Code of Good Governance which incorporated all the measures recommended by the European Commission and repealed the recommendations which had been included as a rule in the SEA.

The proposal for updating the Unified Code was submitted to public consultation between 17 December 2009 and 17 February 2010. Among the comments received, we can highlight the contributions from the members of the special working group

which had advised the CNMV in preparing the Code, as well as those of other persons and institutions of recognised standing.

With these contributions, an update of the Unified Code has been drawn up which includes the new recommendations of the European Commission on remuneration systems which, once the SEA has entered into force, will be submitted for approval by the Board of the CNMV.

The new recommendations which the Unified Code incorporates are as follows:

- 1 That the fixed part accounts for a sufficient percentage of total remuneration.

It is recommended that the fixed part of the remuneration is sufficiently large so that the remuneration of the dedication, qualification and responsibility which the office of director entails is adequate, even in the event that the company agrees not to pay the variable part as it considers that the director has not satisfactorily fulfilled the performance appraisal criteria.

- 2 That the variable components are linked to predetermined and measurable performance appraisal criteria.

The variable components of the remuneration should be linked to predetermined performance appraisal criteria which are measurable and which aim to encourage the sustainability of the company in the long term, including non-financial criteria.

- 3 That a part of the variable component is postponed.

It is recommended that a significant part of the variable component of the remuneration be postponed for a period of time which makes it possible to verify whether the conditions to which its payment were subject have been met.

- 4 That a deferment period of at least three years is established in share-based remuneration systems.

In order to align the interests of the directors with those of the shareholders, in share-based remuneration systems, it is recommended that the company establish a deferment period of at least three years from the company's decision to grant said remuneration.

It is also recommended that the directors are obliged to fully maintain, up to the end of their term of office, a number of shares equivalent to twice the value of their total annual remuneration, without prejudice to the disposal of the shares necessary to finance their acquisition cost.

- 5 That claw-back clauses are included.

Contractual agreements should include clauses or formulas which allow the company to claim back payment of the variable components when the payment has been made without fulfilling the conditions to which it was subject or when it was made as a result of data shown to be inaccurate.

6 That limits are placed on severance pay.

It is recommended that payments for the termination of the contract of directors do not exceed the amount of their fixed annual remuneration over two years.

7 Finally, the new recommendations assign more tasks to the remuneration committee. Specifically, said committee is entrusted to:

- Periodically review the remuneration policy applied to executive directors and senior management, and to ensure that this is proportionate to that paid to other directors and executives.
- Carry out, where appropriate, careful selection of the external advisers so as to ensure that they are not in a situation of conflict of interest.

2.3 Types of directors

One of the basic principles of the Unified Code is the existence of binding definitions. Listed companies are free to follow or not the good governance recommendations, but on reporting whether they comply with them, they must respect the meaning that the Code contributes to the concepts which it uses to formulate them.

These definitions include the classification of directors as executive, representing leading shareholders or independent as established in CNMV Circular 4/2007, which amends the model for the annual corporate governance report of listed public limited companies.

The annual reviews which the CNMV makes of the ACGR have revealed situations in which the use of appropriate classifications for some members of the Board may be questioned. The most frequent incidents occur in the classification of independent directors, which has led to requests being sent for additional information, clarifications or, where appropriate, the publication of an additional information document with the new classification of the affected director.

The SEA strengthens the scope of the definitions used to classify directors, by establishing that the information included in the ACGR on the composition of the Board of Directors, its delegated committees and the classification of its directors must be prepared in accordance with the definitions established by the Ministry of Economy and Finance or, with its express authorisation, the CNMV.

Specifically, the SEA establishes that in order to include a director within the category of independent director it will be necessary to take into account, among other considerations, that the persons are designated, where appropriate, at the proposal of the appointments committee based on personal and professional conditions, and that they may perform their functions without being dependent on their relations with the company, its significant shareholders or its executives.

The Ministry of Economy and Finance or, with its express authorisation, the CNMV, will determine the conditions which a director must meet in order to be classified as

independent, as well as the situations in which said director may not be classified as such.

For this purpose, the SEA establishes that the following situations, *inter alia*, established in the Unified Code may be taken into account when excluding a director from the classification of independent:

- Having been an employee or executive director of companies in the group.
- Being or having been a partner in an external auditor or responsible for the auditors' report.
- Being a spouse or person linked by a similar affective relationship, or up to second level relative of an executive director or senior manager in the company.

2.4 Annual Corporate Governance Report of listed public limited companies

As indicated above, the SEA, with regard to corporate governance, also aims to improve the information which issuers publish about their internal control systems. To this end, it introduces a new heading in the ACGR in which they have to describe the characteristics of their internal control and risk management systems with regard to the process for issuing financial information.

Given that this mandate was provided in the first drafts of the future Act, in April 2009 the CNMV approved the creation of a group of experts entrusted to draw up a report with recommendations for internal control over the reliability of the financial information which included proposals for regulatory changes, a catalogue of principles and good practices and support guides for reporting and supervising, as well as recommendations for the treatment of entities which request their admission to trading for the first time.

The working group was made up of 12 experts from listed companies, the four most representative external auditing firms in the securities market, the Institute of Internal Auditors, a professor of commercial law and the CNMV, with the CNMV performing support and secretarial tasks. The working group reviewed the current Spanish legislative framework with regard to internal control and that of other similar countries, and agreed proposals for improvement with regard to internal control systems for the reliability of financial information.

A document with the group's recommendations was published in June 2010.³ The support guide included in this document contains the reference indicators that listed companies must use to report on their internal control and risk management systems.

The changes introduced by the SEA (new information on internal control systems, definitions of directors and remuneration report) and the updating of the Unified

³ The document is available at the CNMV's website (<http://www.cnmv.es/Portal/Publicaciones/SCIIF.aspx>).

Code involve amending the model ACGR so as to include the new information requirements.

In 2011, a new CNMV circular will be approved with a new model ACGR which includes these changes, as well as the technical improvements which the companies and issuer associations have requested.

3 Amendments to the supervision, inspection and disciplinary regime attributed to the CNMV

The amendments introduced by the SEA mean that new entities will be subject to the CNMV's supervision, inspection and disciplinary powers. New supervisory powers are also granted to the CNMV and amendments are made both to the regulation of professional secrecy and disciplinary administrative proceedings. Noteworthy aspects of the reform include both the introduction of a regulation aimed at strengthening the compensation of damages to investors and clients, and the improvements in the classification of facts amounting to a breach.

3.1 New entities subject to the CNMV's supervision, inspection and disciplinary powers

The SEA adds the following entities to the entities subject to the supervision, inspection and disciplinary regime provided in the prior wording of Article 84 of the SMA: i) companies which manage securities registration, clearing and settlement systems created under the provisions of the SMA, ii) the companies which hold a stake in the capital which confers them direct or indirect control of the entities subject to the supervision, inspection and disciplinary regime, iii) the persons or entities which hold the condition of members of the clearing and settlement systems of the transactions performed on an official secondary market, and iv) management companies of CIS when they provide investment services.

For its part, the new wording that the SEA gives to Article 69 of the CISA adds the following as entities subject to the supervision, inspection and disciplinary procedures of this Act, in addition to those provided in the previous wording: i) the agents of the Spanish management companies of collective investment schemes (Spanish acronym: SGIIC) provided in Title IV of the CISA, with the supervision and inspection powers extending to any office or centre of these companies in Spain or abroad, and ii) those who occupy administration, management or similar positions in the legal entities subject to the supervision regime.

3.2 New supervision and inspection powers of the CNMV and unification of authority

The amendments introduced by the new wording that the SEA gives to Article 85 of the SMA strengthens the supervision and inspection powers granted to the CNMV, granting it the following additional powers:

- 1 That of requiring the persons or entities subject to supervision to send the CNMV those reports which are necessary, drawn up by independent experts, auditors or by their own internal control or compliance bodies so as to provide evidence that the supervised entity complies with the rules and provisions applicable to it and that it has complied with the requirements for rectification or correction made by the CNMV.

This new power will significantly speed up the CNMV's supervision and inspection actions as it may require that the fieldwork, which with the previous wording could only be carried out by CNMV staff, may also be carried out by independent third persons or qualified bodies and sent to the CNMV by the supervised entities. Accordingly, evaluations of the CNMV and, as the case may be, rectification of the problems detected may be completed in a much shorter time, which in turn leads to greater supervision effectiveness.

- 2 That of adopting preventive measures, a concept which substitutes that of the provisional measure included in the previous wording, adding as a new measure, in addition to those already provided in the previous wording, that of temporarily banning the exercise of professional activities. In addition, adoption of these measures shall be dependent only on their need for effective investor protection or correct functioning of markets, therefore eliminating the limits established in the previous wording.
- 3 That of requiring the entities which provide investment services to make available to the CNMV the recordings made of the commercial telephone conversations held with their clients and investors.

This new power may represent an effective instrument when verifying these entities' compliance with the rules of conduct.

- 4 That of accessing the information and data that it requires in exercising its supervision and inspection functions without it being possible to object to information and data being submitted on the basis of personal data protection, currently regulated in Constitutional Law 15/9099, of 13 December, on Personal Data Protection (the Data Protection Act). For this purpose, the new wording of Article 85 expressly declares that the exercising of the CNMV's supervision and inspection functions is included under Article 11.2 a) of said legal text, a fact which was already recognised in the report issued by the Data Protection Agency prior to this reform. Similarly, in line with the spirit of said personal data protection legislation, it is expressly declared that the data to which the CNMV has access in exercising its functions will only be employed in carrying out its powers and in the terms provided in the SMA.

This legislative clarification, carried out in line with the content of the aforementioned Act 15/1999 and the content of the aforementioned reports conducted by the Data Protection Agency at the request of the CNMV, removes the possible objections and delays resulting from the supervised parties opposing the sending of information based on an interested interpretation of data protection legislation.

- 5 That of requesting from public authorities, chambers and corporations, colleges, boards of colleges, professional associations and other public entities and, in general, any entity which exercises public functions, the data, documents, registers, reports and background information that are necessary for executing its functions, with these entities being obliged to provide the CNMV with the collaboration, help and protection necessary to carry out its functions.

With this new duty for collaboration of the aforementioned entities, the CNMV significantly increases its capacity to access information which was previously off-limits.

- 6 That of using electronic means to communicate and make requests to the entities and persons supervised for the information and measures included in the SMA and its implementing legislation. At the same time, the supervised persons and entities are obliged to authorise the technical resources required by the CNMV in order to achieve full effectiveness of the notification and communications using electronic systems. All of this is to be done respecting the principles and guarantees established in Act 11/2007 of 22 June on online access of citizens to public services.

This reform gives a significant boost to electronic communications between the CNMV and supervised entities and hence, speeds up the communications and relations in the field of supervision and inspection.

- 7 For the first time, the probative effect of the documents which include the facts verified by CNMV staff is recognised when, after having been duly authorised by the Board, the staff perform supervision and inspection functions. This probative value of the verified facts does not cancel the possible probative action which may be provided by the supervised entities in defence of their rights and interests. However, this amendment increases the authority of the CNMV's staff and will speed up the investigation of disciplinary proceedings. However, it should be clarified that the probative effect is limited to the facts verified in the supervision and inspection actions and does not include the assessments and conclusions which may be derived from those facts, nor the content of the reports carried out subsequently.
- 8 The SEA extends to all the entities listed in Article 84.1 of the SMA the power of the Ministry of Economy and Finance and, with its express authorisation, the CNMV to regulate the registers, internal databases or statistics and documents which said entities must maintain. In the previous wording, this power only affected investment service firms.
- 9 The SEA extends the power of the CNMV to require investment service firms or their groups to adopt the measures necessary to safeguard their solvency, not only with regard to internal control systems, which was the situation prior to the reform, but the measures may also be required with regard to accounting and valuation systems.

The SEA also introduces new wording to Article 70 of the CISA, which, in line with the reform of the SMA, regulates the supervision and inspection

powers of the CNMV with regard to the entities subject to said Act. This regulation is carried out by means of an express reference to Article 85 of the SMA mentioned above. In addition, on specifying the scope of the supervision and inspection of the persons and entities subject to this control, it adds the legal, technical and economic-financial situation, the internal controls, and accounting and valuation systems to those already provided in the previous wording.

With regard to the supervision and inspection functions which the VCFA attributed to the CNMV, the SEA adds a new heading 7 to Article 50 which expressly refers to the content of the provisions included in Article 70 of the CISA, which in practice leads to a real reference to Article 85 of the SMA. Consequently, the SEA unifies the supervision and inspection powers granted to the CNMV by the SMA, the CISA and the VCFA.

3.3 Amendment to the regulation of professional secrecy

The SEA introduces a new exception to the duty of secrecy regulated in Article 90 of the SMA by adding letter ll) to point four of the Article. Accordingly, an exception is made to the obligation of secrecy and therefore, the CNMV is empowered to send the information which, in the exercise of its functions, the Spanish supervisor authorities require with regard to energy and the supervisory authorities of the Mercado Ibérico de la Energía Eléctrica (Iberian Electricity Market). However, in order to provide maximum guarantees of the rights protected with the obligation of professional secrecy, the reform provides that the disclosure of the communicated information requires the express agreement of the CNMV.

It should be remembered that the obligation to safeguard the information of the reserved data, i.e. all that which is not public, such as the data filed in the registers held by the CNMV to which investors have free access, affects all the persons that perform or have performed their professional activity in the CNMV.

3.4 Amendments in the administrative disciplinary procedure

In this context, we can highlight the amendment that the SEA introduces to Article 97.1 of the SMA, which consists of eliminating the mandatory, but non-binding, report which, according to the previous wording, the Advisory Committee of the CNMV had to issue prior to adoption by the Board of the agreement to send the Ministry of Economy and Finance the proposals for resolution for the imposition of very serious fines.

The new wording of that Article resulting from the SEA eliminates the reference to the authority of the CNMV with regard to the initiation, investigation and resolution of proceedings for breach of the regime for trading treasury shares of public limited companies, which was expressly included in the previous wording. However, this removal does not mean that the CNMV loses this authority, as it is still included in Article 157.6 of the Capital Companies Act.

It also removes the reference which the SMA made to Articles 7, 14 and 15 of Act 26/1988 of 29 July on Discipline and Intervention of Credit Institutions (hereinafter, Credit Institution Discipline Act), with these issues now being directly regulated in the SMA. Accordingly, i) Article 7 of the Credit Institution Discipline Act referred to in the regulation on the prescription period for breaches is now regulated, in the same terms, in the new Article 101(2) of the SMA, ii) Article 14 of the Credit Institution Discipline Act, which established the criteria for classifying the penalties to be imposed, is now regulated in the new Article 106(3) of the SMA in the same terms but adding two new criteria: redress of the damage caused (the effectiveness of which will be commented later) and the collaboration of the breaching party with the CNMV when clarifying the investigated events, and iii) Article 15 of the Credit Institution Discipline Act, which regulated the liability of directors and executives for the breaches committed by legal persons, is now regulated, in the same terms, in Article 95 the SMA.

The objective of the new aspects or improvements introduced to the CISA with relation to the administrative disciplinary procedure is to homogenise it with the regulation in this matter established in the SMA. Accordingly, i) the mandatory report of the Advisory Committee is eliminated, ii) criteria are established for classifying the penalties in line with those established in the SMA and iii) clarification is made, in accordance with the SMA, of those who hold administration or management positions so as to establish possible administrative liability.

Furthermore, a short procedure is established for minor breaches, according to which the penalty may be imposed by processing a summary procedure in which only the hearing of the interested entity will be mandatory.

The new aspects introduced in the VCFA are also aimed at homogenising its regulation with the SMA and the CISA. Accordingly, i) persons who hold administrative or management positions are clarified in the same terms, ii) reference is made to Article 88 of the CISA with regard to the criteria to classify the penalties, thus homogenising it with the SMA, and iii) for the prescription of breaches, Article 83 of the CISA will be applicable, thus homogenising it with the SMA.

Similarly, the same procedure provided in the CISA is established for the imposition of penalties for minor breaches.

3.5 Amendments aimed at strengthening the compensation for damage to investors and clients

The SMA provides that the CNMV, together with other obligations, must ensure investor protection in financial markets. In this regard, in order to promote compensation for damage caused as a result of incorrect application of the rules of conduct established in Chapter I of Title VII of the SMA by investment service firms and, in general, by those who provide investment services, the SEA has adopted a series of measures aimed at ensuring that said compensation is carried out directly and in a reasonable time by the entities, either voluntarily so as not to damage their clients, or motivated by the possibility of avoiding or mitigating the administrative liability

which may derive from their behaviour. These measures can be grouped into three sections:

- 1 Amendment of the penalty classifications for breaches of the rules of conduct regulated in the SMA. It should be clarified that, in general, in administrative law the risk generated by committing the breach is punished irrespective of whether effective damage has taken place or not. Nevertheless, as the amendments analysed aim to achieve compensation for the investor, in this case the illegal activity of the breaching party must have produced effective damage to the investor's or client's assets.

In this regard, the reform distinguishes between i) very serious breaches (Articles 99.z)(2) and 99.z)(3) of the SMA), which require that the conduct is characterised by its regular nature, i.e. that it affects a set of clients in such a way that it makes it possible to consider that the breaches are carried out by the entity on an ongoing basis, ii) serious breaches (Article 100.t of the SMA), in which the conduct is not of a regular nature and therefore constitutes an occasional or isolated failure to observe the rules with regard to a specific group of clients of the entity, and iii) minor breaches (101.2 b of the SMA) where conduct is characterised by the one single failure to comply with the rules of conduct within the framework of a client relationship (this refers to a new type of breaching party introduced by the SEA).

- 2 A new and specific cause is introduced which allows entities to avoid their administrative liability by asset reimbursement of the damages caused to the investors.

Accordingly, the new Article 107(2) of the SMA provides that, in the event of the alleged commission of a minor breach under Article 101.2b), the CNMV may, prior to opening disciplinary proceedings, require the allegedly liable entity to adopt, in a period of 30 days, the appropriate measures to prevent continuation or reiteration of the conduct and to compensate the asset damages caused to investors by its conduct. The entity must provide sufficient evidence that it has complied with the two requirements above. In this case, the CNMV may consider that the supervision objectives have been fully met and, therefore, not initiate the disciplinary proceedings.

This new regulation introduces a legal support which may be of great use for quick and effective compensation of the damage caused to investors as a consequence of entities failing to comply with the rules of conduct. This situation makes most sense in the claims or formal complaints by investors received in the CNMV when they demonstrate failure to comply with the rules of conduct within the specific relations of providing investment services. There is now an incentive for the entities to compensate the damages caused to the claimant person making the official complaint, which will avoid any possible initiation of disciplinary proceedings.

The objective is greater protection for the investor as it increases the effectiveness and value of the report which resolve the claims presented to the CNMV and provides investors with a route for recovering the damage suffered with-

out the need to resort to a civil lawsuit and, consequently, providing the alleged party in breach with the possibility, by compensating the investor, of disciplinary proceedings not being initiated, thereby avoiding the imposition of a possible penalty, as the case may be, for the party in breach.

- 3 Finally reparation of the damage caused has been included as a new cause in the classification of the breaches. This provides an incentive to reimburse the asset damages to investors caused by breaches so that the party in breach may minimise the penalties imposed by compensating the damage caused to its clients.

For its part, the amendments introduced by the SEA in the CISA, in line with the aforementioned amendment to the SMA, incorporates a new Article 88(2), which provides, in the same terms as Article 107(2) of the SMA, the possibility that through compensation and reimbursement of the investor affected by asset damages as a consequence of the entity committing certain minor breaches, the entity has the possibility of avoiding initiation of disciplinary proceedings. The redress of damages caused by the breach committed by the entity has also been included, in the same terms as in the SMA, as a new cause for classification of breaches.

With regard to the VCFA, the new causes for classification of the breaches described above are introduced through reference to Article 88 of the CISA.

3.6 Amendments aimed at improving penalty definitions

The amendments introduced by the SEA with regard to the penalty definitions established in the SMA are a consequence: i) of the amendments introduced in the substantive rules, which, for consistency, required incorporation of new definitions of breaching parties, ii) of the homogenisation of the definitions established in the SMA with those included in the CISA, and iii) of the incorporation of other aspects which prior to the reform were applicable through reference by the SMA to the Credit Institutions Discipline Act.

