I Securities markets and their agents: situation and outlook

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1 Executive summary

- Economic activity strengthened in most advanced economies between the end of 2013 and the first months of 2014, while visibly losing pace in a number of emerging markets. In the United States, the Federal Reserve continued to taper its monetary stimulus measures, while the European Central Bank (ECB) stuck with its monetary stance, despite what some analysts saw as a looming deflationary risk. International financial markets were perturbed in the first quarter by the turbulence affecting certain emerging economies, a series of weak indicators in China, and political tensions between Russia and Ukraine.

- Against this backdrop, leading stock indices turned downward after the run-up of the preceding months, to the extent that most ended the first quarter in negative terrain.[1] In debt markets, benchmark yields headed lower in the first three months of 2014.

- Spain's GDP resumed growth in the third quarter of 2013. An analysis of key GDP components reveals a degree of rebalancing between domestic and foreign demand, while recent labour market data suggest that job destruction and rising unemployment may be coming to an end. At the same time, inflation is nearing zero rates on a combination of demand weakness, falling energy prices and the unwinding of the VAT effect. On the fiscal front, public debt closed the year at 93.9% of GDP, while the public deficit remains at challenging levels. Finally, output growth is forecast to stand at around 1% in 2014.

- The programme of financial assistance to the Spanish banking sector – most prominently the transfer of problems assets to the asset management company for assets arising from bank restructuring (SAREB) and a step-up in provisioning requirements for individual entities – concluded satisfactorily in January 2014. The sector nonetheless still faces major challenges, not least a frail economic recovery which is further eroding the quality of system assets. On the upside, improved income statements and lower funding needs have enabled banks to reduce recourse to the Eurosystem.

- The aggregate profits of non-financial listed companies rose by 7.3% in the year to 11.15 billion euros. Retail and service companies were at the forefront of earnings growth, while construction and real estate operators reined in their losses. A decrease in gross debt to 270 billion euros, 10% less than at year-end 2012, nudged these firms' average leverage ratio down from 1.41 to 1.38.

1 The closing date for this report is 14 March.

- In domestic equity markets, the share price rally initiated in mid-2013 was pulled up short in the first quarter of 2014 by the instability of some emerging economies and political tensions between Russia and Ukraine. The Ibex 35, finally, shed 1.1% of its value over the first three months, though small and medium cap indices continued their ascent. Market volatility and liquidity conditions remained generally favourable, while trading volumes expanded 16.6% in contrast to the lethargy of recent years.

- Domestic fixed-income markets have continued to benefit this year from the easing of tensions on Europe's debt markets and the improved prospects for national economies in the shape of falling public and private debt yields and lower credit spreads. The spread between the Spanish and German long-term bond narrowed from 220 basis points (bp) in December 2013 to 180 bp in mid-March. This reduction in the perceived risk of Spanish borrowers, and the public sector in particular, was corroborated by rating agency Moody's decision, at the end of February, to upgrade the sovereign debt from Baa3 to Baa2, in what was the country's first upward revision since the sovereign debt crisis erupted in Europe. Finally, private debt issuance was relatively subdued over the year's opening months in tune with banks' lower funding needs.

- Investment funds grew their combined assets by 26% in 2013 as far as 156.7 billion euros, after five years' relentless decline. Three-quarters of the increase was sourced from net subscriptions, which exceeded 24 billion in the year, and the rest from portfolio returns. Unit-holder numbers, meantime, moved back above the five million mark. Another stand-out was the expanding business of foreign UCITS marketed in Spain, whose assets under management swelled by 44% to 55 billion at the 2013 close. The industry's improved fortunes were also apparent in the 58% increase in UCITS management companies' pre-tax profits and the smaller number of loss-making entities, down from 28 in 2012 to 11 last year.