Of the set of amendments introduced in the field of the SMA, we can highlight the following:

- 1 The amendments of the existing penalty definitions 99.a) and c) – and the incorporation of new penalty definitions – 99.c) (2), (3) and (4) – to include the breaches which may be committed by: i) the governing councils of official secondary markets, ii) the governing councils of multilateral trade facilities, iii) the companies which manage securities registration, clearing and settlement systems created under the SMA, iv) the Sociedad de Sistemas, v) central counterparties, vi) the Sociedad de Bolsa, and vii) the companies which own all the shares or a holding which attributes direct or indirect control of the companies or entities referred to in points i), ii) and iii). When said companies or entities fail to comply with: i) the limits to their activity provided in law, ii) the regulatory rules of the markets or systems, their own regulations or the regulatory rules of their activity, iii) the reporting requirements with regard to the CNMV,

- iv) the obligations relating to authorisation, approval or non-objection to their articles of association and regulations, v) requirements with regard to capital structure or level of equity, and vi) the exceptions or limitations imposed by the CNMV with regard to their prices, fees or commissions to be applied.
- 2 The creation of a new very serious penalty definition – 99.e) – which categorises non-compliance with CNMV requirements for investment service firms with regard to their internal control, accounting or valuation procedures and the mechanisms or strategies for having appropriate resources and a suitable organisational structure when they pose a risk for the entity’s solvency or viability.
 - 3 The withdrawal from penalty definition 99.l.(2) of the requirement to remind of the obligation or reiterate the request for information when this has not been sent to the CNMV, in the event that this makes it difficult to appraise the solvency of the entity or the consolidatable group or financial conglomerate which it forms part of.
 - 4 The withdrawal of the requirement for there to be fraudulent action in order to classify certain conduct as very serious breaches, with regard to the inaccuracy in regulated information or the significant events submitted by the issuers. In addition, in the penalty definition for accounting breaches of issuers, it is required that the inaccuracy is significant for it to be classified as very serious.
 - 5 The creation of a new very serious penalty definition – 99.z(5) – for failure to comply with the preventive measures agreed by the CNMV outside those decided in disciplinary proceedings.
 - 6 The creation of a new very serious penalty definition – 99.z(6) – for the absence of a customer service department, and a new serious penalty definition – 100.z(6) – for poor functioning of the customer service department.
 - 7 The amendment of the classifications with regard to the acquisitions of significant shareholdings, differentiating the very serious definition, when non-compliance occurs in the acquisition of a significant controlling holding, from that classified as serious, applicable to other non-compliances.
 - 8 The creation of the new serious penalty definition – 100.z(4) – for the situation in which investment service firms exceed the limits provided for major risks, when this is a consequence of a decision by the firm and not an unforeseen event.
 - 9 The creation of a new serious penalty definition – 100.ll(2) – for placing issues without complying with the requirements for intervention of an authorised entity, without fulfilling the advertising conditions, the omission of significant data or the inclusion of inaccuracies, incorrect information or misleading data in the aforementioned advertising, when the amount of the issue and the number of affected investors are not significant.
 - 10 The creation of three new minor penalty definitions – 101.2.a) and b) – for: i) failure to send the CNMV data or information on time, ii) failure to comply with the duty to collaborate with the supervisory actions of the CNMV, includ-

ing the failure to appear following a summons, when this does not constitute a serious or very serious breach, and iii) one-off non-compliance with the rules of conduct in the framework of a client relationship (penalty definition already analysed previously with regard to the amendments to the compensation of asset damages).

With regard to the penalty definitions established in the CISA, the amendments introduced by the SEA are a consequence: i) of legislative changes, ii) the homogenisation process with the SMA and supervisory experience, iii) of better techniques in the breaching party definitions, and iv) of the classification of the penalty definition depending on the existence of certain circumstances. From the set of amendments of this type introduced in the CISA, we can highlight the following:

- 1 The disciplinary regime now covers the new “side pockets” regulated in Article 28(2) of the CISA, in accordance with the second final provision of Act 5/2009 of 29 June on the reform of the regime for significant shareholdings in investment service firms, in credit institutions and in insurance companies. To this end, two new penalty definitions are established: one which is very serious and includes, as a component of the penalty definition, that non-compliance seriously damages the interests of the shareholders or there is a reiterated conduct, and another which is serious, when the circumstances which classify non-compliances as very serious do not exist.

In addition, three new penalty definitions are established, deriving from the new regime for significant shareholdings of CIS management companies included in Act 5/2009. In line with the SMA, the very serious penalty definition requires that non-compliance refers to controlling shareholdings while the two serious penalty definitions refer to other non-compliances.

- 2 Amendments are incorporated based on supervisory experience and/or homogenisation with the criteria established in the SMA, specifically:
 - Non-compliance with the commitments assumed with the CNMV by CIS management companies or investment service firms to rectify the deficiencies detected in a supervision or inspection action are classified as very serious when they seriously damage the interests of the shareholders or refer to reiterated conduct, and are otherwise classified as serious.
 - Non-compliance with the rules for valuing the assets of CIS, which is classified as very serious when it seriously damages the interests of the shareholders, it refers to reiterated conduct or it has a substantial impact on the net asset value of the CIS. Otherwise, it is classified as serious, or as minor when, as it is once single event of a minor significance, it should not be classified as serious.
 - Single non-compliance within the framework of a client relationship with the rules of conduct provided in the SMA. This is classified as a minor breach. This breach is one of those for which administrative liability may be avoided by compensating the asset damages caused, as studied in section 3.5.

- The delegation of functions of the CIS management companies with non-compliance with the conditions established in the rules, which is classified as a very serious breach when the interests of the shareholders are seriously damaged, when referring to reiterated conduct or when it reduces the internal control capacity or supervision capacity of the CNMV. Otherwise, it is classified as serious.
 - Non-compliance with the preventive measures agreed by the CNMV, which is classified as a very serious breach.
 - Conducting advertising and failing to comply with the regulations, which is classified as a serious breach.
 - The effective administration or management of legal entities subject to the supervision or inspection regime by persons who do not exercise in law in said entities such a position, which is classified as a serious breach.
 - Non-compliances relating, *inter alia*, to limits to investment, ratios, obligations with third parties and asset valuation classified as serious, are now classified, following the reform, as minor when they are of limited significance. Administrative liability of this new minor breach may also be avoided by compensating the asset damage caused.
 - Failures to comply with the CISA and its implementing regulation may be classified as a minor breach when they are not specifically classified as serious or very serious breaches.
- 3 The SEA has introduced technical improvements in some of the penalty definitions which were already previously classified. These include the following:
- It specifies the obligations, with which failure to comply is classified as very serious with regard to sending the CNMV periodic information, regulated financial information or the data or documents which the CNMV requires in carrying out its functions. A classification of minor breach is given to the failure to send in time information which must be sent to the CNMV, as well as the failure to collaborate and the failure to appear following a summons.
 - The very serious penalty definition is strengthened with regard to non-compliance with equity requirements, by referring to those which must be held at all items and not the equity required to obtain authorisation, as established in the previous wording of the reform. In addition, the mention of investment service firms is withdrawn as they are not subject to the equity requirements provided in the CISA. Furthermore, a new serious penalty definition is introduced for non-compliance with the reporting requirements to the CNMV and the conditions established for returning to compliance when a management company has equity below the required levels.
 - Two new breaches classified as serious are introduced in relation to the collection of fees. The collection of fees for services which have not been

effectively rendered and the collection of fees not provided in the legislation, articles of association or regulations.

- The lack of procedures is classified as a very serious breach. In the previous wording this was only provided as such in the case of deficiency in the proceedings.
 - A classification of very serious breach is given to obtaining authorisation as result of false declarations or through irregular means or non-compliance with the conditions presented for authorisation.
 - The performance by management companies or investment service firms of activities for which they are not authorised is classified as a very serious breach.
 - Improper use of reserved names is classified as a serious breach.
- 4 The reform introduced by the SEA makes the application of the penalty definitions of serious or very serious, in certain breaches, dependent on the existence of certain circumstances, such as seriously damaging the interests of the shareholders or reiterated non-compliance. In this regard, the following breaches are classified as very serious or serious:
- Investment in assets other than those authorised.
 - Non-compliance with the investment limits or minimum investment ratios.
 - Banned transactions with own shares.
 - Exceeding the limits with regard to obligations assumed with third parties.
 - Valuation of the assets of the CIS by means other than those established in legislation.

Finally, the SEA has introduced limited amendments in the breaches established in the VCFA. Specifically, failure to send the CNMV the documents and information which must be sent or which it requests is classified as a very serious breach when this makes it difficult to appraise the solvency of the entity or its asset situation. Similarly, failure to comply with the rules of conduct is classified as serious when it does not constitute a very serious breach.

4 Conclusions

The SEA introduces reform measures in the financial market to increase transparency and to improve corporate governance. As from the General Shareholders' Meetings held in 2012, listed public limited companies must submit a directors' remuneration report to a vote, on an advisory basis and as an item on the agenda.

Another of the objectives of the SEA, with regard to corporate governance, is to improve the information which issuers publish on their internal control systems. To this end, it introduces a new heading in the ACGR in which they have to break down the characteristics of the internal control and risk management systems with regard to the process of issuing financial information.

A substantial part of the reform introduces amendments to the legislation of the supervision, inspection and disciplinary regime which the law attributes to the CNMV so as to allow it to appropriately carry on its functions as a supervisory body, as provided by law.

In this regard, the reforms performed by the SEA in the SMA, the CISA and the VCFA with the aim of homogenising the legislation, introduce new entities subject to the supervision, inspection and disciplinary power of the CNMV and grant the CNMV new control powers, as well as partially amending the regulation on professional secrecy and the administrative disciplinary procedure. Furthermore, one of the most substantial and novel reforms is the introduction of a new system for compensating the damage caused to investors and clients. Finally, the SEA carries out an improvement of the definitions of breaches.

European Securities and Markets Authority

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1 Introduction

The European Securities and Markets Authority (ESMA) began operating on 1 January 2011.¹ That same day the other two European supervisory authorities were established: The European Banking Authority (EBA) and the European Insurance and Occupational Pensions Authority (EIOPA),² as well as the European Systemic Risk Board (ESRB),³ which is responsible for supervising aggregate risks for the financial system of the European Union as a whole.

The immediate origin of the creation of the European Supervisory Authorities (ESAs) is the report prepared by a high-level expert group chaired by Jacques de Larosière, which the European Commission set up in November 2008 to prepare a series of recommendations for strengthening European supervisory arrangements with the aim of improving citizen protection and restoring confidence in the financial system. In its definitive version, issued on 25 February 2009, the expert group recommended strengthening the supervisory framework with the aim of reducing the risk and seriousness of future financial crises and, among other conclusions, recommended the creation of a European System of Financial Supervisors made up of the three aforementioned authorities and the European Systemic Risk Board.

Taking into account the complexity and significance of the issues addressed, it is of no surprise that the new supervisory structure was built among extensive debates which led to the need to make enormous efforts for consensus.⁴ In the context of the crisis, which highlighted serious deficiencies in financial supervision, both in

1 Regulation (EU) No. 1095/2010 of the European Parliament and of the Council of 24 November establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No. 716/2009/EC and repealing Commission Decision 2009/77/EC (OJEU 2010 L 331/84).

2 **Respectively, Regulation (EU) No. 1093/2010 of the European Parliament and of the Council of 24 November 2010** establishing a European Supervisory Authority (European Banking Authority), amending Decision No. 716/2009/EEC and repealing Commission Decision 2009/78/EC (OJEU 2010 L 331/12) and Regulation (EU) No. 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No. 716/2009/EC and repealing Commission Decision 2009/79/EC (OJEU 2010 L 331/48).

3 Regulation (EU) No. 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board (OJEU 2010 L 331/1) and Council Regulation (EU) No. 1096/2010 of 17 November conferring specific tasks upon the European Central Bank concerning the functioning of the European Systemic Risk Board (OJEU 2010 L 331/162).

4 For further details about the procedure, see N. Moloney, "The European Securities and Markets Authority and institutional design for the EU financial market: a tale of two competences: part (1) rule-making", in *European Business Organisation Law Review*, 12 (1) pp. 41-86 (2011). Also see E. Ferran, *Understanding the New Institutional Architecture of EU Financial Market Supervision*, University of Cambridge Faculty of Law Research Paper No. 29/2011 (2010).

specific cases and with regard to the financial system as a whole, it was necessary to materialise the clear political will in an extremely short period of time: it was necessary to carry out a thorough reform to remedy the deficiencies found and to offer a system in line with the objectives of a stable and single Union financial market for financial services, linking national supervisors within a strong Union network.⁵

In the belief that the Union had reached the limits or even exceeded what could be done with the nature of the former Committees of European Supervisors, including the Committee of European Securities Regulators (CESR), the European Supervisor Authorities not only assume all of its activities but they also incorporate extensive powers both in terms of regulation and in the field of supervision, modifying the distribution of powers in favour of greater Union convergence in both areas.

It was precisely this process of assigning intervention powers which was the main subject of negotiation in order to obtain a cross-institution consensus. A discussion was held with regard to several issues of major importance: the power of ESMA to issue binding decisions, which may be addressed to the competent authorities or supervisors of the Member States in the event of a breach of Community law, as well as in emergency situations or even in the event of a disagreement between supervisors (respectively, Article 17, 18 and 19 of Regulation (EU) No. 1095/2010). In addition, the decision on which European institution was to declare the “emergency” and the nature or scope of the get-out clause which may lead to the suspension of a decision adopted by ESMA (Article 38 of the aforementioned Regulation).

In addition to the above, it was necessary to decide on issues relating to the framework in which ESMA may adopt decisions and address them to the participants of the stock market and even ban specific products and services, as well as the supervisory powers over institutions with cross-border activities or presence and with systemic implications or its quasi-regulatory powers and its interrelation with the powers of the Commission and intervention of the Council and the Parliament in this process.⁶ Regulation 1095/2010 represents the formalisation of the consensus reached in the aforementioned aspects.

This article offers a brief description of the new European supervisory architecture outlined in the previous paragraph. In particular, the article bases its main focus on

⁵ Recital 8 of Regulation (EU) No. 1095/2010.

⁶ The creation of European regulatory authorities in liberalised sectors has not traditionally been an easy issue within the EU, as it has an impact on the distribution of powers between the EU and its Member States. Accordingly, and with the desire to provide the best legal justification for the creation of the new Authorities of the European Financial Supervision System – which are created on the basis of Article 114 of the Treaty of Lisbon (formerly Article 95), a recital in each one of the Regulations creating the ESA expressly refers to the judgement of the CJEU of 2/5/2006 on Case C-217/04 (United Kingdom of Great Britain and Northern Ireland v. European Parliament and Council of the European Union). In this judgement, the CJEU “established that nothing in the wording of Article 95 EC implies that the addressees of the measures adopted by the Community legislator on the basis of that provision can only be the individual Member States. The legislator may deem it necessary to provide for the establishment of a Community body responsible for contributing to the implementation of a process of harmonisation in situations where, in order to facilitate the uniform implementation and application of acts based on that provision, the adoption of non-binding supporting and framework measures seems appropriate (...)”.

ESMA and specifically, on its organic and functional structure, as well as its powers, responsibility and field of application.

The article is structured as follows: section 2 describes the new architecture of European financial supervision of which ESMA forms a part. Section 3 describes the functions and powers of ESMA and its field of application, as well as its internal organisation and the remedies for the decisions of the new authority. Section four includes the main conclusions.

2 The new European supervisory architecture

The European Financial Supervision System is created as a network made up of the ESAs and the national supervisory authorities plus the ESRB. A Joint Committee is established as part of this network to ensure coordination between the ESAs.

2.1 The European Systemic Risk Board

Regulation 1092/2010 recognises the need to exercise European Union macro-prudential oversight of the financial system, and therefore establishes the ESRB, which is based in Frankfurt, to monitor and assess potential threats to financial stability deriving from developments in the broader macroeconomic environment and the financial system in order to contribute towards preventing and mitigating systemic risk in the EU.⁷

The main functions of the ESRB are as follows:

- i To identify and prioritise systemic risks, issue warnings where such systemic risks are deemed to be significant (which it may make public) and issue recommendations for remedial action including legislative initiatives (which it may also make public).

When significant risks threatening financial stability are identified, the ESRB will issue a warning and, as the case may be, issue recommendations for remedial action, including, where appropriate, legislative initiatives. Both warnings and recommendations may be of a general or a specific nature and shall be addressed to the EU as a whole or to one or more Member States, or to one or more of the ESAs, or to one or more of the national supervisory authorities. Recommendations may also be addressed to the European Commission in respect of the relevant EU legislation. The ESRB may decide to make the warnings and recommendations public after having informed the Council sufficiently in advance. The addressees of warnings and recommendations made

⁷ Article 2 c) of Regulation 1092/2010 defines systemic risk as a risk of disruption in the financial system with the potential to have serious negative consequences for the internal market and the real economy. All types of financial intermediaries, markets and infrastructure may be potentially systemically important to some degree.

public by the ESRB are entitled to make public their views and reasoning in response thereto.

- ii To monitor the follow-up to warnings and recommendations.

The obligation of the addressees of the recommendations is what has been referred to as “act or explain”,⁸ i.e. to act on them or to provide an adequate justification in case of inaction. If the ESRB considers that the reaction is inadequate, it should inform the addressees, the Council and, where appropriate, the ESA concerned.

- iii To issue a confidential warning to the Council in the event of an emergency situation and provide an assessment of the situation.

If the ESRB detects a risk which could seriously jeopardise the orderly functioning and integrity of financial markets or the stability of the whole or part of the Union’s financial system, it should inform the Council. If the ESRB determines that an emergency situation may arise, it should contact the Council and provide an assessment of the situation. The Council then assesses the need to adopt a decision addressed to the ESAs within whose authority the emergency situation has been identified.

With regard to its internal organisation⁹ the ESRB has a decision-making body (the General Board), an executive body (the Steering Committee), a representation body (the Chair) and two advisory bodies (the Advisory Scientific Committee and the Advisory Technical Committee), as well as a support body (the Secretariat). The main decision-making body of the ESRB is its General Board, which is made up of, with voting rights, the President and Vice-President of the ECB, the governors of the national central banks, a member of the Commission, the Chairs of the EBA, ESMA and EIOPA, the Chair and two Vice-Chairs of the Advisory Scientific Committee, and the Chair of the Advisory Technical Committee. The participation of the micro-prudential supervisors is provided in some of the above bodies, such as the General Board and the Advisory Technical Committee, in which the CNMV is represented.

2.2 The European supervisory authorities

As indicated above, Regulations (EU) 1093/2010, 1094/2010 and 1095/2010 created respectively, the EBA, EIOPA and ESMA.

The general lines of these regulations are identical (each one of them contains 69 recitals and 82 articles). The differences lie in the objectives of the different ESAs, their field of application and the definitions, which are adapted to the specific characteristics of each sector and current Union legislation.

⁸ See Recital 20 of Regulation (EU) 1092/2010.

⁹ An ESRB Decision on 20 January 2011 adopted Rules of Procedure relating to its organisation and functioning, which supplement Regulations (EU) 1092/2010 and 1096/2010 (OJEU 2011 C58/4).

The ESAs are created as EU bodies with legal personality and enjoy administrative and financial autonomy. They must act independently and objectively, solely in the interest of the EU, and they are accountable to the European Parliament and the Council.

Formally, they substitute the former third level regulatory committees of the Lamfalussy procedure, which was in force up to the introduction of the new authorities. Hence, EBA substitutes the Committee of European Banking Supervisors (CEBS), EIOPA substitutes the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) and ESMA substitutes the Committee of European Securities Regulators (CESR). The head office of the bodies is maintained in all three cases, in London, Frankfurt and Paris respectively.

The Joint Committee

In order to guarantee cross-sectoral consistency of the activities of the ESAs, they must be closely coordinated by means of a joint committee and they must reach, where appropriate, common positions.

The Joint Committee is thus created as a forum with which ESMA will cooperate regularly, ensuring cross-sectoral consistency with EBA and EIOPA, in particular, with regard to aspects which, as a result of the financial crisis, have proven to be essential, such as financial conglomerates, accounting and auditing services, micro-prudential analyses of cross-sectoral developments, risks and vulnerabilities for financial stability, retail investment products and measures combating money-laundering. In addition, the Joint Committee will be the body responsible for exchanging information with the ESRB and developing the relationship between the ESRB and the ESAs. It is made up by the Chairs of the EBA, ESMA and EIOPA, as well as, where appropriate, the Chairs of the subcommittees which are created, and it is chaired, on a rotating basis, for a 12-month period, by the Chairs of the ESAs.

3 ESMA

3.1 Functions and powers

3.1.1 Outline

As indicated above, Regulation 1095/2010 establishes the ESMA's powers with regard to securities markets and their participants within the European Union. Some of these powers are the result of the need to intervene in the event of a crisis or emergency. This is the case of the powers which ESMA has been assigned to adopt mandatory decisions requiring national supervisory authorities and the participants of financial markets to take action in the event of an emergency (Article 18). In addition, ESMA must ensure coordination with regard to managing systemic risk, with participants with cross-border links and with resolving the crises which may occur (Article 22 to 27 and 31), as well as to assume responsibilities with regard to the assessments relating to the resilience of financial market participants to adverse

market developments (Article 32). All of this is to be governed by the general obligation to pay special attention to systemic risk (Article 1.5).

All these powers have significant implications, which should not be minimised, but which are limited in daily practice as they are powers to be used as a “last resort” in exceptional situations.¹⁰

However, the quasi-regulatory powers, as well as those relating to supervisory practices, may have the greatest real implications in daily activities. There are powers to develop draft regulatory technical standards and draft implementing technical standards, to develop guidelines and recommendations, to issue an opinion addressed to the European Parliament, Council and the Commission, to collect information and to develop common methodology and to provide an extensive database on institutions and other participants and information which allows a clear, extensive and updated picture of the full European financial system.¹¹

Main powers of ESMA

TABLE 1

• Rule-making powers Regulatory technical standards (Art. 10) Implementing technical standards (Art. 15) Guidelines and recommendations (Art. 16)
• Action in the event of a breach (Art. 17)
• Powers in emergency situations (Art.18)
• Settlement of disagreements (Art. 19 and 20)
• College of supervisors, delegation and cooperation (Art. 21, 28 and 31)
• Peer review of competent authorities (Art. 30)
• Tasks related to consumer protection and financial activities (Art. 8 and 9)
• Providing opinions to the European Parliament, the Council or the Commission (Art. 34)
• Collection of information on participants in financial markets (Art. 35)
• Developing a centrally accessible database (Art. 1.2 and 8)
• Specific supervision tasks: authorisation and supervision of credit rating agencies, central counterparties and repositories; choice of OTC derivatives for clearing

Source: CNMV.

3.1.2 Rule-making powers: Technical standards

3.1.2.1 Definition and general considerations

Since the entry into force of the Treaty on the Functioning of the European Union, referred to as the Treaty of Lisbon, the European Commission, following authorisation

10 See Question 12 (page 9), *Frequently Asked Questions. A Guide to Understanding ESMA*, 3 January 2011 (ESMA/2011/009).

11 This has to be put into the context of the review clauses contained in Regulation 1095/2010 and which are aimed at assessing, before January 2014, the work carried out and for the necessary adjustments to be performed so as to adapt the activities and powers of ESMA to the actual situation.

tion, may adopt two types of secondary measures or implementing acts which are mutually exclusive: delegated acts, in accordance with the provisions of Article 290, and implementing acts, in accordance with Article 291.

Delegated acts are general non-legislative acts which supplement or amend non-essential elements of the legislative act from which they derive. Implementing acts are non-legislative acts which include the uniform conditions for implementing legally binding Union acts which require uniform application throughout the Union and which cannot be reached through the measures which States may usually adopt. These acts will normally contain individual decisions, without prejudice to the fact that in some cases they may have a more general scope, although the room for action by the Commission will be more limited than in delegated acts.

Within the category of delegated acts¹² we can distinguish the regulatory technical standards, proposed and adopted in accordance with Articles 10 to 14 of Regulation 1095/2010, and those delegated acts which ESMA is not involved in developing. In the former, a prior legislative act will empower ESMA to develop the draft technical standards and at the same time, the Commission will delegate sufficient power to adopt them. In the latter, the delegation, both of the development of the draft and its approval, will fall exclusively to the Commission, which will not be obliged to consult national experts, although it may choose to do so.

With regard to implementing acts, we can also distinguish between the implementing technical standards, developed and adopted in accordance with Article 15 of Regulation 1095/2010, from those implementing acts which ESMA is not involved in developing. In the former, a prior legislative act will empower said Authority to develop the draft implementing standards and at the same time the Commission will delegate sufficient power to adopt them. In the latter, the delegation both of the preparation of the draft and its approval will fall exclusively to the Commission, and control of the Member States will be carried out through intervention during the development stage.

Consequently, Regulation 1095/2010 grants ESMA extremely significant quasi-regulatory powers which may lead to significant intensification of the EU single rulebook,¹³ even though the limits imposed by the Treaty of Lisbon have a compromise, which is not free of controversy, about the control to be executed by the European Commission with regard to the independence of ESMA.¹⁴ Chapter II includes the powers of ESMA, determining that it must “contribute to the establishment of high-quality, regulatory and supervisory standards and practices”.

The procedure for preparing the draft regulatory technical standards (Article 10) and implementing technical standards (Article 15) are virtually identical with the exception that regulatory technical standards are subject to greater scrutiny by other European institutions. These procedures are developed over several stages and are the product of agreement between Member States and the European institutions

12 Commission Communication to the Parliament and the Council on implementation of Article 290 of the Treaty on the Functioning of the European Union (COM [2009] 673 Final).

13 See Question 1 (page. 3), Frequently Asked Questions. A Guide to Understanding ESMA, *op. cit.*

14 Article 63, with regard to the independence of the Board of Supervisors.

involved in the negotiation of the text of the Regulation when designing the delegation of powers to the new authority in the context of the limits imposed by the Treaty of Lisbon.

The Securities and Markets Stakeholder Group has been set up to help facilitate consultation with stakeholders in areas relevant to the tasks of ESMA. The Group will be consulted on actions concerning regulatory technical standards and implementing technical standards, and on proposals for guidelines and recommendations, when these do not refer to individual participants in financial markets. The Group is made up of thirty members representing, in balanced proportions, financial market participants operating in the EU, their employees' representatives, consumers, users of financial services and representatives of SMEs, as well as academics. The Group includes two Spanish representatives: Carlos Arenillas (former Vice-Chairman of the CNMV), representing the users of financial services, and Professor Ángel Berges-Lobera, as an independent top-ranking academic.

The power to adopt regulatory technical standards is conferred to the Commission to be executed over a period of four years from the entry into force of Regulation 1095/2010, which may be automatically extended for periods of four years, unless expressly revoked by the European Parliament and Council. Six months prior to the end of the first four-year period, the European Commission will issue a report assessing the exercise of this power.

Said standards will be technical and, therefore, their development requires the experience of experts in supervision. In addition, they may not entail strategic decisions or political options and their content will be restricted by the legislative acts on which they are based (Article 10) or will be limited to establishing the application conditions for said acts (Article 15).

When the act entails strategic decisions or political options, the Commission retains the discretion to approve the delegated acts, and in this regard, it is agreed that future regulations must specify which acts must be endorsed by the Commission and which with the intervention of ESMA.¹⁵

In practice, situations will arise in which drawing the line between purely technical issues and/or political strategic issues will not be an easy task as there are technical situations which may have far-reaching consequences. Consequently, the clear determination of the distribution of authority in future legislative acts represents a fundamental issue in this regard.

3.1.2.2 Procedure

With regard to the procedure, before presenting the draft technical standards to the Commission, ESMA will carry out public consultations and analyse their poten-

15 In this regard, see Article 3 of Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 relating to Alternative Investment Fund Managers and amending Directive 2003/41/EC and 2009/65/EC and Regulations (EC) No. 1060/2009 and (EU) No. 1095/2010.

tial costs and benefits unless said consultations and analyses are disproportionate with regard to the scope and effects of the draft implementing technical standards in question or with regard to the urgency of the issue. The Authority will also collect the opinion of the Securities and Markets Stakeholder Group referred to in Article 37.¹⁶

When the Authority presents a draft technical standard, the Commission will immediately send it on to the European Parliament and the Council. It may endorse the draft implementing technical standard in part or with amendments, where the Union's interests so require.

When the Commission intends not to endorse a draft technical standard or to endorse it in part or with amendments, it shall send the draft technical standard back to ESMA, explaining why it does not endorse it, or, as the case may be, explaining the reasons for its amendments, and ESMA must amend the draft in the periods established for this purpose. If it does not do so, the Commission may endorse the technical standard without the intervention of the Authority.

3.1.2.3 Other considerations

With regard to regulatory technical standards, in accordance with Article 290 of the Treaty of Lisbon, the European Parliament or the Council may revoke the delegation of powers granted to ESMA at any time (Article 12).

Similarly, the European Parliament or the Council may object to a regulatory technical standard prepared by ESMA and endorsed by the Commission in a period of three months from the notification date. This deadline may be extended for another three months at the initiative of the European Parliament or the Council (Article 13).

If, on the expiry of the objection period, neither the European Parliament nor the Council has objected to the standard, it shall be published in the Official Journal of the European Union and enter into force on the date stated therein. In practice, this may mean that in the event of a dispute, the period for endorsing the regulatory technical standards may be up to 6 months from the date on which the Commission has endorsed a standard proposed by the ESMA.

Technical standards, once endorsed and published, shall be directly applicable and executable in Member States.

16 In order to facilitate the consultation with the interested parties of the areas related to the functions of ESMA, Article 37 of Regulation 1095/2010 provides for the creation of a Securities and Markets Stakeholder Group. It will consist of 30 members, who will be appointed by the Board of Supervisors of ESMA at the request of the pertinent interested parties, which will provide balanced representation to the participants in financial markets which operate in the EU, to their employees' representatives, to their consumers and to other retail users of financial services and to SMEs. ESMA must consult the stakeholder group about the regulatory technical standards or implementing technical standards and, to the extent that they do not refer to individual participants in the financial markets, the guidelines and recommendations, and to offer them a reasonable opportunity to formulate observations on the measures proposed.

3.1.3 Guidelines and recommendations

ESMA is also attributed the power to issue non-binding guidelines and recommendations addressed to the national supervisory authorities and to market participants so as to establish consistent and uniform supervisory practices, as well as to guarantee common and consistent application of Community legislation.

Despite their non-binding nature, Regulation 1095/2010 expressly indicates that the national supervisory authorities must make every effort to comply with the guidelines or recommendations issued by ESMA, adding as a deterrent measure and, at any event, as a transparency measure, that said authorities must inform in a period of two months from their issue whether they comply or have the intention to comply with them or not. In the event that a competent authority does not comply or does not intend to fully comply, it shall inform ESMA, which may publish the reasons¹⁷ following notification to the corresponding authority.

The level of compliance by the national supervisory authorities will also be included in the annual report which ESMA must prepare and submit to the European Commission, the Parliament and the Council, including a mention of the measures which ESMA plans to adopt to ensure compliance with its guidelines or recommendations by said authorities.

3.1.4 Action in the event of a breach of Community law

In the event that a national supervisory authority has not applied the provisions contained in the technical standards or has applied them in a manner which may result in a breach of Community law or in which it fails to ensure that a participant or institution complies with the obligations established in said standards, a resolution mechanism is provided consisting of three stages which cover specific events, procedures and deadlines (Article 17).

As a first step, ESMA may investigate the alleged breach or non-application of Community law on its own initiative or at the request of one or more national supervisory authorities, the European Parliament, the Council, the Commission or the Securities and Markets Stakeholder Group. To this end, ESMA may collect the information which it considers relevant from the corresponding national supervisory authority, which is obliged to provide it. In this context, ESMA may address a recommendation to said authority for it to take the necessary measures to re-establish compliance with Community law. The national supervisory authority must inform ESMA of the measures which it has adopted or it proposes to adopt in order to ensure compliance.

As a second step, in the event that the authority has not adopted any measure, the Commission, following communication from ESMA or on its own initiative, will

¹⁷ The possibility of adopting guidelines, recommendations and non-binding standards was already assigned to CESR, although the attribution to ESMA of the transparency measure described above is a new aspect incorporated by Regulation 1095/2010, given that the Commission Decision of 23 January 2009 establishing the Committee of European Securities Regulators, only established that members of the CESR which did not follow the guidelines, recommendations, standards and other measures agreed by the CESR must "be prepared to present the reasons for this choice".

issue a formal opinion requiring the national supervisory authority to take the action necessary to comply with Community law, taking into account the recommendation by ESMA. The national supervisory authority will inform the Commission and ESMA of the action to be carried out to comply with the formal opinion.

As a third step, the resolution mechanism includes the possibility that ESMA may adopt an individual decision directly addressed to a participant or institution, including cessation of any practice. Said decision must meet the following objectives: (i) maintain or restore “neutral conditions of competition in the market” or (ii) “ensure the orderly functioning and integrity of the financial system” (Article 17.6).

For this purpose, Regulation 1095/2010 expressly establishes that the decisions of ESMA shall prevail over any previous decision adopted by the competent authorities on the same matter (Article 17.7).

3.1.5 Powers in emergency situations

Article 18 provides a warning procedure with less intervention by the Commission than the procedure described in the above section, but subject to the limits deriving from the prohibition on intervening in fiscal/budgetary aspects and which is applicable both to the procedure described herein and that established in Article 19 (Article 38). Specifically, Article 18 provides that, in the case of “adverse developments which may seriously jeopardise the orderly functioning and integrity of financial markets or the stability of the whole or part of the financial system in the Union”, ESMA may actively facilitate and, where deemed necessary, coordinate any actions undertaken by the relevant national competent supervisory authorities. In order to be able to perform that task, ESMA shall be fully informed of any relevant event, and it shall be invited to participate as an observer in any relevant meeting of national competent supervisory authorities.

However, in some situations simple coordination may not be sufficient, especially when the national supervisory authorities individually lack the necessary instruments to react quickly to a cross-border emergency. Therefore, in said circumstances, ESMA is empowered to oblige the aforementioned authorities to jointly adopt specific measures.

Nevertheless, since the determination of the existence of a cross-border emergency situation entails a significant level of discretion, it is the Council that must declare the emergency situation. In this regard, Article 18 establishes that the Council, following a request from any of the ESAs, the Commission or the ESRB, “may adopt a decision addressed to ESMA, in which it determines the existence of an emergency situation”.

Only if the Council endorses this decision, and in the exceptional circumstances in which coordinated action of the national supervisory authorities is necessary to respond to adverse situations, ESMA may adopt individual decisions requiring competent authorities to take the necessary action to address any such situation.¹⁸

18 It should be pointed out that, although the wording of Article 18.3 is not totally clear, there is consensus in interpreting that this power requires both conditions, i.e. that the Council has issued the declaration of an emergency situation and that there are “exceptional circumstances”.

In accordance with section 4 of Article 18 of Regulation 1095/2010, where a competent authority does not comply with the decision of ESMA, then ESMA may adopt (where the relevant requirements laid down in sectoral legislation, including the technical standards adopted in accordance with said legislation are directly applicable to financial market participants) an individual decision addressed to a financial market participant requiring necessary action to comply with its obligations under that legislation, including the cessation of any practice. The wording of this clause, although similar to the procedure established in Article 17 for resolving alleged breaches of Community law, differs in that its application requires a “manifest breach” instead of a simple breach and, at the same time, where urgent remedying is necessary to restore the orderly functioning or integrity of financial markets or the stability of the whole or part of the financial system in the Union. Decisions adopted by virtue of this procedure shall prevail over any previous decision adopted by the competent authorities in the same matter.

At any event, the measure described in the above paragraph must be understood without prejudice to the possible commencement of breach procedures by the Commission against the Member States for failure to fulfil an obligation (Article 258 of the Treaty of Lisbon), without prejudice to the right of the Commission in said circumstances to request provisional measures in accordance with the rules of procedure of the Treaty of Lisbon, and without prejudice to any liability of the Member States in accordance with the case-law of the Court of Justice of the EU if its national supervisory authority does not adopt the measures required by ESMA.

Notwithstanding the above, the powers attributed to ESMA in emergency situations have a significant limit in the get-out clause. This provision allows Member States to request that ECOFIN cancels the decisions which ESMA (Article 38) has adopted in use of the procedures established in Article 18 (emergency situations) or Article 19 (disagreement between supervisors) which impinge on the fiscal responsibilities of the Member States.

3.1.6 Mechanism for settling disagreements between national supervisory authorities

Article 19 provides a mechanism for settling disagreements between the different national supervisory authorities. Pursuant to this mechanism, ESMA is empowered to assist the national authorities in conflict with the aim of reaching an agreement in those events in which it can be determined that there are disputes on the basis of “objective criteria” either at the request of any of the authorities involved or on its own initiative. However, Regulation 1095/2010 provides no guidelines on what are considered objective criteria, which provides a certain margin of discretion to ESMA to initiate the procedure.

Having determined the existence of a dispute, ESMA will firstly act as a mediator. It will set a time limit for conciliation between the national supervisory authorities, taking into account any relevant time period specified in the base legislation as well as “the complexity and urgency of the matter” (Article 19 [2]).

If the national supervisory authorities fail to reach an agreement within the conciliation phase, ESMA may require said authorities to adopt decisions or meas-

ures aimed at resolving the disagreement in accordance with and consistent with Community law. The decision by ESMA will be binding on the authorities involved.

Without prejudice to the powers which Article 258 of the Treaty of Lisbon confers on the Commission, where a competent national supervisory authority does not comply with the decision of the ESMA and thereby fails to ensure that the financial institution complies with the applicable legislation or the decision adopted in accordance with the paragraphs above, ESMA may adopt an individual decision addressed to said financial institution requiring that it adopt the measures necessary to comply with its obligations under Community law, including the cessation of any practice (Article 19 [4]). The decisions adopted pursuant to this Article shall prevail over any previous decision adopted by the national supervisory authorities on the same matter.

The procedure provided in Article 19 aims to avoid conflict between national supervisors, and between the supervisors and ESMA, as well as to ensure consistent and uniform application of Community law. In practice, ESMA is granted considerable powers both with regard to national authorities, on which it may impose a decision, and with regard to institutions, which it may directly address in the event of a failure to comply with obligations.

3.1.7. Execution of the decisions

Regulation 1095/2010 does not provide the manner of execution of the decisions and measures adopted by ESMA with regard to the procedures included in Article 17 (action in the event of a breach of Community law), Article 18 (emergency situations) and Article 19 (disagreement between supervisors).

During the legislative debates, the European Parliament proposed that in the event of a breach by a market participant of the decision adopted by ESMA, the Authority may initiate a procedure before a national court, which will include all types of summary or interlocutory procedures.¹⁹ However, in the end no mention is included. Consequently, the future sectoral and specific legislation will need to be consulted to verify the inclusion of rules in this matter.

3.1.8 Other tasks and responsibilities

In addition to the tasks of ESMA presented above, which have been thoroughly explained due to their special importance, Regulation 1095/2010 confers other tasks and responsibilities, some of which were held by the CESR (although not exactly of the same nature) in accordance with the Commission Decision of 23 January 2009, establishing the Committee of European Securities Regulators,²⁰ while others have been conferred to ESMA for the first time.

19 See the report of the Committee of Economic and Monetary Affairs of the European Parliament of 3 July 2010, amendment 103.

20 OJEU 2009, L25/18.

The former, for information purposes, includes but is not limited to the following tasks:

- Monitoring, assessing and informing on trends, potential risks and vulnerabilities with regard to securities so as to be able to determine at an early stage possible risks existing at a cross-border and cross-sectoral level.²¹
- Contributing to establishing a common supervisory culture, ensuring uniform procedures and consistent supervisory practices in the EU.
- Stimulating and facilitating delegation of tasks and responsibilities from a national supervisory authority to ESMA or to other national authorities, identifying those tasks and responsibilities that can be delegated or jointly exercised by promoting best practices.
- Contributing to promoting and monitoring the functioning of the colleges of supervisors.²²
- Periodically conducting peer reviews of some or all of the activities of national supervisory authorities to further strengthen consistency in supervisory outcomes (to that end, methods shall be developed to allow for objective comparisons of the activities of the national supervisory authorities examined). Based on these reviews, ESMA will publish the best practices that have been identified, and all the other results of the reviews may be publicly disclosed with the agreement of the national supervisory authority subject to the review. On the basis of a review, ESMA may issue non-binding guidelines and recommendations.
- Playing an international and advisory role.²³

21 Although ESRB will be responsible for macro-prudential assessment of the financial sector in the EU, ESMA must continue the work of CESR in this area, as the object of this analysis will be different, in the sense that the micro-prudential analysis provides an ascending analysis, while the macro-potential analysis is descending.

22 ESMA has the right to fully participate in the colleges of supervisors (including on-site examinations), with the aim of streamlining its functioning and information exchange process and to stimulate convergence and consistency between the colleges when applying EU law (thus avoiding distortions in competition and the regulatory arbitrage which derives from different supervisory practices). Nowadays, in the strict field of securities there are no colleges of supervisors, unlike in the banking sector, where they play an extremely important role.