- Investment firms too did improved business in the year thanks to the stronger performance of key business lines like order processing and execution, UCITS marketing, financial advice and portfolio management. As with the collective investment industry, the comeback came after five years of earnings decline and extended to all key sector variables, with pre-tax profits up four fold (to 217 million euros), the number of loss-making companies down from 31 to 12, and capital adequacy holding well above the regulatory requirement. Investment advisory firms also expanded their business, with assets under advice climbing 19% to 17.6 billion euros. The outlook for the sector is generally fair, though note that investment firms face growing competition from other investment service providers like domestic banks and foreign companies passported to operate in Spain.

- The report includes six exhibits:

  - Exhibit 1 looks at the impact on emerging financial markets of the US' decision to phase out its monetary stimulus.

  - Exhibit 2 summarises the main features of bank asset funds (BAFs), closed asset pools lacking legal personality that number among the SAREB's main instruments for the disinvestment process.

- Exhibit 3 examines the role of the Registro Mercantil in issuing and managing the codes that form part of the legal entity identifier (LEI) endorsed by the G-20 and now being rolled out worldwide.

- Exhibit 4 describes the content of ESMA's guidelines on assessing interoperabilty arrangements between central counterparties, as applied by the CNMV since September 2013.

- Exhibit 5 deals with the entry into force of the rules and obligations contained in Regulation (EU) No. 648/2012 (EMIR).

- Finally, exhibit 6 runs through the main points in ESMA's opinion on investment firm practices in the sale of complex products.

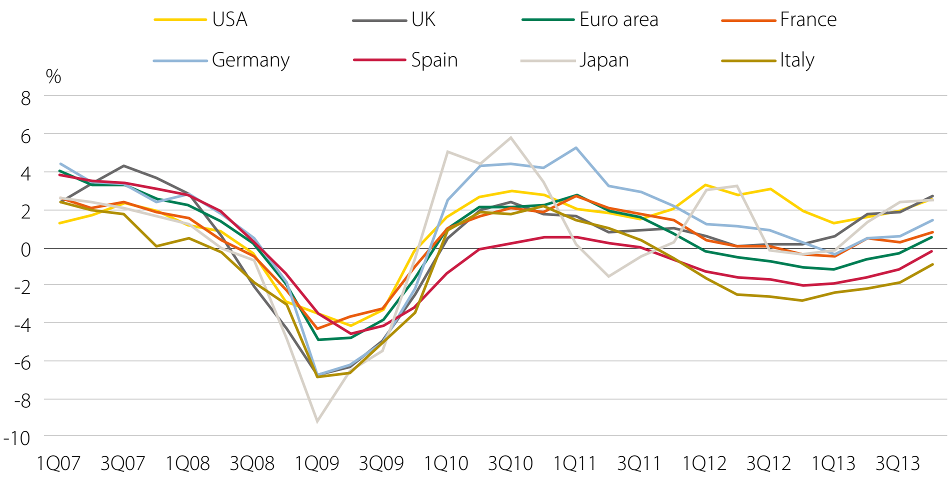
2 Macro-financial background

2.1 International economic and financial developments

Activity gathers speed in most advanced economies through the closing months of 2013…

The latest activity data, corresponding to the fourth quarter of 2013, confirm that most of the advanced economies are set on a recovery path. The United States and the United Kingdom retained the lead observed in previous quarters, closing the year with growth rates near or exceeding 2.5%, while euro-area growth was on a considerably more modest scale. Nonetheless the area's GDP expanded 0.5% in annual terms in last year's closing quarter, as activity gained speed in the majority of economies, including the most fragile (see figure 1).

Gross domestic product (annual % change) FIGURE 1



Source: Thomson Datastream.

…in a context of reduced inflation expectations, especially in the euro area.