23 Although CESR already exercised these functions, Regulation 1095/2010 provides new powers to ESMA in this respect. Therefore, in an attempt to respond to the need for actions which make it possible to build a stronger and more coherent regulation and supervision system for financial services worldwide, the role of ESMA (and other ESAs) is strengthened as a point of contact for the supervisory authorities of third countries, providing it with the possibility to enter into administrative agreements with supervisory authorities, international organisations and third country administrations and to participate in preparing decisions on the equivalence of the supervisory regimes in third countries. Regulation 1095/2010 also strengthens the advisory role of ESMA, assigning it the possibility, on its own initiative, or at the request of the European Parliament, the Council or the Commission to issue opinions addressed to the Parliament, the Council and the Commission on all issues relating to its area of authority, i.e. assigning it the authority to act as an independent advisory body of said Community institutions.

From the latter, we can highlight the assignment of responsibilities relating to the European investor compensation scheme,²⁴ or certain tasks assigned to ESMA with regard to systemic risk, as well as its relations with the ESRB. In this regard, ESMA will conduct the following tasks:

- In collaboration with the ESRB, it will develop a common approach for the identification and measurement of systemic risk.
- It shall consider, where appropriate, the monitoring and assessment of systemic risk as developed by the ESRB and ESMA, and shall respond to warnings and recommendations by the ESRB.
- It shall draw up, as necessary, additional guidelines and recommendations for key financial market participants, to take account of the systemic risk posed by them.
- Upon a request from one of the national supervisory authorities, the European Parliament, the Council or the Commission, or on its own initiative, ESMA may conduct an inquiry into a particular type of financial activity or type of product or conduct in order to assess potential threats to the integrity of financial markets and make appropriate recommendations for action to the national supervisory authorities concerned.
- Following consultation with the ESRB, ESMA shall establish criteria for the identification and measurement of systemic risks and an adequate stress testing regime.
- ESMA shall contribute to active participation in the development and coordination of effective and consistent recovery and resolution plans, procedures in emergency situations and preventive measures to minimise the systemic impact of any failure (it may develop, in this regard, regulatory and implementing technical standards).

With regard to the specific relations between ESMA and the ESRB, and for the purpose of ensuring fluid interaction between macro-prudential and micro-prudential supervision, Regulation 1095/2010 establishes, in addition to the mutual obligation to share all the pertinent information, the obligation of ESMA to ensure appropriate follow-up of the warnings and recommendations which the ESRB addresses to ESMA or to a national supervisory authority, as the case may be. Regulation 1095/2010 specifies the procedure to be followed by ESMA in these cases. If ESMA or the addressee decides not to follow the recommendation of the ESRB, they must explain the reasons – although in general it is established that in discharging its task, ESMA shall take the “utmost account” of the warnings and recommendations of the ESRB.

24 Within the context of the current review of Directive 97/9/EC, relating to the investor compensation systems, Regulation 1095/2010 indicates that the Commission wishes to pay special attention to the need for greater harmonisation throughout the EU. Hence, recognition is given to the need that ESMA play a significant role in this area, assigning the capacity to adopt guidelines and recommendations and to prepare regulatory technical standards and implementing technical standards in this matter.

Finally, it is important to point out a new attribution of Regulation 1095/2010, relating to the possibility to address a duly justified and reasoned request for information directly to a financial market participant where a national competent authority, which would normally be responsible for providing the information as it is the closest authority, does not or cannot provide such information in a timely fashion.²⁵

3.2 Field of application

3.2.1 Omnibus I Directive

Regulation 1095/2010 already established in Article 1 the sectoral guidelines which had to be amended to allow the new responsibilities, indicating the possibility that new legislation would be drawn up in the future. In this regard, it expressly stated the need to amend, *inter alia*, the following directives:

- Directive 98/26/EC of 19 May 1998 on settlement finality in payment and security settlement systems.
- Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market.
- Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money-laundering and terrorist financing.
- Directive 2006/48/EC of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions.
- Directive 2004/39/EC of the European Parliament and the Council of 21 April 2004 on markets in financial instruments (MiFID Directive).
- Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS Directive).
- Directive 2006/49/EC of 14 June 2006 on the capital adequacy of investment firms and credit institutions (evaluation methodology, notification of waiver to application of capital requirements).

²⁵ In this regard, Regulation 1095/2010 goes beyond the Commission Decision of 23 January 2009, establishing the Committee of European Banking Supervisors, which only entrusted the CESR with the task of promoting an effective bilateral and multilateral exchange of information between supervisory authorities.

- Regulation (EC) No. 1060/2009 (credit rating agencies).
- Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directive 2003/41/EC and 2009/65/EC and Regulations (EC) No. 1060/2009 and (EU) No. 1095/2010.

It was Directive 2010/78/EU of 24 November 2010 (known as Omnibus I Directive) which was the legislative instrument chosen to carry out the amendments in the aforementioned sectoral directives.

In addition to the general objectives of all Community legislation (ensuring a unified European code, attempting to consistently apply EU rules and ensuring a common supervisory culture), the Omnibus Directive was designed to address the problems found on analysing the legislative framework of each one of the sectoral directives. The aim was essentially to resolve the failures demonstrated in cross-border supervision, divergent supervisory practices and the fragmentation of supervisory responsibilities in a single group, as well as the lack of consistency and harmonisation of the penalty regime throughout the Union.

The selection of the specific areas for action in each sectoral directive was governed by clear and precise principles. On drawing up the Omnibus Directive, an attempt was made to only select fields which actually contributed effectively to achieving the objectives set, that were truly technical (principle of proportionality), which did not involve strategic decisions or fiscal responsibilities and which could not be achieved by the Member States, thus justifying intervention of the Union (principle of subsidiarity).

In addition, any legislation needed to be based on factual evidence accompanied by a prior periodic cost-benefit analysis, which in turn was preceded by public consultation to allow clear, concise and unambiguous technical standards to be drawn up (principle of legislative hierarchy).

In turn, the rules or the intervention had to respect the discretion provided in sectoral directives (principle of caution in supervision) as well as to guarantee and facilitate cooperation between supervisors (principle of cooperation).

Bearing in mind the above, the Omnibus Directive was drawn up in such a way that each one of the sectoral directives was defined in the specific areas in which the European supervisory authorities can and should propose technical standards, the specific cases in which the ESAs may intervene using the mechanism for resolving disagreements in those cross-border contexts in which the legislative acts provided for cooperation, as well as the actions of the authorities in specific emergency situations.

Finally, the Omnibus Directive determines specific requirements for registration, communication and information for the national supervisory authorities with regard to the corresponding European Authority so that the latter may have as full and up-to-date an image as possible of the financial market and its participants within the Union.

3.2.2 European Regulation on credit rating agencies

The Commission proposed including significant amendments to Regulation (EC) No. 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, for the purposes of entrusting ESMA with the direct responsibility for supervising these agencies as from July 2011.

As a result of the proposal, on 31 May 2011, Regulation (EU) No. 513/2011 of the European Parliament and of the Council of 11 May 2011 amending Regulation (EC) No. 1060/2009 on credit rating agencies, was published.²⁶

In this context, it was appropriate to clearly define the scope of the responsibilities of the new authority, so that the participants in financial markets could identify which authority was responsible for the activity of credit rating agencies. Accordingly, ESMA is assigned general powers with regard to permanent registration and supervision of registered credit rating agencies and must be the exclusive body responsible for registration and supervision of credit rating agencies in the Union. Accordingly, although ESMA may delegate specific tasks to national supervisory authorities, it is explicitly stated that in these circumstances ESMA remains legally responsible.

It is also assigned disciplinary powers. In this regard, during the legislative drafting period, the Commission argued that it was the only Community institution empowered to sanction said institutions. With a consensus promoted by the Parliament, it was finally agreed to grant the new authority powers to impose fines. Accordingly, ESMA is empowered to impose compulsory fines aimed at obliging credit agencies to put an end to an infringement, to supply complete information required by ESMA or to submit to an investigation or on-site inspection. The fines must be imposed based on the seriousness of the infringement. In order to determine the amount of the fine corresponding to a specific infringement, the Authority must use a two-step methodology, consisting of setting a basic amount for the fine and adjusting that basic amount, if necessary, by certain coefficients linked to aggravating and mitigating circumstances in order to ensure that the fine is proportionate to the seriousness of the infringement committed by a credit rating agency, taking into account the circumstances under which the infringement was committed.

In order to carry out its function effectively, ESMA is empowered to require, by simple request or by decision, all the information necessary from credit rating agencies, persons involved in credit rating activities, rated entities and related third parties, third parties to whom the credit rating agencies have outsourced operational functions or activities and persons otherwise closely and substantially related to those credit rating agencies or credit rating activities. Similarly, in order to exercise the supervisory powers effectively, ESMA should be able to conduct investigations and on-site inspections.

²⁶ In June, the BOE (Official State Gazette) published Act 15/2011 of 16 June amending certain financial rules for the application of Regulation (EC) No. 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies.

It is also empowered to submit draft regulatory technical standards to the Commission with regard to various issues and areas. These issues may include the information which agencies must provide in their applications for registration, for the application for certification and for an assessment of its systemic importance as well as other aspects relating to the presentation of the information. On drawing up its draft technical standards, ESMA must assess whether it is appropriate and necessary to update the guidelines already issued by the Committee of European Securities Regulators regarding the content of Regulation 1060/2009.

In the areas not covered by technical standards, the Authority should have the power to issue and update non-binding guidelines on aspects related to the application of Regulation No. 1060/2009.

In short, the new provisions show the importance of the powers granted to ESMA in this area, largely as a consequence of the support of the European Parliament for ESMA as a specialised and independent body within the European institutions which is different from the Commission.

3.2.3 Other empowering legislative instruments

3.2.3.1 Omnibus II Directive

On 19 January 2011, the European Commission published its proposal for the Omnibus II Directive, as it had already announced at the end of 2009. This Directive aims to amend Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published with securities offered to the public or admitted to trading and amending Directive 2001/34/EC, as well as Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) to include the powers of ESMA adjusted to the new supervisory situation.

3.2.3.2 Legislative proposals on OTC derivatives

In September 2010, the Commission published a proposal for a regulation on over-the-counter (OTC) derivatives, central counterparties (CCP) and repositories pursuant to which ESMA is granted significant powers as it must develop a series of draft technical standards in critical areas. It is also granted powers with regard to third country central counterparties and centralisation of information registers on derivatives, as well as disciplinary powers in the event of infringements. Once again, ESMA will play a significant role in the new legislation.

3.3 Internal organisation

3.3.1 Decision-making body: the Board of Supervisors

The Board of Supervisors is the main decision-making body of ESMA and, as such, is responsible for adopting the draft technical standards, the opinions, the recommendations and the decisions of ESMA.

It is made up, with voting rights, of the head of the competent supervisory authority of each Member State (who, as the case may be, may be accompanied by a representative of the bodies which administer the investor compensation schemes in each Member State, without voting rights). It also includes, without voting rights, the Chair of ESMA, a representative of the Commission, a representative of the ESRB, a representative of EBA and another of EIOPA. The Executive Director of ESMA may participate in the meetings of the Board of Supervisors, without voting rights. In addition, the Board of Supervisors may decide to admit observers.

In general, its decisions are adopted by a simple majority of its members, with each member having one vote, with one exception: the development of draft technical standards, guidelines and recommendations and the decisions on the financial provisions of ESMA, which are adopted by a qualified majority.²⁷

The Chair and the members of the Board of Supervisors with voting rights must act independently and objectively solely in the interests of the EU as a whole, and may not request or accept any instruction from EU institutions or bodies or any Government of a Member State or any other private or public entity. Neither the Member States nor the EU institutions or bodies, nor any other public or private entity may try to exercise their influence over the members of the Board of Supervisors.

3.3.2. Administration body: the Management Board

The Management Board ensures that ESMA complies with its obligations and carries out its assigned tasks and is responsible for preparing the working program and the program for adopting its internal regulation.

The Management Board is composed of, with voting rights, the Chair of ESMA and another six members of the Board of Supervisors, elected by the members with voting rights of said Board. It is also made up, without voting rights, of the Executive Director of ESMA and by a representative from the Commission. The members of the Management Board are subject to the same obligations of independence and objectivity as described above for the members of the Board of Supervisors. Its decisions are adopted by majority of the members present, with each member having one vote.

The Vice-President of the CNMV, Fernando Restoy, forms part of the first Management Board of ESMA.

3.3.3. Representation body: the Chair

ESMA is represented by a full-time Chair, designated by the Board of Supervisors on the basis of his/her merits, following an open selection process. The European Par-

²⁷ This decision-making system is very different from that which existed in the CESR, where decisions were generally taken by the agreement of its members. Only in the event that an agreement could not be reached would said decisions be taken by a qualified majority, with the correspondence between votes of the members of the CESR and votes of the Member States provided in Article 238 (formerly Article 205, sections 1 and 2 TCE) of the Treaty on the Functioning of the EU. See Article 14 of the Commission Decision of 23 January 2009 establishing the Committee of European Securities Regulators.

liament may object to his/her designation. Steven Maijor (from the AFM)²⁸ was recently elected as the first Chair of ESMA for a period of five years, with the approval of the European Parliament.

The Chair is responsible for preparing the work of the Board of Supervisors and chairs both the meetings of this body and those of the Management Board. The Chair's independence and objectivity is guaranteed by similar provisions to those applicable to the members of the Board of Supervisors and the Management Board.

3.3.4 Management body: the Executive Director

Management of ESMA is entrusted to an Executive Director, who is a full-time independent professional, appointed by the Board of Supervisors in an open selection process based on the merits of the candidates. The appointment requires prior confirmation by the European Parliament. Verena Ross (FSA)²⁹ was recently elected as the first Executive Director of ESMA for a period of five years.

The Executive Director prepares the work of the Management Board and is responsible for executing the work programme of ESMA. He/she has the right to participate, without voting rights, in the meetings of the Board of Supervisors and the Management Board and is subject to similar independence and objectivity provisions as those provided for the members of the Board of Supervisors and the Management Board.

3.4 Legal remedies

Any natural or legal person, including the national supervisory authorities, may appeal the decisions of ESMA relating to breaches of EU law or its actions in an emergency situation and the binding resolution of disagreements between national supervisory authorities, as well as any other decision adopted by ESMA, in accordance with sectoral legislation, of which it is the addressee, or a decision which, although it appears to address another person, affects him/her directly and individually.

For this purpose, a Board of Appeal is established, conceived as a common body for ESMA, EBA and EIOPA, to deal with issues related with banking, insurance and securities. It is made up of six members and six alternates, who will be independent and impartial in exercising their functions. The Management Board of ESMA will appoint two members of the Board of Appeal and two alternates from a restricted list proposed by the Commission, for a term of five years (and the management boards of the EBA and EIOPA will do the same).

The decisions of the Board of Appeal will be adopted by a majority, as a minimum, of four of its six members, and when the appealed decision belongs to the field of application of Regulation 1095/2010, this majority must include at least one of the two members appointed by ESMA.

28 The Autoriteit Financiële Markten is the supervisory authority of the Netherlands.

29 The Financial Services Authority is the supervisory authority of the United Kingdom.

The period for presenting the appeal is two months from the notification date to the interested party or, failing that, from the date on which ESMA published its decision. Filing of the appeal shall not have suspensive effect, but the Board of Appeal may suspend application of the appealed decision if it considers that the circumstances require it.

The Board of Appeal may confirm the decision adopted by the competent Department of ESMA or it may submit the issue to said Department. This will be bound by the decision of the Board of Appeal and will adopt an amended resolution relating to the issue in question.

The resolutions of the Board of Appeal or, in the event that it does not intervene, of ESMA, may be appealed in the Court of Justice of the EU in accordance with Article 263 of the Treaty of Lisbon, both by the Member States and the institutions of the EU, and by any natural or legal person. It is also established that an action for a declaration of failure to act may be brought before the Court of Justice in accordance with Article 265 of the Treaty of Lisbon in the event that ESMA, being obliged to intervene, fails to take a decision.

4 Final reflections

The supervisory and regulatory system of the securities markets in Europe has been characterised until recently by a prevalence of local control over EU control. It has only been in the first decade of this century that the regulation and supervision of the securities market has been “impregnated” with Community harmonisation, mainly as a consequence of the development of the Financial Services Action Plan, published in 1999.

In the field of the supervision of securities markets, the creation of a new European supervisory architecture as a response to the recent crisis which began in 2007 has meant that national supervisory authorities must coexist with the new European Securities and Markets Authority, which was created with a wide range of powers to develop draft technical standards, intervene by means of the mechanism for resolving disagreements and act directly on institutions and markets in emergency situations, which is going to involve a challenge with regard to coordination and supervision and control actions of securities markets and their participants.

The assumption by the European Union of greater responsibilities will have effects on the distribution of powers in this matter with the aim of achieving market unity and a single economic structure and planning which, in the case of securities markets goes beyond national boundaries in favour of Community harmonisation and the single rulebook.

All of this will have an immediate reflection on Spanish legislation and it is possible that the mission to be fulfilled by the competent administrative authorities will vary, as well as the powers that they have had up to now to achieve the mandates entrusted to them and which justify intervention in the financial market.

IV Legislative Annex

New legislation approved since publication of the CNMV bulletin for the second quarter of 2011, in chronological order, is as follows:

- **Royal Decree 771/2011, of 3 June**, which amends Royal Decree 216/2008, of 15 February, on Own Funds of Financial Institutions and Royal Decree 2606/1996, of 20 December, on Deposit Guarantee Funds of Credit Institutions.

This legislation implements the modifications related to the own funds of financial institutions introduced by Act 6/2011, of 6 April, by transposing Directive 2009/111/EC, of 16 September 2009 (known as the Basel II Agreement). The main aspects of this legislation, which affects both credit institutions and investment service firms, are as follows:

- It introduces amendments relating to risk concentration.
 - It improves the supervision of cross-border banking groups: it regulates the “colleges of supervisors” for the financial groups which operate in various EU countries and clarifies the powers and responsibilities of the national supervisory authorities, making their cooperation more effective.
 - It improves regulation of the quality of banks’ own funds, especially relating to “hybrid” instruments. For the purposes of solvency legislation, it distinguishes the instruments that do not rank *pari passu* with ordinary shares during liquidation or do not fully absorb losses on a going-concern basis *pari passu* with ordinary shares.
 - It adapts liquidity risk management and improves risk management for securitised instruments. Firms which assign their assets in the securitisation process must maintain part of the risks inherent to those assets, while companies which invest in the assets must show due diligence and acquire sufficient information. If they fail to do so, they will be subject to heavy capital penalties.
 - It regulates the remuneration policy for employees and executives so that variable remuneration is to some extent related to the long-term results of the financial institutions. Similarly, it requires that staff undertake not to use personal hedging or insurance strategies relating to the remuneration and responsibility that reduces the affects of alignment with the risk included in their remuneration systems.
 - Furthermore, in line with the provisions relating to deposit guarantee funds which are currently being carried out at a European level, it introduces a new regime for additional contributions to these funds based on the remuneration of the deposits. Specifically, it requires additional contributions from institutions which excessively remunerate both their term and sight deposits.
- **Directive 2011/61/EU of the European Parliament and of the Council, of 8 June 2011**, on Alternative Investment Fund Managers amending Directive 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

The Directive establishes common requirements applicable to the authorisation and supervision of alternative investment fund managers (hedge funds), which are those not subject to Directive 2009/65/EC, of 13 July (UCITS Directive). It therefore establishes a harmonised framework for regulating and supervising the activities of all alternative fund managers in the EU, including those with their registered office outside the EU, establishing a passport system which allows cross-border activity in the EU. The Directive does not regulate the alternative investment funds themselves, but their managers, and establishes a period of two years for its transposition to national law.

In summary, it establishes the authorisation and registration regime, the rules of conduct and transparency of alternative fund managers, and the capital and organisational requirements. It should be highlighted that the legislation has a particular impact on remuneration policies, which must promote effective and responsible risk management. It also has an impact on the need to value assets reliably and objectively, the appointment of independent depositories, on the conditions for delegating functions, on the prevention of systemic risk deriving from the leverage of these alternative investment funds, for which it provides new instruments to ESMA and to the ESRB (European Systemic Risk Board), and the possible conflict-of-interest arising from the control of a company (whether listed or not) by an alternative investment fund.

- **CNMV Circular 2/2011, of 9 June**, on Information of Foreign UCITS Registered in the CNMV Registries.

As a result of the end of the period for transposing Directive 2009/65/EC of the European Parliament and of the Council (UCITS Directive), CNMV Circular 2/2006, of 27 June, is repealed and substituted, simplifying the notification procedure required of foreign collective investment schemes (CIS) which are going to be marketed in Spain and streamlining the information which must be sent to the CNMV about these CIS.

This notification procedure requires that CIS present the pertinent documentation to the competent authority of the home Member State. The Circular establishes a standardised model for the marketing report, since part of the information which must be provided in this notification procedure is not harmonised and refers to the provisions provided for marketing CIS in the host State.

Furthermore, it eliminates the requirements to register in the CNMV Registry of compartments, and it extends the content of the communication to be made to the CNMV in accordance with Article 52 of the Personal Income Tax Regulation so as to include the details of the compartments and/or classes referred to in the tax information. With regard to non-harmonised CIS, the requirement to send information by electronic means is cancelled.

- **CNMV Circular 3/2011, of 9 June**, which partially amends Circular 1/2009, of 4 February, on the Categories of Collective Investment Schemes based on their Investment Profile.

This Circular introduces some amendments relating to the categories of collective investment schemes (CIS) based on their investment profile, which is

regulated in Circular 1/2009, of 4 February. Accordingly, it clarifies that the calculation of the investment percentages of fixed income and equity of the investment profiles will take into account both spot investments and derivatives, i.e. the fund's total exposure. It also slightly amends the types of CIS and incorporates a harmonised EU-wide definition of monetary funds.

- **Act 15/2011, of 16 June**, amending certain Financial Rules for the application of Regulation (EC) No 1060/2009 of the European Parliament and of the Council, of 16 September 2009, on Credit Rating Agencies.

The approval of Regulation 1060/2009/EC on credit rating agencies makes it necessary to adapt the Securities Market Act 19/1992, of 7 July, on the Regime for Real Estate Investment Companies and Funds and on Mortgage Securitisation Funds and Act 13/1985, of 25 May, on Investment Ratios, Own Funds and Reporting Obligations of Financial Intermediaries, specifying the obligation of certain financial institutions to use the ratings issued by registered or certified agencies pursuant to the Regulation.

The authority to supervise these entities, in accordance with the EU Regulation, lies with the European Securities and Markets Authority, but it also regulates the relations which that body must maintain with the CNMV in this matter.

- **Royal Decree-Law 8/2011, of 1 July**, on Support Measures for Mortgage Debtors, on Control of Public Spending and Cancellation of Debts with Companies and Self-Employed Persons Contracted by Local Entities, on Promotion of Business Activities and Fostering Administrative Restructuring and Simplification.

This Decree-Law adopts an extremely varied series of measures to strengthen the response capacity of the Spanish economy to the international financial crisis. Together with other fiscal measures or measures to speed up the process of creating companies, the following significant amendments to mortgage law are adopted, which have an indirect impact on the securities market:

- It extends the limit of the immunity from seizure of income up to 150% of the minimum inter-professional salary (Spanish acronym: SMI) for those mortgage debtors who have lost their first residence and an additional 30% for each family member who does not receive income above the aforementioned SMI.
 - In order to promote legal security in the real estate sector, the Property Register will now incorporate information that will allow purchasers of real estate to know in advance any possible litigation involving the property, including the proceedings which may involve the imposition of fines or future demolition.
- **Act 21/2011, of 26 July**, on Electronic Money.

This Act introduces amendments to the legislation on electronic money institutions which had been introduced by Act 44/2002, of 22 November, on

Reform Measures for the Financial System, and its implementing legislation. It adapts the regulation of these institutions to Act 16/2009, of 13 November, on Payment Services, in some aspects such as the field of services to which the regulation on electronic money is not applicable. It also allows electronic credit institutions to provide payment services.

- **Act 25/2011, of 1 August**, on the partial reform of the Capital Companies Act and incorporation of Directive 2007/36/EC, of the European Parliament and of the Council, of 11 July 2007, on the Exercise of Certain Rights of Shareholders in Listed Companies.

The Act of partial reform of the Capital Companies Act and incorporation of Directive 2007/36/EC, of the European Parliament and of the Council, of 11 July, on the exercise of certain rights of shareholders in listed companies has a two-fold aim. Firstly, it aims to reduce the organisation and operating costs of capital companies and achieve the necessary modernisation of the law of these types of companies, as well as to remove some of the most unjustified differences existing between the regime for *sociedades anónimas* (public limited companies) and that for *sociedades de responsabilidad limitada* (limited liability companies). Secondly, it obeys the need to transpose to national law Directive 2007/36/EC, the essential purpose of which lies in facilitating and promoting the exercise of information and voting rights of the shareholders of listed companies within the EU.

With regard to reducing the costs of capital companies, the Act eliminates some requirements to place advertisements in the official or private press, especially those relating to the calling of the General Shareholders' Meeting, resolutions for amending articles of association, publication of the dissolution of the company or the annual accounts during the liquidation period. It also establishes measures which lower the cost of filing the annual accounts, reducing the required paperwork.

For the first time by force of law, it regulates the legal regime of the legal entity director, with specific reference to the joint and several liability of the represented legal entity and the representative. Furthermore, it empowers directors which represent at least one third of the Board of Directors to call a meeting when the Chairman, despite being required to do so, has not called a meeting.

Unification of the regime of public limited companies and limited liability companies occurs with regard to the calling of General Shareholders' Meetings, the acceptance that the articles of association of public limited companies may establish, instead of a rigid structure of the management body, two or more types of organisation, the possibility of introducing into the articles causes for exclusion of shareholders, the consideration of inactivity as a cause for dissolving all capital companies, the generalisation of the default rule on automatic conversion of the company's directors in liquidators and the legal regime of the liquidators of cancelled companies. Similarly, in reference to the amendment of point 1 of Article 157 of the Capital Companies Act, failure to comply with the obligations or infringement of the prohibitions established in said

chapter by public limited companies and limited liability companies shall be considered a breach.

Furthermore, starting from the principle of equal treatment for shareholders which are in the same position with regard to information, participation and votes in the General Shareholders' Meeting, a special regime is created for exercising shareholders' rights to participation in the General Shareholders' Meeting of listed companies. It regulates in special detail the functioning of the General Shareholders' Meeting, requiring that Extraordinary Meetings are called at least 15 days in advance. It also provides the possibility of shareholders voting by electronic means, and regulates the advertising of the announcement and the complementary documentation, the right to complete this announcement and to present new agreement proposals, as well as the shareholders' right to information and participation, and distance voting in the General Shareholders' Meeting.

Finally, it limits the set of rules contained in Title XIV of the Capital Companies Act. Failure to comply with these rules will lead to the CNMV starting disciplinary proceedings. Similarly, it amends the Securities Market Act 24/1988, of 28 July, in such a way that the events of non-compliance included in Articles 516, 517, 520.2 and 524.2 of the consolidated text of the Capital Companies Act are now considered as serious breaches in accordance with the provisions in Article 100 of the Securities Market Act.

- **Order EHA/2288/2011, of 2 August**, which amends the Order of 19 May 1987, which implements Royal Decree 505/1987, of 3 April, which provides the creation of a Book-Entry System of Government Debt.

This Order grants the possibility that other bodies of the Central Government, in addition to the Public Treasury and the General Treasury of the Social Security are recognised as holders of accounts in the Book-Entry System of Government Debt.

Accordingly, the public bodies of the Central Government other than the Public Treasury and the General Treasury of the Social Security, following the procedure established for acquiring the condition of account holder in their own name in the Book-Entry System of Government Debt, may carry out the operations which they deem necessary in the public book-entry debt market, without having to act through an intermediary or financial institution.

V Statistics Annex

1 Markets

1.1 Equity

Share issues and public offerings¹

TABLE 1.1

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
CASH VALUE³ (million euro)								
Total	16,349.3	11,390.7	16,012.7	2,322.6	8,333.3	3,237.0	4,797.6	6,321.8
Capital increases	16,339.7	11,388.7	15,407.0	2,322.6	8,262.0	3,237.0	4,797.6	6,321.8
Of which, primary offerings	292.0	17.3	958.7	6.0	14.2	0.0	3,696.4	8.4
With Spanish tranche	292.0	14.9	61.6	5.9	13.9	0.0	3,696.4	8.4
With international tranche	0.0	2.5	897.2	0.0	0.3	0.0	0.1	0.0
Secondary offerings	9.5	1.9	605.7	0.0	71.4	0.0	0.0	0.0
With Spanish tranche	9.5	1.9	79.1	0.0	71.4	0.0	0.0	0.0
With international tranche	0.0	0.0	526.7	0.0	0.0	0.0	0.0	0.0
NOMINAL VALUE (million euro)								
Total	1,835.8	1,892.1	6,313.4	2,234.5	1,083.2	547.7	1,975.9	2,624.5
Capital increases	1,835.7	1,892.0	6,304.4	2,234.5	1,074.3	547.7	1,975.9	2,624.5
Of which, primary offerings	100.0	0.1	1.9	0.7	1.0	0.0	1,871.3	0.5
With Spanish tranche	100.0	0.1	1.8	0.7	0.9	0.0	1,871.3	0.5
With international tranche	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0
Secondary offerings	0.1	0.0	9.0	0.0	8.9	0.0	0.0	0.0
With Spanish tranche	0.1	0.0	8.9	0.0	8.9	0.0	0.0	0.0
With international tranche	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
NO. OF FILES⁴								
Total	54	53	69	12	29	17	23	21
Capital increases	53	53	67	12	28	17	22	21
Of which, primary offerings	2	2	12	2	4	0	3	3
Of which, bonus issues	18	11	15	3	7	2	5	6
Secondary offerings	2	1	3	0	1	0	1	0
NO. OF ISSUERS⁴								
Total	39	34	46	10	23	13	16	18
Capital increases	38	34	45	10	22	13	15	18
Of which, primary offerings	2	2	12	2	4	0	3	3
Secondary offerings	2	1	2	0	1	0	1	0

1 Includes registered offerings with issuance prospectuses and listings admitted to trading without register issuance prospectuses.

2 Available data: August 2011.

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	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
PRIMARY OFFERINGS								
Total	292.0	17.3	958.7	6.0	14.2	0.0	3,696.4	8.4
Spanish tranche	282.0	14.9	61.6	5.9	13.9	0.0	3,684.9	8.4
Private subscribers	191.5	0.0	2.5	2.5	0.0	0.0	2,203.9	2.3
Institutional subscribers	90.5	14.9	59.0	3.4	13.9	0.0	1,481.0	6.0
International tranche	0.0	2.5	897.2	0.0	0.3	0.0	0.1	0.0
Employees	10.0	0.0	0.0	0.0	0.0	0.0	11.4	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
SECONDARY OFFERINGS								
Total	9.5	1.9	605.7	0.0	71.4	0.0	0.0	0.0
Spanish tranche	9.5	1.5	79.1	0.0	71.4	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	9.5	1.5	79.1	0.0	71.4	0.0	0.0	0.0
International tranche	0.0	0.0	526.7	0.0	0.0	0.0	0.0	0.0
Employees	0.0	0.4	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

1 Available data: August 2011.

Companies listed¹

TABLE 1.3

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
Total electronic market ³	136	133	129	129	129	130	130	130
Of which, without Nuevo Mercado	136	133	129	129	129	130	130	130
Of which, Nuevo Mercado	0	0	0	0	0	0	0	0
Of which, foreign companies	5	5	6	5	6	7	7	7
Second Market	8	7	6	6	6	6	6	6
Madrid	2	2	2	2	2	2	2	2
Barcelona	6	5	4	4	4	4	4	4
Bilbao	0	0	0	0	0	0	0	0
Valencia	0	0	0	0	0	0	0	0
Open outcry ex SICAVs	29	29	28	28	28	28	28	28
Madrid	13	13	13	13	13	13	13	13
Barcelona	19	19	18	18	18	18	18	18
Bilbao	8	8	8	8	8	8	8	8
Valencia	7	6	6	6	6	6	6	6
Open outcry SICAVs	3	1	1	1	1	1	1	1
MAB ⁴	3,347	3,251	3,144	3,175	3,144	3,121	3,091	3,083
Latibex	35	32	29	31	29	29	29	29

1 Data at the end of period.

2 Available data: August 2011.

3 Without ETFs (Exchange Traded Funds).

4 Alternative Stock Market.

Capitalisation¹

TABLE 1.4

Million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
Total electronic market ³	531,194.2	634,762.8	590,182.8	568,142.8	565,585.2	619,538.0	609,135.8	503,669.4
Of which, without Nuevo Mercado	531,194.2	634,762.8	590,182.8	568,142.8	565,585.2	619,538.0	609,135.8	503,669.4
Of which, Nuevo Mercado	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which, foreign companies ⁴	61,317.5	94,954.0	92,275.8	83,898.4	100,249.8	104,571.0	103,403.8	79,323.3
Ibex 35	322,806.6	404,997.3	376,747.6	364,914.0	348,998.9	385,136.5	382,731.8	320,157.0
Second Market	109.9	80.9	69.1	74.9	74.6	59.4	57.5	58.8
Madrid	22.8	24.9	23.4	26.4	24.7	25.5	23.6	24.9
Barcelona	87.1	56.0	45.7	48.5	49.9	33.9	33.9	33.9
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	4,226.5	4,159.1	3,859.2	4,128.2	3,980.3	3,835.4	3,686.7
Madrid	1,454.7	997.3	958.0	924.0	878.8	873.3	841.7	814.0
Barcelona	3,580.2	3,400.6	3,336.4	3,139.2	3,432.2	3,325.1	3,187.2	3,077.9
Bilbao	45.9	435.4	433.4	386.9	362.1	322.4	321.2	316.9
Valencia	760.4	559.2	554.8	475.2	458.7	426.4	423.6	370.4
Open outcry SICAVs ⁵	126.8	28.5	28.1	30.9	32.6	33.0	36.1	36.2
MAB ^{5,6}	24,718.6	26,282.9	26,502.4	26,046.2	26,340.8	26,581.5	26,043.0	24,248.7
Latibex	210,773.5	412,628.9	437,016.7	408,834.8	435,337.8	425,895.7	452,926.3	404,800.3

1 Data at the end of period.

2 Available data: August 2011.

3 Without ETFs (Exchange Traded Funds).

4 Foreign companies capitalisation includes their entire shares, whether they are deposited in Spain or not.

5 It is only calculated with outstanding shares, but not with treasury shares, because they only report the capital stock at the end of the year.

6 Alternative Stock Market.

Trading

TABLE 1.5

Million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Total electronic market ²	1,228,392.4	877,073.5	1,026,478.5	213,520.2	291,987.6	244,908.3	236,325.4	173,997.0
Of which, without Nuevo Mercado	1,228,380.9	877,073.5	1,026,478.5	213,520.2	291,987.6	244,908.3	236,325.4	173,997.0
Of which, Nuevo Mercado	11.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Of which, foreign companies	1,407.1	4,750.4	6,415.3	1,158.2	1,258.6	1,379.9	1,056.0	757.9
Second Market	31.7	3.2	3.0	0.5	1.4	0.8	0.3	0.1
Madrid	3.4	2.0	2.8	0.5	1.3	0.5	0.1	0.1
Barcelona	28.3	1.2	0.3	0.0	0.0	0.3	0.2	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	182.1	52.8	157.2	53.1	81.2	18.1	7.5	2.1
Madrid	73.9	16.5	15.7	8.6	1.5	4.5	1.8	0.6
Barcelona	103.6	29.4	135.7	44.4	78.0	13.5	5.6	1.4
Bilbao	0.1	1.1	3.9	0.0	0.0	0.0	0.0	0.0
Valencia	4.5	5.9	1.9	0.1	1.7	0.1	0.1	0.0
Open outcry SICAVs	25.3	19.7	8.1	0.5	0.5	1.7	3.0	0.8
MAB ³	7,060.3	5,080.1	4,147.9	768.4	1,146.9	879.6	1,134.0	851.3
Latibex	757.7	434.7	521.2	93.5	119.2	102.3	89.4	60.5

1 Available data: August 2011.

2 Without ETFs (Exchange Traded Funds).

3 Alternative Stock Market.

Trading on the electronic market by type of transaction¹

TABLE 1.6

Million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
Regular trading	1,180,835.9	833,854.9	983,584.5	202,084.6	280,656.0	235,958.6	225,422.9	161,896.0
Orders	774,718.1	499,182.8	541,879.8	112,273.3	131,954.9	153,546.1	119,669.8	95,091.6
Put-throughs	105,673.9	51,335.8	58,678.1	12,924.2	15,505.2	22,522.2	13,555.7	12,780.9
Block trades	300,443.9	283,336.3	383,026.6	76,887.0	133,196.0	59,890.3	92,197.4	54,023.5
Off-hours	10,175.2	5,996.6	17,209.5	4,932.9	3,064.3	2,096.0	2,645.6	2,016.0
Authorised trades	3,183.2	4,695.6	2,660.5	200.2	1,025.8	843.3	676.6	1,116.7
Art. 36.1 SML trades	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Tender offers	17,461.2	7,188.9	312.0	38.8	0.0	0.0	233.8	3,983.1
Public offerings for sale	292.0	1,325.0	1,448.2	0.0	0.0	0.0	0.0	3,922.1
Declared trades	1,066.8	5,202.6	2,273.4	2,272.7	0.0	0.0	2,171.6	0.0
Options	9,661.9	11,443.2	11,474.7	2,010.5	5,235.2	3,501.6	2,717.4	245.7
Hedge transactions	5,716.3	7,366.7	7,515.8	1,980.4	2,006.3	2,508.7	2,457.5	817.5

1 Without ETFs (Exchange Traded Funds).

2 Available data: August 2011.

Margin trading for sales and securities lending

TABLE 1.7

Million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
TRADING								
Securities lending ²	583,950.8	471,007.1	556,246.7	123,594.7	154,640.3	108,561.1	142,262.8	96,636.9
Margin trading for sales of securities ³	624.9	704.3	598.0	155.6	130.1	212.3	112.9	70.8
Margin trading for securities purchases ³	154.7	106.4	65.9	12.9	16.9	19.8	11.4	11.2
OUTSTANDING BALANCE								
Securities lending ²	43,647.8	47,322.2	36,195.9	37,101.6	36,195.9	39,779.8	39,553.6	33,100.1
Margin trading for sales of securities ³	20.7	21.1	9.9	19.1	9.9	17.6	12.7	7.8
Margin trading for securities purchases ³	7.0	5.6	5.0	3.4	5.0	4.5	5.2	4.7

1 Available data: August 2011.

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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
NO. OF ISSUERS								
Total	179	168	115	33	47	43	42	24
Mortgage covered bonds	19	27	25	13	13	14	15	6
Territorial covered bonds	7	1	6	1	1	2	4	2
Non-convertible bonds and debentures	30	50	39	11	11	10	12	5
Convertible bonds and debentures	1	3	2	0	2	3	1	0
Backed securities	88	68	36	7	15	8	9	6
Commercial paper	77	69	58	9	19	15	12	6
Of which, asset-backed	2	2	2	0	1	0	1	0
Of which, non-asset-backed	75	67	56	9	18	15	11	6
Other fixed-income issues	0	0	0	0	0	0	0	0
Preference shares	8	23	0	0	0	1	0	0
NO. OF ISSUES								
Total	337	512	349	60	98	88	82	39
Mortgage covered bonds	47	75	88	24	21	32	29	7
Territorial covered bonds	8	1	9	1	2	4	4	10
Non-convertible bonds and debentures	76	244	154	19	38	19	27	10
Convertible bonds and debentures	1	6	3	0	3	6	1	0
Backed securities	108	76	36	7	15	10	9	6
Commercial paper	88	73	59	9	19	15	12	6
Of which, asset-backed	2	2	2	0	1	0	1	0
Of which, non-asset-backed	86	71	57	9	18	15	11	6
Other fixed-income issues	0	0	0	0	0	0	0	0
Preference shares	9	37	0	0	0	2	0	0
NOMINAL AMOUNT (million euro)								
Total	476,275.7	387,475.8	226,448.9	61,634.8	55,736.9	77,161.3	59,900.0	19,684.4
Mortgage covered bonds	14,300.0	35,573.9	34,378.5	10,317.0	8,519.1	19,254.0	18,980.0	2,250.0
Territorial covered bonds	1,820.0	500.0	5,900.0	300.0	500.0	2,935.0	1,800.0	2,664.2
Non-convertible bonds and debentures	10,489.6	62,249.0	24,356.0	1,287.2	7,524.7	2,578.1	3,320.2	407.6
Convertible bonds and debentures	1,429.1	3,200.0	968.0	0.0	968.0	681.6	1,500.0	0.0
Backed securities	135,252.5	81,651.2	63,260.5	28,189.7	16,497.3	26,585.0	11,168.4	6,159.3
Spanish tranche	132,730.1	77,289.4	62,743.0	28,189.7	16,473.3	23,706.2	10,130.0	6,159.3
International tranche	2,522.4	4,361.9	517.5	0.0	24.0	2,878.8	1,038.4	0.0
Commercial paper ³	311,738.5	191,341.7	97,586.0	21,540.9	21,727.9	24,927.6	23,131.3	8,203.3
Of which, asset-backed	2,843.1	4,758.4	5,057.0	1,723.0	1,409.0	546.0	913.0	84.0
Of which, non-asset-backed	308,895.4	186,583.3	92,529.0	19,817.9	20,318.9	24,381.6	22,218.3	8,119.3
Other fixed-income issues	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Preference shares	1,246.0	12,960.0	0.0	0.0	0.0	200.0	0.0	0.0
Pro memoria:								
Subordinated issues	12,949.5	20,988.5	9,154.2	1,838.5	2,048.2	5,407.9	2,696.5	1,640.0
Underwritten issues	9,169.5	4,793.8	299.0	0.0	0.0	10.0	0.0	0.0

1 Includes issuance and trading prospectuses.

2 Available data: August 2011.

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	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Total	476,710.4	388,455.0	223,404.5	65,590.3	48,230.5	70,790.8	68,289.8	26,343.6
Commercial paper	314,417.4	191,427.7	99,784.4	22,148.0	21,521.8	25,096.2	23,094.5	9,437.0
Bonds and debentures	10,040.3	61,862.5	24,728.6	1,541.1	7,512.4	2,080.6	3,616.9	585.5
Mortgage covered bonds	14,150.0	35,568.9	32,861.0	9,767.0	8,499.1	17,244.0	21,435.0	3,425.0
Territorial covered bonds	1,930.0	500.0	5,900.0	300.0	500.0	2,935.0	300.0	4,164.2
Backed securities	135,926.6	85,542.9	60,030.5	31,834.2	10,197.3	23,235.0	19,843.4	8,731.9
Preference shares	246.0	13,552.9	100.0	0.0	0.0	200.0	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: August 2011.