Price behaviour in the advanced economies over the last few months evidences the absence of inflationary pressures. In the euro area, however, the speed with which prices have fallen has set some analysts talking about a risk of deflation. Specifically, euro-area headline rates have tumbled from nearly 3% at the 2011 close to less than

1% in recent months, due to weak domestic demand in a context of moderating commodity prices.[2]

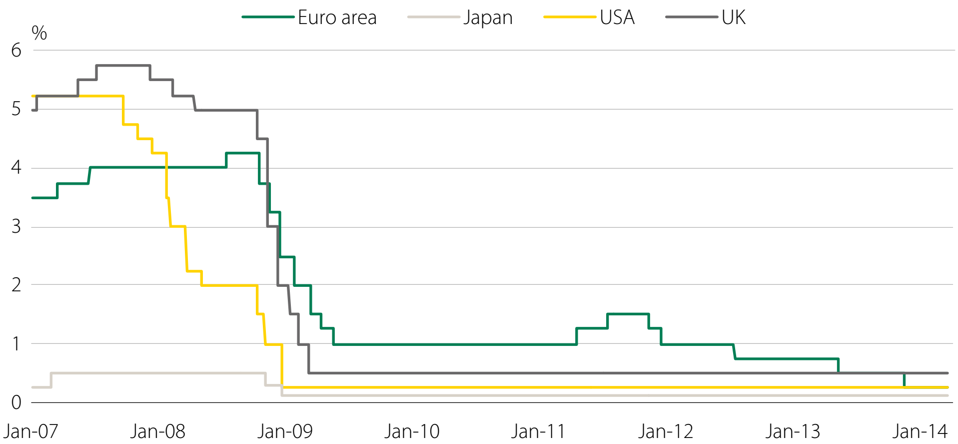
Monetary expansion in Japan has lifted inflation rates to levels comparable with other advanced economies.

Japan was the sole advanced economy where inflation advanced on a significant scale, from around 1% in spring 2013 to almost 1.5% this year to date. The aggressive monetary expansion promoted by the central bank has placed Japanese inflation rates on a par with those of other advanced economies like the United States or the United Kingdom.

In the United States, the Federal Reserve began to withdraw its monetary stimulus in January.

Although US inflation has tended to fluctuate more, rates have held within the 1% to 2% range for practically the last two years. The anchoring of inflation expectations in the economy, and the greater impetus of activity and employment led the Federal Reserve to confirm the phased withdrawal of its monetary stimulus programme in December 2013, with effect from the following month. Its initial announcement included a ten-billion-dollar reduction in the bond buying programme to a monthly rate of 75 billion. This was followed in late January and the middle of March by announcements of two new "tapering" moves of ten billion dollars each, scaling monthly purchase volumes down to 55 billion dollars. As regards interest rates, the message from both forward contracts and analysts' forecasts is no rates upcycle in the current year.

Official interest rates FIGURE 2



Source: Thomson Datastream. Data to 14 de March.

In international debt markets, the yields of US, UK and German benchmarks head lower in the first quarter…