AIAF. Issuers, issues and outstanding balance

TABLE 1.10

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
NO. OF ISSUERS								
Total	556	614	634	628	634	631	613	609
Commercial paper	72	67	60	66	60	56	46	47
Bonds and debentures	93	91	93	91	93	91	93	93
Mortgage covered bonds	22	29	33	31	33	35	36	38
Territorial covered bonds	11	11	12	11	12	12	12	12
Backed securities	383	442	459	454	459	458	441	436
Preference shares	52	60	59	59	59	60	60	60
Matador bonds	12	12	12	12	12	12	12	12
NO. OF ISSUES								
Total	4,639	4,084	3,630	3,646	3,630	3,570	3,454	3,439
Commercial paper	2,489	1,507	958	999	958	911	851	838
Bonds and debentures	450	611	645	639	645	631	627	631
Mortgage covered bonds	146	202	253	239	253	267	277	282
Territorial covered bonds	26	25	26	25	26	28	29	38
Backed securities	1,436	1,629	1,641	1,637	1,641	1,625	1,562	1,542
Preference shares	78	96	93	93	93	94	94	94
Matador bonds	14	14	14	14	14	14	14	14
OUTSTANDING BALANCE² (million euro)								
Total	819,637.7	870,981.1	850,181.7	851,730.8	850,181.7	854,735.5	849,569.3	851,056.2
Commercial paper	71,762.2	41,647.0	23,233.6	27,299.7	23,233.6	24,274.6	22,123.1	21,667.1
Bonds and debentures	122,001.9	150,886.3	146,077.7	144,437.2	146,077.7	139,744.8	136,241.1	133,151.7
Mortgage covered bonds	162,465.5	185,343.8	195,734.8	189,145.7	195,734.8	202,528.8	219,313.8	222,488.8
Territorial covered bonds	17,030.0	16,030.0	18,350.0	18,650.0	18,350.0	20,485.0	20,285.0	24,149.2
Backed securities	422,010.7	442,831.5	434,835.1	440,244.9	434,835.1	435,551.9	419,458.0	417,451.1
Preference shares	23,308.6	33,183.8	30,891.8	30,894.5	30,891.8	31,091.8	31,089.6	31,089.6
Matador bonds	1,058.8	1,058.8	1,058.8	1,058.8	1,058.8	1,058.8	1,058.8	1,058.8

1 Available data: August 2011.

2 Nominal amount.

AIAF. Trading

TABLE 1.11

Nominal amount in million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
BY TYPE OF ASSET								
Total	2,521,040.1	4,658,633.2	4,383,118.7	1,088,985.4	1,811,416.3	2,540,940.4	1,618,996.9	1,203,982.8
Commercial paper	591,943.8	533,331.0	385,238.9	92,307.2	72,604.4	67,260.3	57,492.7	30,998.6
Bonds and debentures	80,573.8	321,743.0	922,393.1	192,302.0	349,527.2	241,674.3	96,130.6	64,047.4
Mortgage covered bonds	129,995.3	263,150.0	271,441.8	86,114.0	96,608.6	169,889.3	115,484.5	69,918.8
Territorial covered bonds	10,142.3	7,209.0	14,458.2	3,213.7	1,924.7	32,764.3	43,117.1	51,669.9
Backed securities	1,704,341.8	3,527,486.4	2,784,775.4	714,081.4	1,289,446.1	2,028,138.1	1,303,425.0	986,470.7
Preference shares	4,030.0	5,668.5	4,635.7	966.9	1,273.8	1,178.3	3,337.6	842.1
Matador bonds	13.2	45.2	175.7	0.2	31.6	35.9	9.5	35.4
BY TYPE OF TRANSACTION								
Total	2,521,040.1	4,658,633.2	4,383,118.7	1,088,985.4	1,811,416.3	2,540,940.4	1,618,996.9	1,203,982.8
Outright	387,897.1	378,348.4	288,927.3	55,230.8	69,161.4	100,126.8	78,598.4	35,316.5
Repos	381,505.0	362,068.7	304,493.2	72,123.5	61,165.8	55,980.9	51,485.2	30,796.6
Sell-buybacks/Buy-sellbacks	1,751,638.0	3,918,216.1	3,789,698.3	961,631.2	1,681,089.0	2,384,832.7	1,488,913.3	1,137,869.7

1 Available data: August 2011.

AIAF. Third-party trading. By purchaser sector

TABLE 1.12

Nominal amount in million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Total	744,652.5	681,946.6	553,896.6	121,757.2	120,800.2	136,405.9	120,560.2	62,055.2
Non-financial companies	285,044.4	256,224.6	162,949.5	37,846.5	33,281.8	36,362.7	37,287.8	21,335.9
Financial institutions	334,851.6	298,909.1	289,950.4	68,828.4	67,718.0	67,797.2	55,419.8	29,935.0
Credit institutions	130,056.0	125,547.5	102,372.1	21,916.4	29,970.9	34,359.6	27,624.9	13,393.8
IICs ² , insurance and pension funds	154,709.8	115,865.3	125,899.4	31,339.1	22,618.2	24,511.6	25,796.8	15,969.7
Other financial institutions	50,085.8	57,496.3	61,678.9	15,572.8	15,128.9	8,926.0	1,998.1	571.4
General government	6,331.2	5,808.5	3,117.7	160.5	309.8	295.8	392.8	470.5
Households and NPISHs ³	13,344.0	14,647.8	14,244.4	2,234.1	2,541.9	1,866.8	2,817.3	1,242.0
Rest of the world	105,081.2	106,356.6	83,634.6	12,687.8	16,948.7	30,083.5	24,642.5	9,071.8

1 Available data: August 2011.

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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
NOMINAL AMOUNTS (million euro)								
Total	3,390.6	5,866.8	868.0	0.0	468.0	500.0	681.6	1,500.0
Non-convertible bonds and debentures	0.0	0.0	400.0	0.0	0.0	0.0	0.0	0.0
Convertible bonds and debentures	0.0	4,510.8	468.0	0.0	468.0	500.0	681.6	1,500.0
Backed securities	3,390.6	1,356.0	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	33	10	8	0	1	1	4	1
Non-convertible bonds and debentures	0	0	7	0	0	0	0	0
Convertible bonds and debentures	0	4	1	0	1	1	4	1
Backed securities	33	6	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: August 2011.

Equity markets. Issuers, issues and outstanding balances

TABLE 1.14

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
NO. OF ISSUERS								
Total	58	62	60	62	60	57	59	59
Private issuers	45	48	46	48	46	44	46	46
Non-financial companies	5	6	5	5	5	4	4	4
Financial institutions	40	42	41	43	41	40	42	42
General government ²	13	14	14	14	14	13	13	13
Regional governments	3	3	3	3	3	3	3	3
NO. OF ISSUES								
Total	271	269	247	257	247	237	245	244
Private issuers	157	155	145	150	145	137	137	136
Non-financial companies	9	10	7	8	7	7	7	7
Financial institutions	148	145	138	142	138	130	130	129
General government ²	114	114	102	107	102	100	108	108
Regional governments	82	76	64	68	64	63	72	73
OUTSTANDING BALANCES³ (million euro)								
Total	29,142.6	36,299.5	41,091.3	36,480.1	41,091.3	41,497.4	45,280.8	44,190.2
Private issuers	17,237.9	21,600.9	19,261.5	19,110.1	19,261.5	19,301.5	19,017.9	18,309.6
Non-financial companies	381.0	1,783.7	376.6	377.1	376.6	375.8	375.8	375.8
Financial institutions	16,856.9	19,817.2	18,884.8	18,733.0	18,884.8	18,925.7	18,642.1	17,933.8
General government ²	11,904.7	14,698.6	21,829.9	17,370.0	21,829.9	22,195.9	26,262.9	25,880.6
Regional governments	9,972.5	12,338.3	19,442.4	14,961.8	19,442.4	19,812.5	23,992.9	23,710.6

1 Available data: August 2011.

2 Without public book-entry debt.

3 Nominal amount.

Trading on equity markets

TABLE 1.15

Nominal amounts in million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Electronic market	1,580.1	633.0	510.5	97.1	122.5	81.5	100.5	50.4
Open outcry	7,842.1	4,008.4	7,525.6	1,117.8	4,674.4	2,413.6	582.7	405.3
Madrid	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Barcelona	7,674.9	3,821.1	7,146.7	1,051.6	4,620.6	2,379.4	578.6	398.2
Bilbao	6.1	4.6	2.3	0.4	0.5	0.2	0.1	0.1
Valencia	161.1	182.7	376.6	65.8	53.4	34.0	3.9	7.0
Public book-entry debt	46.2	49.1	331.1	6.3	9.1	4.4	187.8	274.2
Regional governments debt	71,054.9	70,065.8	59,017.0	13,613.0	13,336.2	11,806.8	16,842.8	9,660.9

1 Available data: August 2011.

Organised trading systems: SENAF y MTS. Public debt trading by type

TABLE 1.16

Nominal amounts in million euro	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Total	132,327.4	202,120.5	265,966.0	75,677.6	41,660.2	27,593.2	28,318.9	10,154.0
Outright	89,010.5	114,314.0	110,011.0	16,173.0	21,116.0	27,293.0	26,482.0	10,154.0
Sell-buybacks/Buy-sellbacks	43,316.9	86,806.5	155,433.0	59,504.6	20,394.2	300.2	1,836.9	0.0
Others	0.0	1,000.0	522.0	0.0	150.0	0.0	0.0	0.0

1 Available data: August 2011.

1.3 Derivatives and other products

1.3.1 Financial derivatives markets: MEFF

Trading on MEFF

TABLE 1.17

Number of contracts	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Debt products	12	18	14	4	2	6	4	0
Debt futures ²	12	18	14	4	2	6	4	0
Ibex 35 products ^{3,4}	8,433,963	6,187,544	6,946,167	1,446,089	1,585,302	1,714,038	1,403,188	1,172,177
Ibex 35 plus futures	7,275,299	5,436,989	6,280,999	1,327,272	1,432,956	1,575,272	1,280,699	1,065,471
Ibex 35 mini futures	330,042	314,829	357,926	69,900	72,265	90,048	72,265	68,769
Call mini options	323,874	230,349	122,158	21,602	30,717	17,606	19,733	16,328
Put mini options	504,749	205,377	185,083	27,315	49,364	31,111	30,491	21,609
Stock products ⁵	64,554,817	80,114,693	57,291,482	13,107,040	17,395,281	16,374,082	10,805,253	3,114,196
Futures	46,237,568	44,586,779	19,684,108	4,969,808	6,650,855	8,006,039	5,337,121	1,348,379
Call options	7,809,423	18,864,840	17,186,515	4,413,718	4,250,315	3,761,646	2,026,429	722,555
Put options	10,507,826	16,663,074	20,420,859	3,723,514	6,494,111	4,606,397	3,441,703	1,043,262
Pro-memoria: MEFF trading on Eurex								
Debt products ⁶	869,105	558,848	373,113	59,521	71,884	90,405	75,174	32,834
Index products ⁷	1,169,059	835,159	604,029	101,741	124,415	106,551	96,795	76,837

1 Available data: August 2011.

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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
WARRANTS²								
Premium amount (million euro)	12,234.4	5,165.1	4,915.3	761.4	1,227.4	1,174.6	891.4	1,414.9
On stocks	6,914.1	2,607.1	2,537.4	302.5	705.7	666.8	462.2	754.3
On indexes	4,542.8	2,000.1	1,852.6	367.3	380.8	387.8	293.9	480.9
Other underlyings ³	777.5	558.0	525.4	91.6	140.9	120.0	135.2	179.7
Number of issues	9,790	7,342	8,375	1,260	2,534	1,946	1,842	2,182
Number of issuers	8	9	9	6	7	7	6	6
OPTION BUYING AND SELLING CONTRACTS								
Nominal amounts (million euro)	77.0	35.0	64.0	20.0	7.0	0.0	0.0	0.0
On stocks	77.0	25.0	47.0	10.0	7.0	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	0.0	10.0	17.0	10.0	0.0	0.0	0.0	0.0
Number of issues	4	3	7	2	1	0	0	0
Number of issuers	1	1	1	1	1	0	0	0

1 Available data: August 2011.

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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
WARRANTS								
Trading (million euro)	2,943.7	1,768.4	1,603.2	397.9	366.2	466.4	286.0	303.0
On Spanish stocks	1,581.9	809.9	759.8	198.0	181.1	212.5	129.8	114.7
On foreign stocks	145.7	97.6	60.7	8.4	17.2	23.7	15.3	15.6
On indexes	1,063.3	761.2	689.5	169.2	130.8	157.1	75.3	97.8
Other underlyings ²	152.8	99.7	93.2	22.4	37.1	73.1	65.6	75
Number of issues ³	9,770	8,038	7,750	3,007	3,060	2,746	3,038	2,822
Number of issuers ³	10	10	10	9	10	9	9	9
CERTIFICATES								
Trading (million euro)	16.8	39.2	22	7.8	3.7	4.1	9.3	24.6
Number of issues ³	26	22	16	13	13	11	10	7
Number of issuers ³	4	4	2	2	2	2	2	2
ETF								
Trading (million euro)	6,938.1	3,470.6	6,229.7	746.4	831.3	1,081.7	571.1	787.9
Number of funds	30	32	65	43	65	67	67	67
Assets ⁴ (million euro)	1,630.3	1,648.4	827.8	960.2	827.8	859.4	867.3	n.a.

1 Available data: August 2011.

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 ETF 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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
Number of contracts								
On olive oil								
Extra-virgin olive oil futures ³	48,091	135,705	165,840	41,555	25,050	23,120	16,401	5,151

1 Olive oil futures market.

2 Available data: August 2011.

3 Nominal amount of the contract: 1,000 kg.

2 Investment services

Investment services. Spanish firms, branches and agents

TABLE 2.1

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
BROKER-DEALERS								
Spanish firms	51	50	50	51	50	50	50	50
Branches	79	78	80	79	80	80	79	76
Agents	6,041	6,102	6,455	6,387	6,455	6,560	6,518	6,545
BROKERS								
Spanish firms	50	50	47	47	47	45	45	45
Branches	9	9	10	8	10	13	13	12
Agents	639	638	665	660	665	689	652	652
PORTFOLIO MANAGEMENT COMPANIES								
Spanish firms	10	9	7	8	7	6	6	6
Branches	4	5	5	5	5	5	5	5
Agents	6	5	3	4	3	2	2	3
FINANCIAL ADVISORY FIRMS²								
Spanish firms	–	16	48	42	48	58	64	73
CREDIT INSTITUTIONS³								
Spanish firms	195	193	186	189	186	186	189	191

1 Available data: August 2011.

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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Total	2,232	2,346	2,604	2,563	2,604	2,671	2,743	2,784
European Economic Area investment services firms	1,818	1,940	2,176	2,129	2,176	2,238	2,303	2,344
Branches	37	36	41	40	41	40	40	40
Free provision of services	1,781	1,904	2,135	2,089	2,135	2,198	2,263	2,304
Credit institutions ²	414	424	428	434	428	433	440	440
From EU member states	405	414	418	424	418	423	430	430
Branches	56	53	53	56	53	55	56	55
Free provision of services	348	360	364	367	364	368	374	375
Subsidiaries of free provision of services institutions	1	1	1	1	1	0	0	0
From non-EU states	9	10	10	10	10	10	10	10
Branches	8	8	8	8	8	8	8	8
Free provision of services	1	2	2	2	2	2	2	2

1 Available data: August 2011.

2 Source: Banco de España and CNMV.

Intermediation of spot transactions¹

TABLE 2.3

Million euro	II 2010				II 2011			
	Spanish organised markets	Other Spanish markets	Foreign markets	Total	Spanish organised markets	Other Spanish markets	Foreign markets	Total
FIXED-INCOME								
Total	776,688	2,687,669	124,424	3,588,781	777,958	2,414,999	216,945	3,409,902
Broker-dealers	146,195	811,964	42,032	1,000,191	111,850	675,987	170,888	958,725
Brokers	630,493	1,875,705	82,392	2,588,590	666,108	1,739,012	46,057	2,451,177
EQUITY								
Total	298,855	1,310	27,329	327,494	237,168	965	19,442	257,575
Broker-dealers	293,039	1,119	26,120	320,278	232,609	817	18,235	251,661
Brokers	5,816	191	1,209	7,216	4,559	148	1,207	5,914

1 Period accumulated data. Quarterly.

Intermediation of derivative transactions^{1,2}

TABLE 2.4

Million euro	II 2010				II 2011			
	Spanish organised markets	Foreign organised markets	Non-organised markets	Total	Spanish organised markets	Foreign organised markets	Non-organised markets	Total
Total	1,263,917	2,501,023	786,422	4,551,362	806,521	2,634,116	152,643	3,593,280
Broker-dealers	1,255,305	2,056,111	636,811	3,948,227	804,187	1,474,841	90,058	2,369,086
Brokers	8,612	444,912	149,611	603,135	2,334	1,159,275	62,585	1,224,194

- 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

	II 2010			II 2011			
	IIC ²	Other ³	Total	IIC ²	Other ³	Total	
NUMBER OF PORTFOLIOS							
Total		159	13,100	13,259	134	14,128	14,262
Broker-dealers		85	7,555	7,640	87	7,032	7,119
Brokers		51	3,231	3,282	42	3,661	3,703
Portfolio management companies		23	2,314	2,337	5	3,435	3,440
ASSETS UNDER MANAGEMENT (thousand euro)							
Total		2,122,271	7,938,523	10,060,795	1,693,067	7,967,760	9,660,829
Broker-dealers		909,965	3,217,426	4,127,391	957,375	3,276,545	4,233,922
Brokers		1,039,573	1,342,372	2,381,946	627,525	1,651,721	2,279,246
Portfolio management companies		172,733	3,378,725	3,551,458	108,167	3,039,494	3,147,661

- 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

	II 2010			II 2011		
	Retail clients	Professional clients	Total ²	Retail clients	Professional clients	Total ²
NUMBER OF CONTRACTS						
Total	5,088	71	5,163	7,400	102	7,519
Broker-dealers	1,203	5	1,211	1,485	2	1,492
Brokers	3,153	55	3,209	4,773	93	4,878
Portfolio management companies	732	11	743	1,142	7	1,149
ASSETS ADVISED (thousand euro)						
Total	2,179,095	4,160,382	6,720,000	3,011,362	4,436,334	7,924,222
Broker-dealers	537,441	220,779	1,138,712	514,319	35,050	951,344
Brokers	1,273,260	862,871	2,136,162	1,953,461	995,592	3,023,604
Portfolio management companies	368,394	3,076,732	3,445,126	543,582	3,405,692	3,949,274

- 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	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
I. Interest income	109,682	163,272	102,054	79,231	102,054	15,186	52,973	72,762
II. Net commission	674,204	562,082	533,858	391,165	533,858	157,082	275,520	309,994
Commission revenues	943,619	782,214	798,152	593,521	798,152	231,177	419,375	477,001
Brokering	648,036	548,362	555,207	420,088	555,207	166,934	285,047	320,745
Placement and underwriting	42,502	26,326	8,499	4,314	8,499	1,057	2,830	3,279
Securities deposit and recording	21,198	16,183	22,367	16,775	22,367	5,465	10,887	12,565
Portfolio management	17,306	11,768	13,880	10,044	13,880	4,180	7,911	9,204
Design and advising	56,671	60,477	53,722	38,344	53,722	16,802	39,550	43,337
Stocks search and placement	12	10	36	36	36	179	184	334
Market credit transactions	19	14	9	8	9	2	4	5
IICs ³ marketing	91,167	63,341	65,487	48,242	65,487	16,053	31,359	36,352
Other	66,708	55,733	78,944	55,672	78,944	20,503	41,601	51,180
Commission expenses	269,415	220,133	264,294	202,356	264,294	74,095	143,855	167,007
III. Financial investment income	800,194	45,266	48,588	9,841	48,588	28,085	38,782	9,846
IV. Net exchange differences and other operating products and expenses	-626,527	21,820	26,081	39,867	26,081	2,089	-5,173	13,619
V. Gross income	957,553	792,440	710,580	520,104	710,580	202,442	362,102	406,221
VI. Operating income	434,209	339,706	276,253	197,788	276,253	88,668	142,774	150,280
VII. Earnings from continuous activities	365,374	250,984	196,834	173,280	196,834	73,044	121,402	127,599
VIII. Net earnings of the period	367,665	250,984	196,834	173,280	196,834	73,044	121,402	127,599

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: July 2011.