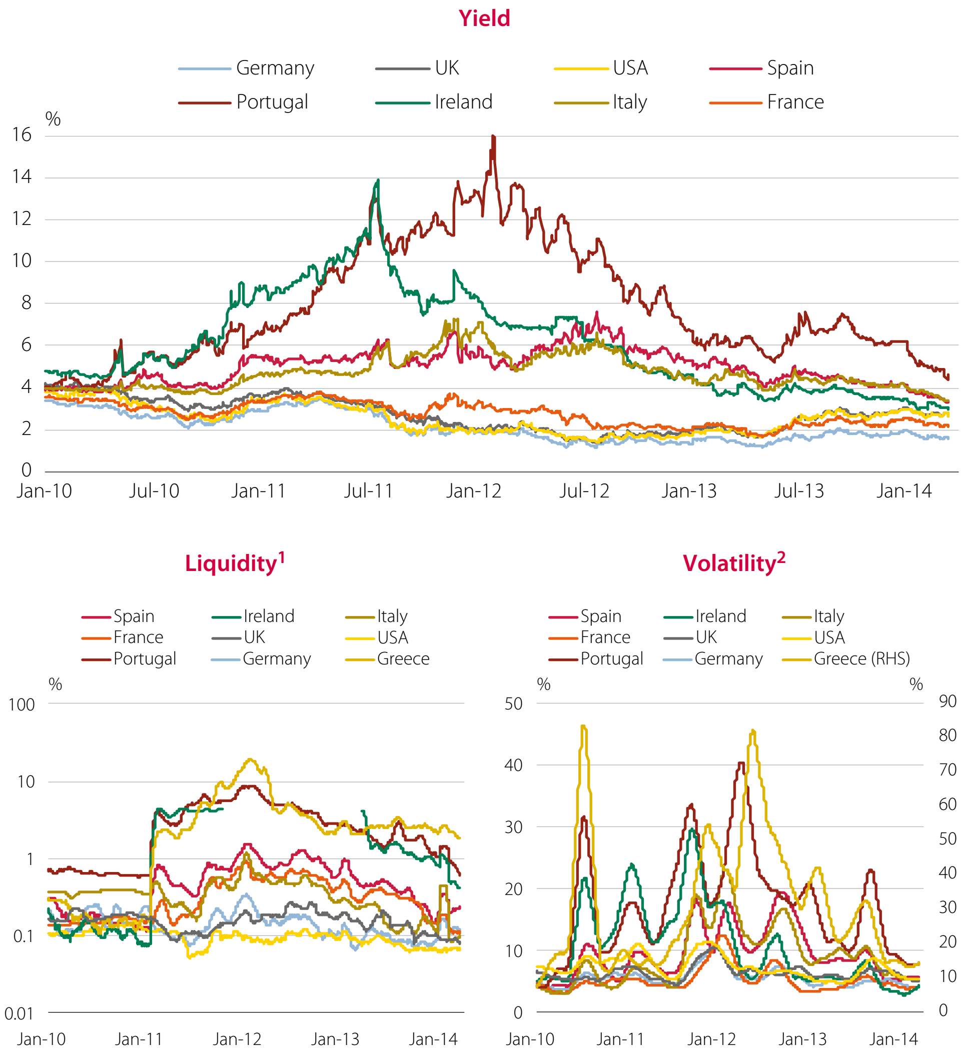
Some of the trends emerging on world debt markets in the second half of 2013 have subsequently run their course. In particular, the rise in the long-term bond yields of the United States, United Kingdom and Germany, spurred by their greater economic buoyancy and the increasingly attractive debt prices of more fragile European economies, gave way to a renewed run-down in the opening quarter of 2014, when they dropped around 0.4 points vs. year-end levels (see figure 3). The turmoil affecting markets in the year's first weeks – provoked by instability among the emerging economies (see exhibit 1) and, later, political tensions in Ukraine – has reignited the "flight to quality" and ramped up purchases of these countries' debt.

2 Core inflation in the euro area dropped from 2.0% to 1.1% in the same period.

The improved risk tone of Europe's more fragile economies was sustained through the opening months of 2014, enhancing the attractiveness of their debt, above all for yield-seeking investors. The long-term bond yields of Ireland, Spain, Italy and Portugal fell in consequence to mid-March levels of 3.0%, 3.3%, 3.4% and 4.6% respectively, from 42 bp to 158 bp lower than at year-end 2013. With the exception of Portugal, this movement restored yields to their levels preceding the economic and financial crisis.

…accompanied this time by Europe's more fragile economies.

Ten-year sovereign bond market indicators FIGURE 3



Source: Bloomberg, Thomson Datastream and CNMV. Data to 14 March.