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	
	II 2010	II 2011	II 2010	II 2011	II 2010	II 2011	II 2010	II 2011
	Total	43,915	52,973	76,990	38,783	-33,338	-6,521	87,568
Money market assets and public debt	2,376	967	4,080	5,670	-	-	6,456	6,637
Other fixed-income securities	9,514	13,963	34,660	14,860	-	-	44,174	28,823
Domestic portfolio	8,737	12,437	31,708	10,599	-	-	40,445	23,036
Foreign portfolio	777	1,526	2,952	4,261	-	-	3,729	5,786
Equities	34,049	30,269	-53,586	-128,191	-	-	-19,537	-97,922
Domestic portfolio	24,238	20,501	-81,483	35,292	-	-	-57,245	55,793
Foreign portfolio	9,811	9,768	27,898	-163,483	-	-	37,709	-153,716
Derivatives	-	-	64,524	140,562	-	-	64,524	140,562
Repurchase agreements	-1,115	346	-	-	-	-	-1,115	346
Market credit transactions	0	0	-	-	-	-	0	0
Deposits and other transactions with financial intermediaries	-1,222	8,379	-	-	-	-	-1,222	8,379
Net exchange differences	-	-	-	-	-38,210	-5,344	-38,210	-5,344
Other operating products and expenses	-	-	-	-	1,437	170	1,437	170
Other transactions	313	-951	27,312	5,881	3,435	-1,347	31,061	3,583

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	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
I. Interest income	7,980	2,652	1,629	1,099	1,629	351	1,144	1,263
II. Net commission	149,874	127,410	109,165	80,234	109,165	26,048	50,423	58,226
Commission revenues	172,344	144,373	126,055	92,624	126,055	29,798	57,899	67,159
Brokering	62,345	53,988	38,176	29,565	38,176	10,080	19,345	22,250
Placement and underwriting	4,847	2,989	2,748	1,368	2,748	350	1,181	1,360
Securities deposit and recording	676	509	366	276	366	97	191	225
Portfolio management	21,137	19,633	19,489	13,861	19,489	3,818	6,760	7,747
Design and advising	4,962	2,806	3,618	1,972	3,618	1,147	2,634	3,211
Stocks search and placement	0	0	304	128	304	174	538	616
Market credit transactions	10	28	27	26	27	10	13	14
IICs ³ marketing	31,287	23,966	23,946	17,611	23,946	5,828	11,097	12,777
Other	47,081	40,453	37,381	27,816	37,381	8,294	16,141	18,959
Commission expenses	22,470	16,963	16,890	12,390	16,890	3,750	7,476	8,933
III. Financial investment income	-1,176	1,709	456	23	456	151	-54	-10
IV. Net exchange differences and other operating products and expenses	3,526	-1,111	-1,416	-955	-1,416	-455	-1,306	-1,354
V. Gross income	160,204	130,661	109,834	80,400	109,834	26,095	50,207	58,125
VI. Operating income	20,377	9,090	9,457	6,330	9,457	3,444	5,568	6,199
VII. Earnings from continuous activities	14,372	4,862	6,452	5,700	6,452	3,298	5,289	5,830
VIII. Net earnings of the period	14,372	4,862	6,452	5,700	6,452	3,298	5,289	5,830

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: July 2011.

3 IIC: Instituciones de Inversión Colectiva / CIS: Collective Investment Schemes.

Aggregated income statement. Portfolio management companies

TABLE 2.10

Thousand euro ¹	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
I. Interest income	1,482	341	407	274	407	154	293	359
II. Net commission	12,044	10,734	10,097	8,393	10,097	1,897	3,840	4,466
Commission revenues	23,877	21,750	20,994	16,559	20,994	4,531	9,123	10,641
Portfolio management	20,683	18,463	18,020	13,645	18,020	4,224	8,323	9,689
Design and advising	2,484	2,698	1,160	1,101	1,160	307	800	952
IICs ³ marketing	66	18	34	34	34	0	0	0
Other	644	571	1,779	1,779	1,779	0	0	0
Commission expenses	11,833	11,016	10,897	8,167	10,897	2,634	5,283	6,175
III. Financial investment income	-108	92	51	96	51	243	233	217
IV. Net exchange differences and other operating products and expenses	-418	-383	21	-265	21	13	-19	-20
V. Gross income	13,000	10,784	10,577	8,497	10,577	2,307	4,347	5,022
VI. Operating income	1,157	1,296	1,154	1,189	1,154	415	677	739
VII. Earnings from continuous activities	765	889	939	1,009	939	304	490	534
VIII. Net earnings of the period	765	889	939	1,009	939	304	490	534

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: July 2011.

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	1,527,805	366.38	9	18	12	8	15	9	7	12	5	6
Broker-dealers	1,441,784	393.82	3	5	1	2	12	7	6	7	4	3
Brokers	69,503	198.11	5	11	11	5	3	1	1	5	1	2
Portfolio management companies	16,518	104.43	1	2	0	1	0	1	0	0	0	1

1 Available data: June 2011.

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

Thousand euro	Average ³	Losses	Number of companies according to its annualised return								
			0-5%	6-15%	16-30%	31-45%	46-60%	61-75%	76-100%	> 100%	
Total	14.99	30	18	25	11	6	4	1	1	5	
Broker-dealers	15.40	13	11	11	9	2	1	0	0	3	
Brokers	10.66	16	5	12	2	3	3	1	1	2	
Portfolio management companies	4.19	1	2	2	0	1	0	0	0	0	

1 ROE has been calculated as:

$$ROE = \frac{\text{Profit before taxes (annualised)}}{\text{Equity}}$$

Own_Funds = Share capital + Paid-in surplus + Reserves – Own shares + Prior year profits and retained earnings – Interim dividend.

2 Available data: June 2011.

3 Average weighted by equity, %.

Financial advisory firms. Main figures

TABLE 2.13

Thousand euro	2008	2009	2010	2009		2010		2011	
				II	I	I	II	I	II
ASSETS ADVISED¹									
Total	–	1,410,985	16,120,751	1,410,985	11,929,643	16,120,751	16,968,190		
Retail clients	–	364,284	1,707,278	364,284	1,164,130	1,707,278	2,090,669		
Professional	–	1,046,702	14,321,020	1,046,702	10,746,313	14,321,020	14,786,650		
Other	–	0	92,453	0	19,200	92,453	90,871		
COMMISSION INCOME²									
Total	–	3,183	21,863	3,183	7,783	21,863	14,113		
Commission revenues	–	3,183	21,747	3,183	7,726	21,747	14,077		
Other income	–	0	116	0	57	116	36		
EQUITY									
Total	–	1,500	10,224	1,500	9,312	10,224	10,363		
Share capital	–	1,043	3,014	1,043	2,379	3,014	3,386		
Reserves and retained earnings	–	36	384	36	3,333	384	2,808		
Income for the year ²	–	421	6,826	421	3,600	6,826	4,169		

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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ¹
Total financial IICs	6,354	5,892	5,627	5,679	5,627	5,603	5,551	5,498
Mutual funds	2,943	2,593	2,429	2,443	2,429	2,436	2,410	2,370
Investment companies	3,347	3,232	3,133	3,171	3,133	3,105	3,077	3,064
Funds of hedge funds	40	38	32	33	32	29	28	28
Hedge funds	24	29	33	33	33	33	36	36
Total real estate IICs	18	16	16	16	16	16	16	15
Real estate investment funds	9	8	8	8	8	8	8	7
Real estate investment companies	9	8	8	8	8	8	8	8
Total foreign IICs marketed in Spain	563	582	660	652	660	669	695	697
Foreign funds marketed in Spain	312	324	379	376	379	383	395	395
Foreign companies marketed in Spain	251	258	281	276	281	286	300	302
IIC Management companies	120	120	123	123	123	120	118	117
IIC Depositories	125	124	114	117	114	113	107	102

1 Available data: August 2011.

Number of IICs investors and shareholders

TABLE 3.2

	2008	2009	2010 ¹	2010		2011		
				II	III	IV	I	II ¹
Total financial IICs	6,358,753	5,895,009	5,578,524	5,841,721	5,765,250	5,578,524	5,575,859	5,460,738
Mutual funds	5,923,352	5,475,403	5,160,889	5,423,206	5,348,536	5,160,889	5,160,482	5,044,106
Investment companies	435,401	419,606	417,635	419,307	416,714	417,635	415,377	416,632
Total real estate IICs	98,327	84,511	76,223	77,714	77,116	76,223	34,690	32,906
Real estate investment funds	97,390	83,583	75,280	76,772	76,182	75,280	33,747	31,963
Real estate investment companies	937	928	943	942	934	943	943	943
Total foreign IICs marketed in Spain ²	593,488	685,094	865,767	791,381	811,553	865,767	855,877	856,882
Foreign funds marketed in Spain	102,922	139,102	193,233	181,039	186,804	193,233	197,965	195,525
Foreign companies marketed in Spain	490,566	545,992	666,534	610,342	624,749	666,534	657,912	661,357

1 Provisional data for foreign IICs.

2 Exchange traded funds (ETFs) data is not included.

IICs total net assets

TABLE 3.3

Million euro	2008	2009	2010 ¹	2010		2011		
				II	III	IV	I	II ¹
Total financial IICs	200,522.4	196,472.5	170,073.1	180,899.1	178,778.0	170,073.1	170,409.6	166,446.6
Mutual funds ²	175,865.5	170,547.7	143,918.2	155,295.5	152,646.5	143,918.2	144,428.0	140,351.3
Investment companies	24,656.9	25,924.8	26,155.0	25,602.6	26,131.5	26,155.0	26,491.4	26,095.4
Total real estate IICs	7,778.8	6,773.7	6,437.5	6,606.6	6,524.2	6,437.5	6,403.6	6,313.7
Real estate investment funds	7,406.9	6,465.1	6,115.6	6,279.6	6,201.5	6,115.6	6,083.3	5,995.5
Real estate investment companies	371.9	308.6	321.9	327.0	322.7	321.9	320.3	318.2
Total foreign IICs marketed in Spain ³	18,254.8	25,207.2	36,692.9	32,362.8	32,826.7	36,692.9	37,636.4	35,582.2
Foreign funds marketed in Spain	3,352.0	5,215.1	8,535.9	7,477.2	7,650.1	8,535.9	8,092.4	7,303.2
Foreign companies marketed in Spain	14,902.8	19,992.0	28,156.9	24,885.7	25,176.6	28,156.9	29,544.0	28,279.0

1 Provisional data for foreign IICs.

2 For June 2011, mutual funds investments in financial IICs reached 6.2 billion euro.

3 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	2008	2009	2010	2010			2011	
				II	III	IV	I	II ²
Asset	175,865.5	170,547.7	143,918.1	155,295.5	152,646.5	143,918.2	144,428.0	140,351.3
Portfolio investment	166,384.7	163,165.5	137,295.4	148,166.2	144,724.4	137,296.1	137,441.4	133,666.7
Domestic securities	107,347.7	100,642.6	89,630.2	92,605.7	91,413.1	89,632.4	92,205.1	91,324.1
Debt securities	81,904.6	74,628.9	68,575.1	69,173.9	68,366.9	68,574.5	71,784.6	70,905.2
Shares	4,023.2	4,741.0	3,829.2	3,611.2	3,994.8	3,829.2	3,990.3	3,944.8
Investment collective schemes	10,134.3	9,041.5	7,338.6	8,876.9	8,415.2	7,338.6	6,338.7	6,387.3
Deposits in Credit institutions	10,657.6	11,552.2	9,460.8	10,508.4	10,167.6	9,460.8	9,634.7	9,665.8
Derivatives	627.9	679.0	426.2	435.3	467.6	429.0	456.5	420.9
Other	0.1	0.0	0.4	0.0	1.0	0.4	0.3	0.0
Foreign securities	59,035.2	62,487.1	47,626.5	55,515.6	53,272.4	47,625.1	45,198.9	42,329.6
Debt securities	49,659.8	48,435.3	30,337.4	39,619.4	36,499.7	30,337.4	26,875.7	24,575.4
Shares	5,216.1	7,783.2	8,385.8	7,615.6	8,003.2	8,386.4	8,604.6	8,758.1
Investment collective schemes	3,524.5	5,666.4	8,404.7	7,844.9	8,264.9	8,404.7	9,252.1	8,548.4
Deposits in Credit institutions	17.5	82.4	108.0	81.5	73.1	108.0	86.7	61.2
Derivatives	599.5	518.7	387.1	349.2	427.4	385.1	376.5	384.2
Other	17.8	1.1	3.6	5.0	4.1	3.6	3.3	2.4
Doubtful assets and matured investment	1.8	35.8	38.6	44.9	38.9	38.6	37.4	12.2
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	8,703.2	7,267.7	6,531.4	6,817.4	7,933.3	6,531.3	6,876.8	6,459.0
Net balance (Debtors - Creditors)	777.7	114.5	91.4	311.9	-11.2	90.7	109.8	225.5

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	2008	2009	2010	2010			2011	
				II	III	IV	I	II ¹
Asset	24,656.9	25,924.8	26,155.0	25,602.6	26,131.5	26,155.0	26,491.4	26,095.4
Portfolio investment	23,446.9	24,813.5	25,187.3	24,471.5	25,015.5	25,187.1	25,262.0	24,915.3
Domestic securities	16,176.3	13,514.3	12,881.4	12,390.0	13,035.9	12,880.2	12,864.2	12,848.4
Debt securities	10,435.1	7,400.5	5,435.9	5,840.4	5,717.5	5,435.9	5,870.6	6,628.9
Shares	3,214.9	3,376.3	2,988.6	2,754.0	2,945.3	2,989.5	3,033.8	2,993.4
Investment collective schemes	1,108.8	1,091.1	758.7	831.9	806.5	756.5	801.9	816.0
Deposits in Credit institutions	1,383.5	1,631.5	3,675.2	2,963.0	3,546.8	3,675.2	3,133.2	2,381.5
Derivatives	9.8	-6.6	-5.9	-22.4	-5.8	-5.9	-4.9	-2.1
Other	24.4	21.7	29.0	23.1	25.7	29.0	29.6	30.6
Foreign securities	7,267.8	11,294.2	12,298.1	12,075.1	11,971.9	12,300.0	12,390.9	12,060.7
Debt securities	2,609.6	4,606.6	3,606.8	4,340.4	4,001.8	3,606.8	3,407.6	3,241.5
Shares	2,014.6	3,559.3	4,166.0	3,793.3	3,852.6	4,166.0	4,381.9	4,264.5
Investment collective schemes	2,486.4	2,987.4	4,390.5	3,807.1	3,933.9	4,392.6	4,415.0	4,349.0
Deposits in Credit institutions	28.9	26.3	12.1	18.0	44.5	12.1	47.1	45.4
Derivatives	120.5	113.0	119.9	108.3	134.9	119.7	135.1	157.8
Other	7.8	1.6	2.8	8.0	4.3	2.8	4.2	2.4
Doubtful assets and matured investment	2.8	4.9	7.9	6.4	7.7	6.9	6.9	6.3
Intangible assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net fixed assets	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Cash	1,021.0	976.4	832.0	896.0	903.3	832.1	1,014.6	946.9
Net balance (Debtors - Creditors)	188.8	134.8	135.5	235.0	212.6	135.6	214.6	233.0

1 Provisional data.

Financial mutual funds: Number, investors and total net assets by category¹

TABLE 3.6

	2008	2009	2010	2010			2011	
				II	III	IV	I	II
NO. OF FUNDS								
Total financial mutual funds	2,912	2,536	2,408	2,436	2,421	2,408	2,417	2,389
Fixed-income ²	629	582	537	547	540	537	543	530
Mixed fixed-income ³	195	169	160	168	162	160	158	152
Mixed equity ⁴	202	165	138	143	140	138	136	132
Euro equity ⁵	237	182	172	179	174	172	171	157
Foreign equity ⁶	330	242	232	233	233	232	222	222
Guaranteed fixed-income	260	233	276	251	261	276	303	324
Guaranteed equity ⁷	590	561	499	530	518	499	485	470
Global funds	469	187	192	181	189	192	197	203
Passive management ⁸	–	69	61	64	61	61	61	57
Absolute return ⁸	–	146	141	140	143	141	141	142
INVESTORS								
Total financial mutual funds	5,923,346	5,475,403	5,160,889	5,423,206	5,348,536	5,160,889	5,160,482	5,044,106
Fixed-income ²	2,204,652	2,041,487	1,622,664	1,865,575	1,745,375	1,622,664	1,525,292	1,466,938
Mixed fixed-income ³	277,629	290,151	270,341	295,325	280,230	270,341	251,992	238,275
Mixed equity ⁴	209,782	182,542	171,336	185,111	182,860	171,336	162,861	156,631
Euro equity ⁵	377,545	299,353	266,395	280,529	280,573	266,395	253,365	248,355
Foreign equity ⁶	467,691	458,097	501,138	487,813	502,491	501,138	493,052	493,057
Guaranteed fixed-income	538,799	570,963	790,081	690,600	762,369	790,081	967,561	990,997
Guaranteed equity ⁷	1,402,948	1,188,304	1,065,426	1,142,072	1,115,180	1,065,426	1,027,392	981,572
Global funds	444,300	88,337	105,720	99,163	110,538	105,720	114,244	124,088
Passive management ⁸	–	85,403	90,343	97,949	93,049	90,343	85,254	82,371
Absolute return ⁸	–	270,766	277,445	279,069	275,871	277,445	279,469	261,822
TOTAL NET ASSETS (million euro)								
Total financial mutual funds	175,865.2	170,547.7	143,918.2	155,295.5	152,646.5	143,918.2	144,428.0	140,351.3
Fixed-income ²	92,813.1	84,657.2	56,614.6	69,654.5	64,102.1	56,614.6	51,565.6	49,449.9
Mixed fixed-income ³	5,803.0	8,695.5	7,319.0	8,264.2	8,109.9	7,319.0	6,570.0	6,251.9
Mixed equity ⁴	3,958.8	3,879.6	3,470.5	3,441.5	3,520.2	3,470.5	3,484.5	3,345.6
Euro equity ⁵	5,936.9	6,321.6	5,356.8	5,181.2	5,504.4	5,356.8	5,656.3	5,687.2
Foreign equity ⁶	4,256.6	5,902.4	8,037.3	6,682.5	7,203.6	8,037.3	7,896.1	7,751.6
Guaranteed fixed-income	21,281.6	21,033.4	26,180.2	23,520.3	25,795.6	26,180.2	32,084.4	32,742.1
Guaranteed equity ⁷	30,742.4	25,665.8	22,046.5	23,981.7	23,600.0	22,046.5	21,181.6	19,827.6
Global funds	11,072.8	3,872.5	4,440.3	3,991.1	4,093.9	4,440.3	5,481.7	5,718.1
Passive management ⁸	–	3,216.6	2,104.8	2,350.2	2,323.6	2,104.8	2,193.0	2,172.2
Absolute return ⁸	–	7,303.0	8,348.1	8,228.4	8,393.2	8,348.1	8,314.8	7,405.1

1 Mutual funds which have sent reports to the CNMV, excluding those in process of dissolution or liquidation.

2 Until I 2009 this category includes: Short-term fixed income, Long-term fixed income, Foreign fixed-income and Monetary market funds. From II 2009 on includes: Fixed income euro, Foreign fixed-income and Monetary market funds. Until December 2006 it included FIAMM.