1 Monthly average of the daily bid-ask spread of ten-year sovereign yields. Y axis on a logarithmic scale.

2 Annualised standard deviation of daily changes in 40-day sovereign bond prices. Moving average of 50 periods.

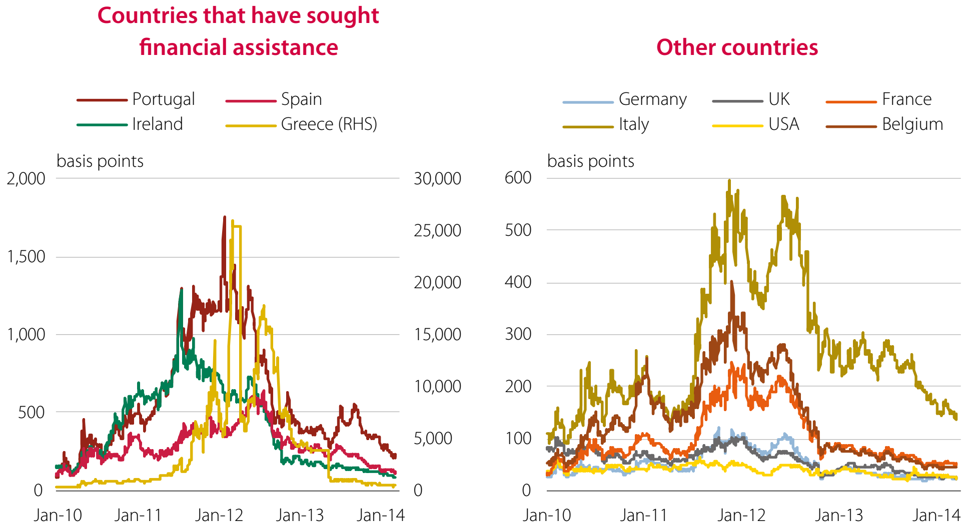
Sovereign risk premiums reflected this fading of concerns over Europe's weaker economies in the first quarter of 2014. As we can see from figure 4, the sovereign spreads of Ireland, Spain and Italy, as derived from five-year CDS, were running at mid-March levels of 86 bp, 115 bp and 147 bp respectively; between 20 bp and 38 bp lower than at end-2013. In the case of Portugal, the run-down was even more intense, with CDS spreads narrowing by 120 bp as far as 225 bp at the first-quarter close.

Lesser uncertainty regarding the weakest European economies and investor yield-seeking strategies spur further reduction in sovereign spreads.

Corporate bond spreads also feel the benefit, especially those of the lowest-rated instruments.

The spreads being charged on corporate bonds in the United States and Europe (see figure 5) testified to their continuing attractiveness vs. alternative investments. Buyers have been rushing into corporate debt for several quarters now, with a preference for the riskier assets that fulfil the goals of high-yield investment strategies. The result has been a historic fall in the risk premiums of certain categories of debt. Hence the spreads of the lowest-rated debt have dropped to almost 350 bp in the United States and 380 bp in Europe, zeroing in on the pre-crisis levels of mid-2007.

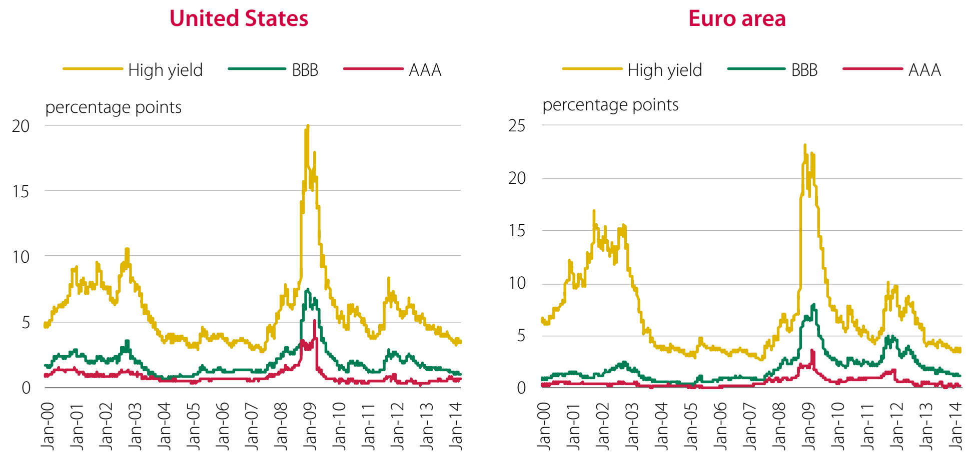
Sovereign credit spreads (five-year CDS) FIGURE 4



Source: Thomson Datastream. Data to 14 March.

Corporate bond spreads FIGURE 5

Spread vs. the ten-year government bond[1]



Source: Thomson Datastream and CNMV.

1 In the euro area, versus the German benchmark.

Net sovereign debt issuance in full-year 2013 sinks from 3.7 to 2.5 trillion dollars.

Net issuance on international debt markets summed 3.6 trillion dollars in the full-year period, 23.7% less than in 2012. Leading the decline was net sovereign debt issuance, which dropped to 2.5 trillion dollars from 3.7 trillion the previous year as governments in main world regions, the United States especially, continued to apply the brakes (see figure 6). Among private-sector borrowers, salient developments were the upswing in net debt financing by both US and European banks, after several years in negative terrain. Finally, the net issue volumes of non-financial corporations fell slightly in the United States, and notably in Europe.

Data for the opening months of 2014 point to the persistence of most of these trends, i.e., a further decrease in net sovereign issuance, especially in Europe, positive net debt financing by financial institutions in the United States and Europe, and a run-down in issuance by non-financial corporations that has been particularly intense in Europe.

Most of last year's issuance trends have persisted through the opening quarter.

Net international debt issuance FIGURE 6

Source: Dealogic. Half-year data. Data for the first half of 2014 run to 14 March, but are restated on a semiannual basis to facilitate comparison.

After a year that closed with strong gains on leading advanced economy stock indices, the first three months of 2014 brought a reversal of the trend. The price rally buckled as concerns mounted about the vulnerability of emerging economies, the more negative activity data coming out of China, and political tensions between Russia and Ukraine. Against this backdrop, US indices closed the first-quarter period strung out between the -3.1% of the Dow Jones and the 1.6% of the Nasdaq, and

Bull trend exhaustion sets in during the first quarter of 2014.

European indices between the -5.2% of Germany's Dax and the 6.9% of Italy's Mib 30 (see table 1). Falls were steeper still on Japanese indices (from the -10.6% of the Topix index to the -12.1% of the Nikkei 225), whose volatility readings also climbed to the neighbourhood of 30% (see figure 7).

Performance of main stock indices[1] (%)

TABLE 1

%	2010	2011	2012	2013	1Q13	2Q13	3Q13	4Q13	1Q14 (to 14 March) % prior quarter	1Q14 (to 14 March) % y/y[2]
World										
MSCI World	9.6	-7.6	13.2	24.1	7.2	-0.1	7.7	7.6	-1.2	14.0
Euro area										
Euro Stoxx 50	-5.8	-17.1	13.8	17.9	-0.5	-0.8	11.2	7.5	-3.4	9.5
Euronext 100	1.0	-14.2	14.8	19.0	4.7	-1.3	10.3	4.4	-1.6	9.3
Dax 30	16.1	-14.7	29.1	25.5	2.4	2.1	8.0	11.1	-5.2	12.4
Cac 40	-3.3	-17.0	15.2	18.0	2.5	0.2	10.8	3.7	-1.9	8.9
Mib 30	-8.7	-24.0	10.2	18.8	-2.6	-0.4	11.8	9.4	6.9	26.8
Ibex 35	-17.4	-13.1	-4.7	21.4	-3.0	-2.0	18.3	8.0	-1.1	13.3
United Kingdom										
FTSE 100	9.0	-5.6	5.8	14.4	8.7	-3.1	4.0	4.4	-3.3	0.0
United States										
Dow Jones	11.0	5.5	7.3	26.5	11.3	2.3	1.5	9.6	-3.1	10.5
S&P 500	12.8	0.0	13.4	29.6	10.0	2.4	4.7	9.9	-0.4	17.8
Nasdaq-Cpte	16.9	-1.8	15.9	38.3	8.2	4.2	10.8	10.7	1.6	30.3
Japan										
Nikkei 225	-3.0	-17.3	22.9	56.7	19.3	10.3	5.7	12.7	-12.1	15.7
Topix	-1.0	-18.9	18.0	51.5	20.3	9.6	5.3	9.1	-10.6	12.2

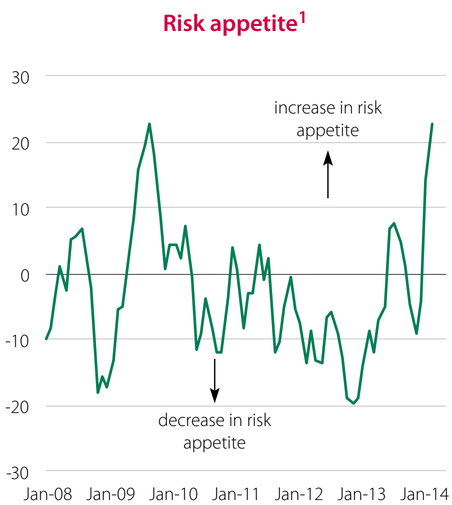
Source: Datastream.