3 Until I 2009 this category includes: Mixed fixed-income and Foreign mixed fixed-income. From II 2009 on includes: Mixed euro fixed-income and Foreign mixed fixed-income.

4 Until I 2009 this category includes: Mixed equity and Foreign mixed equity. From II 2009 on includes: Mixed euro equity and Foreign mixed equity.

5 Until I 2009 this category includes: Spanish equity and Euro Equity. From II 2009 on includes: Euro equity (which includes domestic equity).

6 Until I 2009 this category includes: Foreign equity Europe, Foreign equity Japan, Foreign equity USA, Foreign equity emerging countries and Other foreign equity. From II 2009 on includes: Foreign equity.

7 Until I 2009 this category includes: Guaranteed equity. From II 2009 on includes: Guaranteed equity and partial guarantee.

8 New categories from II 2009 on. Before it, absolute return funds were classified as Global funds.

Financial mutual funds: Detail of investors and total net assets by type of investors

TABLE 3.7

	2008	2009	2010	2010			2011	
				II	III	IV	I	II
INVESTORS								
Total financial mutual funds	5,923,352	5,475,403	5,160,889	5,423,206	5,348,536	5,160,889	5,160,482	5,044,106
Individuals	5,754,049	5,322,214	5,019,902	5,272,045	5,201,334	5,019,902	5,020,705	4,907,283
Residents	5,677,123	5,252,126	4,954,891	5,203,616	5,134,719	4,954,891	4,955,440	4,843,565
Non-residents	76,926	70,088	65,011	68,429	66,615	65,011	65,265	63,718
Legal entities	169,303	153,189	140,987	151,161	147,202	140,987	139,777	136,823
Credit institutions	1,713	674	524	582	568	524	500	491
Other resident institutions	166,041	151,479	139,550	149,581	145,690	139,550	138,402	135,505
Non-resident institutions	1,549	1,036	913	998	944	913	875	827
TOTAL NET ASSETS (million euro)								
Total financial mutual funds	175,865.5	170,547.7	143,918.1	155,295.5	152,646.5	143,918.1	144,428.0	140,351.3
Individuals	135,756.2	132,860.5	113,660.6	121,762.4	119,808.3	113,660.6	115,233.0	111,732.9
Residents	133,878.1	130,954.4	111,900.1	119,898.1	117,961.2	111,900.1	113,442.6	110,123.1
Non-residents	1,878.1	1,906.0	1,760.5	1,864.3	1,847.1	1,760.5	1,790.3	1,609.9
Legal entities	40,109.3	37,687.2	30,257.5	33,533.9	32,838.1	30,257.5	29,195.0	28,618.3
Credit institutions	4,193.0	2,572.0	1,926.1	2,145.0	2,152.9	1,926.1	1,869.9	1,854.3
Other resident institutions	34,738.0	34,065.1	27,644.6	30,614.8	29,926.8	27,644.6	26,666.9	26,205.8
Non-resident institutions	1,178.4	1,050.1	686.9	774.1	758.5	686.9	658.2	558.3

Subscriptions and redemptions of financial mutual funds by category¹

TABLE 3.8

Million euro	2008	2009 ²	2010	2010			2011	
				II	III	IV	I	II
SUBSCRIPTIONS								
Total financial mutual funds	135,461.7	109,915.2	78,805.2	24,172.2	13,395.6	16,011.4	22,756.0	13,174.5
Fixed-income	101,909.7	73,718.8	41,656.1	13,605.3	6,206.7	6,603.3	7,890.1	6,478.3
Mixed fixed-income	1,914.5	5,267.6	3,538.8	1,082.2	571.7	641.4	358.0	517.3
Mixed equity	1,350.2	1,135.4	1,221.7	556.5	118.5	254.6	270.4	345.6
Euro equity	2,858.0	2,183.8	1,673.0	464.0	291.1	335.4	575.2	524.1
Foreign equity	3,309.6	2,929.5	4,455.2	1,190.3	778.5	1,227.3	2,488.7	721.4
Guaranteed fixed-income	11,937.0	11,755.4	11,513.4	3,244.1	3,403.9	2,505.8	7,424.2	2,595.3
Guaranteed equity	6,544.7	5,589.1	5,120.1	1,539.4	726.8	1,246.5	828.6	622.0
Global funds	5,638.0	2,754.4	3,018.1	440.6	265.4	1,767.1	1,534.3	838.6
Passive management	–	535.5	683.8	271.1	73.7	96.4	220.5	149.2
Absolute return	–	4,045.7	5,924.8	1,778.8	959.1	1,333.6	1,165.9	382.4
REDEMPTIONS								
Total financial mutual funds	202,864.1	122,617.5	104,385.6	33,041.1	18,442.3	24,577.5	23,528.9	17,269.3
Fixed-income	124,242.9	81,197.6	68,806.1	22,951.2	12,006.3	13,908.1	13,298.5	8,737.2
Mixed fixed-income	8,136.6	2,724.4	4,955.7	1,653.8	812.4	1,383.5	1,138.4	892.1
Mixed equity	4,675.6	1,596.5	1,311.8	601.2	168.0	316.9	267.4	446.3
Euro equity	8,617.2	2,457.8	2,369.9	673.9	452.4	534.0	594.8	453.7
Foreign equity	8,657.3	2,165.3	3,303.3	991.1	625.5	981.8	2,521.1	800.6
Guaranteed fixed-income	9,499.1	15,004.5	6,797.4	1,529.0	1,414.2	1,718.5	2,007.8	2,223.6
Guaranteed equity	18,216.4	10,990.8	7,620.2	1,852.4	1,399.8	2,550.0	1,624.7	1,717.3
Global funds	20,819.0	2,548.6	2,694.4	461.1	382.9	1,581.1	507.0	601.0
Passive management	–	708.0	1,474.1	682.1	141.6	254.2	236.7	108.3
Absolute return	–	3,224.0	5,053.0	1,645.3	1,039.3	1,349.5	1,332.4	1,289.5

1 Estimated data.

2 For Passive Management and Absolute return, data refers to the last three quarters of the year.

Financial mutual funds asset change by category: Net subscriptions/redemptions and return on assets

TABLE 3.9

Million euro	2008	2009 ¹	2010	2010			2011	
				II	III	IV	I	II
NET SUBSCRIPTIONS/REDEMPTIONS								
Total financial mutual funds	-67,402.4	-12,702.3	-25,580.6	-9,124.0	-5,056.0	-8,607.1	-765.2	-4,121.9
Fixed-income	-22,333.2	-7,478.8	-27,149.9	-9,531.5	-5,962.0	-7,266.9	-5,379.3	-2,280.5
Mixed fixed-income	-6,222.1	2,543.2	-1,417.0	-566.2	-302.3	-746.8	-814.4	-323.8
Mixed equity	-3,325.4	-461.1	-90.0	-106.5	-79.4	-75.8	-61.2	-128.4
Euro equity	-5,759.2	-274.0	-696.9	-210.4	-185.9	-206.2	-16.4	59.0
Foreign equity	-5,347.7	764.2	1,152.1	183.9	178.3	255.5	-61.8	-45.7
Guaranteed fixed-income	2,437.9	-3,249.1	4,716.0	1,761.1	2,045.5	712.1	5,631.2	531.1
Guaranteed equity	-11,671.7	-5,401.7	-2,500.1	-376.7	-648.1	-1,238.0	-1,016.9	-1,288.1
Global funds	-15,181.0	205.8	323.6	-8.2	-6.6	266.4	997.6	247.1
Passive management	-	-172.5	-790.3	-387.0	-160.3	-219.6	-11.6	-10.8
Absolute return	-	821.7	871.7	117.4	64.6	-87.7	-52.6	-881.9
RETURN ON ASSETS								
Total financial mutual funds	-11,988.0	8,389.8	135.7	-3,097.1	2,418.2	-115.4	1,280.9	47.2
Fixed-income	1,927.7	1,535.3	64.5	-486.4	409.7	-218.4	330.4	164.9
Mixed fixed-income	-716.8	507.9	-56.4	-194.3	148.0	-44.2	65.4	5.6
Mixed equity	-1,589.0	529.9	-53.4	-227.6	158.1	29.1	75.2	-10.5
Euro equity	-5,172.6	1,477.1	-254.1	-638.6	509.2	59.6	319.2	-26.9
Foreign equity	-4,092.4	1,309.0	877.4	-390.0	342.8	578.2	-79.3	-98.8
Guaranteed fixed-income	597.6	830.5	-170.4	-286.3	229.7	-327.4	273.0	127.2
Guaranteed equity	-1,310.4	1,024.0	-392.8	-438.4	266.4	-315.5	151.9	-65.8
Global funds	-1,632.1	272.2	123.1	-121.9	109.4	80.0	43.8	-10.7
Passive management	-	657.8	-109.7	-205.1	144.7	3.5	81.9	-9.9
Absolute return	-	246.4	107.7	-108.4	100.2	42.6	19.3	-27.9

¹ The data refers to the last three quarters of the year for Passive Management and Absolute return categories.

Financial mutual funds return on assets. Detail by category

TABLE 3.10

% of daily average total net assets	2008	2009 ¹	2010	2010			2011	
				II	III	IV	I	II
MANAGEMENT YIELDS								
Total financial mutual funds	-4.09	6.13	1.09	-1.67	1.82	0.17	0.89	0.27
Fixed-income	2.53	2.69	0.78	-0.47	0.81	-0.18	0.62	0.51
Mixed fixed-income	-5.75	9.34	0.61	-1.94	2.13	-0.25	0.95	0.41
Mixed equity	-23.30	16.44	0.11	-5.96	4.95	1.19	2.16	0.16
Euro equity	-47.02	31.02	-3.05	-10.85	9.84	1.62	5.73	0.15
Foreign equity	-49.55	33.16	14.8	-5.08	5.48	8.11	-0.98	-0.67
Guaranteed fixed-income	3.39	4.10	-0.11	-1.10	1.05	-1.18	0.94	0.44
Guaranteed equity	-1.88	5.08	-0.46	-1.50	1.44	-1.07	0.71	0.01
Global funds	-7.36	10.82	4.15	-2.67	2.97	2.17	0.88	0.13
Passive management	-	-	-2.50	-7.34	6.43	0.41	3.74	-0.21
Absolute return	-	-	2.49	-1.04	1.48	0.8	0.23	-0.07
EXPENSES. MANAGEMENT FEE								
Total financial mutual funds	0.87	0.87	0.91	0.22	0.23	0.24	0.23	0.23
Fixed-income	0.58	0.63	0.65	0.16	0.16	0.16	0.16	0.16
Mixed fixed-income	1.14	1.14	1.20	0.29	0.30	0.30	0.29	0.29
Mixed equity	1.54	1.58	1.65	0.39	0.41	0.41	0.40	0.39
Euro equity	1.60	1.75	1.78	0.43	0.45	0.45	0.44	0.44
Foreign equity	1.69	1.79	1.84	0.42	0.45	0.50	0.44	0.43
Guaranteed fixed-income	0.49	0.65	0.62	0.15	0.16	0.17	0.16	0.18
Guaranteed equity	1.29	1.26	1.24	0.30	0.30	0.31	0.30	0.30
Global funds	1.04	1.08	1.06	0.22	0.27	0.30	0.29	0.27
Passive management	-	-	0.72	0.16	0.18	0.19	0.19	0.18
Absolute return	-	-	1.06	0.25	0.26	0.28	0.29	0.26
EXPENSES. DEPOSITORY FEE								
Total financial mutual funds	0.08	0.09	0.09	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	0.09	0.09	0.10	0.02	0.03	0.03	0.03	0.03
Mixed equity	0.11	0.10	0.12	0.03	0.03	0.03	0.03	0.03
Euro equity	0.10	0.10	0.11	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	0.07	0.02	0.02	0.02	0.02	0.02
Guaranteed equity	0.11	0.11	0.10	0.02	0.02	0.03	0.02	0.02
Global funds	0.09	0.08	0.09	0.02	0.02	0.02	0.02	0.02
Passive management	-	-	0.07	0.02	0.02	0.02	0.02	0.02
Absolute return	-	-	0.08	0.02	0.02	0.02	0.02	0.02

1 Passive management and absolute annual returns are not included because they are new categories from II 2009 on.

Mutual funds quarterly returns. Detail by category

TABLE 3.11

In %	2008	2009 ¹	2010	2010			2011	
				II	III	IV	I	II
Total financial mutual funds	-4.21	5.73	0.35	-1.83	1.64	-0.04	0.95	0.03
Fixed-income	2.06	1.91	0.11	-0.62	0.63	-0.35	0.63	0.33
Mixed fixed-income	-7.14	6.85	-0.54	-2.18	1.82	-0.56	0.9	0.09
Mixed equity	-22.21	16.47	-0.98	-6.00	4.67	0.78	2.23	-0.31
Euro equity	-39.78	32.41	-2.94	-10.66	10.11	1.27	6.11	-0.45
Foreign equity	-41.71	37.28	14.22	-4.97	5.35	8.01	-0.49	-1.15
Guaranteed fixed-income	3.29	3.81	-0.67	-1.24	0.89	-1.28	0.89	0.36
Guaranteed equity	-2.61	3.56	-1.79	-1.91	1.20	-1.45	0.71	-0.48
Global funds	-8.64	10.90	3.22	-2.82	2.80	1.87	0.98	-0.14
Passive management	-	-	-2.36	-7.28	6.32	0.31	3.74	-0.30
Absolute return	-	-	1.53	-1.19	1.17	0.58	0.28	-0.35

1 Passive management and absolute annual returns are not included because they are new categories from II 2009 on.

Hedge funds and funds of hedge funds

TABLE 3.12

	2008	2009	2010	2010			2011	
				II	III	IV	I	II ¹
HEDGE FUNDS								
Investors/shareholders	1,589	1,917	1,852	2,061	1,925	1,852	1,958	1,984
Total net assets (million euro)	539.4	652.0	646.2	674.1	639.3	646.2	693.5	719.0
Subscriptions (million euro)	390.4	248.7	236.6	76.0	21.2	31.0	56.0	24.9
Redemptions (million euro)	258.3	198.3	268.6	99.2	73.2	42.6	20.2	18.9
Net subscriptions/redemptions (million euro)	132.7	50.4	-32.0	-23.2	-52.1	-11.6	35.9	6.0
Return on assets (million euro)	-39.1	62.2	26.3	-25.1	17.4	18.4	11.5	7.7
Returns (%)	-4.82	14.94	5.37	-3.17	2.97	3.11	1.79	1.18
Management yields (%) ²	-2.51	13.76	6.33	-3.25	3.24	3.45	2.38	1.50
Management fee (%) ²	2.50	2.55	1.91	0.35	0.47	0.49	0.48	0.29
Financial expenses (%) ²	0.16	0.11	0.07	0.02	0.02	0.02	0.02	0.02
FUNDS OF HEDGE FUNDS								
Investors/shareholders	8,516	5,321	4,404	5,109	4,901	4,404	4,240	4,181
Total net assets (million euro)	1,021.3	810.2	694.9	738.0	726.8	694.9	667.2	650.3
Subscriptions (million euro)	967.3	302.4	47.9	2.2	13.9	10.4	2.3	-
Redemptions (million euro)	700.9	585.4	184.8	52.8	23.7	57.2	29.9	-
Net subscriptions/redemptions (million euro)	266.4	-283.0	-136.9	-50.6	-9.8	-46.8	-27.6	-
Return on assets (million euro)	-245.7	71.9	21.7	-5.3	-1.3	14.9	-0.1	-
Returns (%)	-17.8	7.85	3.15	-0.61	-0.1	2.13	-0.01	-0.03
Management yields (%) ³	-17.84	11.54	4.38	-0.34	0.14	2.46	0.36	-
Management fee (%) ³	1.63	1.34	1.25	0.30	0.31	0.32	0.31	-
Depository fee (%) ³	0.11	0.11	0.08	0.02	0.02	0.02	0.02	-

1 Available data: May 2011. Return refers to the period March-May.

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

	2008	2009	2010	2010			2011	
				II	III	IV	I	II ²
NUMBER OF PORTFOLIOS								
Mutual funds	2,943	2,593	2,429	2,443	2,429	2,436	2,410	2,381
Investment companies	3,240	3,135	3,068	3,096	3,068	3,059	3,024	3,014
Funds of hedge funds	40	38	32	33	32	29	28	28
Hedge funds	24	28	31	32	32	32	35	35
Real estate investment fund	9	8	8	8	8	8	8	7
Real estate investment companies	9	8	8	8	8	8	8	8
ASSETS UNDER MANAGEMENT (million euro)								
Mutual funds	175,865.5	170,547.7	143,918.2	152,646.5	143,918.2	144,428.0	140,351.3	-
Investment companies	23,656.1	24,952.8	25,361.3	25,307.7	25,361.3	25,835.9	25,399.1	-
Funds of hedge funds ³	1,021.3	810.2	709.2	726.8	694.9	667.2	650.3	-
Hedge funds ³	539.4	652.0	614.5	635.5	643.5	666.3	690.6	-
Real estate investment fund	7,406.9	6,465.1	6,115.6	6,201.5	6,115.6	6,083.3	5,995.5	-
Real estate investment companies	371.9	308.5	321.9	322.7	321.9	320.3	318.2	-

1 From II quarter 2009 on 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: July 2011.

3 Available data for II quarter 2011: May 2011.

Foreign Collective Investment Schemes marketed in Spain¹

TABLE 3.14

	2008	2009	2010 ²	2010			2011	
				II	III	IV	I	II ²
INVESTMENT VOLUME³ (million euro)								
Total	18,254.8	25,207.2	36,692.9	32,362.8	32,826.7	36,692.9	37,636.4	35,582.2
Mutual funds	3,352.0	5,215.1	8,535.9	7,477.2	7,650.1	8,535.9	8,092.4	7,303.2
Investment companies	14,902.8	19,992.0	28,156.9	24,885.7	25,176.6	28,156.9	29,544.0	28,279.0
INVESTORS/SHAREHOLDERS								
Total	593,488	685,094	865,767	791,381	811,553	865,767	855,877	856,882
Mutual funds	102,922	139,102	193,233	181,039	186,804	193,233	197,965	195,525
Investment companies	490,566	545,992	666,534	610,342	624,749	666,534	657,912	661,357
NUMBER OF SCHEMES								
Total	563	582	660	636	652	660	669	695
Mutual funds	312	324	379	365	376	379	383	395
Investment companies	251	258	281	271	276	281	286	300
COUNTRY								
Luxembourg	274	275	290	288	287	290	292	298
France	161	178	225	210	222	225	229	239
Ireland	63	64	75	69	74	75	77	84
Germany	16	17	20	20	20	20	20	21
UK	14	14	16	15	15	16	17	19
The Netherlands	1	1	1	1	1	1	1	1
Austria	28	27	27	27	27	27	27	27
Belgium	5	5	5	5	5	5	5	5
Malta	1	1	1	1	1	1	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

	2008	2009	2010	2010		2011		
				III	IV	I	II	III ²
REAL ESTATE MUTUAL FUNDS								
Number	9	8	7	8	7	7	7	7
Investors	97,390	83,583	75,280	76,182	75,280	33,747	31,963	31,591
Assets (million euro)	7,406.9	6,465.1	6,115.6	6,201.5	6,115.6	6,083.3	5,995.5	5,983.0
Return on assets (%)	0.69	-8.31	-4.74	-1.31	-0.9	-0.66	-0.65	-0.23
REAL ESTATE INVESTMENT COMPANIES								
Number	9	8	8	8	8	8	8	8
Shareholders	937	928	943	934	943	943	943	943
Asset (million euro)	371.9	308.6	321.9	322.7	321.9	320.3	318.2	317.0

1 Real estate investment schemes which have sent reports to the CNMV, excluding those in process of dissolution or liquidation.

2 Available data: July 2011. In this case, return on assets is monthly.