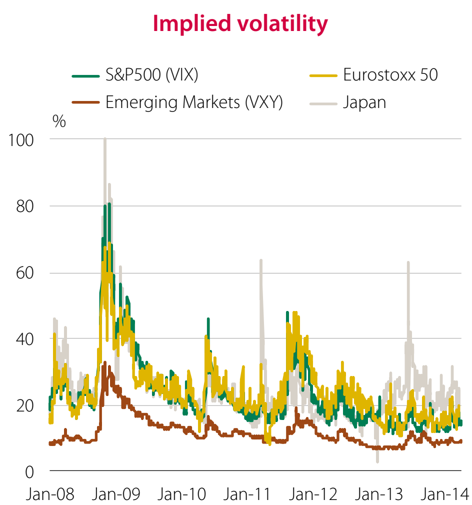
1 In local currency.

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

Financial market indicators

FIGURE 7





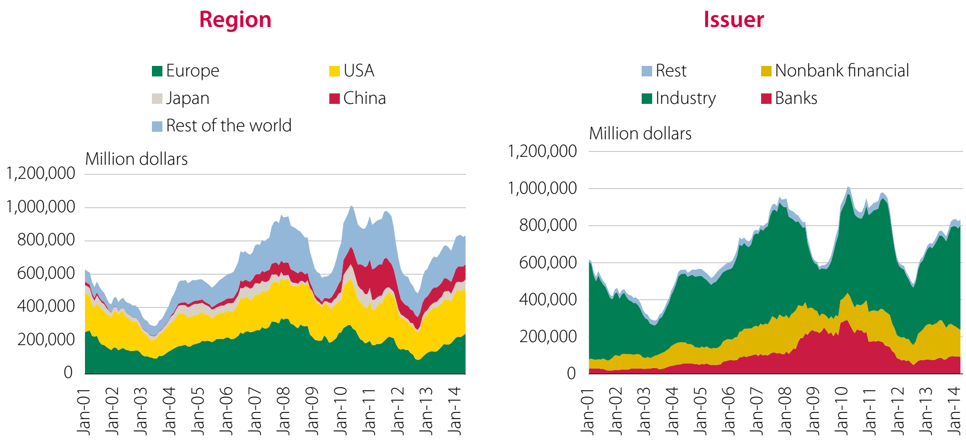
Source: Thomson Datastream and CNMV.

1 State Street indicator.

The value of equity issues on world financial markets rose by 25.7% in 2013 as far as 834 billion dollars. Although all main economic areas participated in the increase to some extent, the stand-outs were the 67% rebound in European issuance to 224 billion dollars, and placement volumes in Japan nearly doubling the previous year's. US companies, meantime, raised 280 billion dollars in equity capital, 13.7% more than in 2012. A breakdown by sector shows that industrial firms accounted for the lion's share of the 2013 increase, with issuance up by 38.3% to 535 billion dollars, while financial institutions raised 96 billion, an annual increase of 26.1%. Issuance has held up strongly through the first quarter of 2014, particularly in Europe, fuelled, it would appear, by investors' keener appetite for risk (see left-hand panel of figure 7).

Equity issuance keeps up a brisk pace after the 26% increase of 2013.

Global equity issuance FIGURE 8



Source: Dealogic. Accumulated twelve-month data to 14 March. For comparative purposes, the figure for March is restated on a monthly basis.

The tapering of the US monetary stimulus and its impact on emerging market economies

EXHIBIT 1

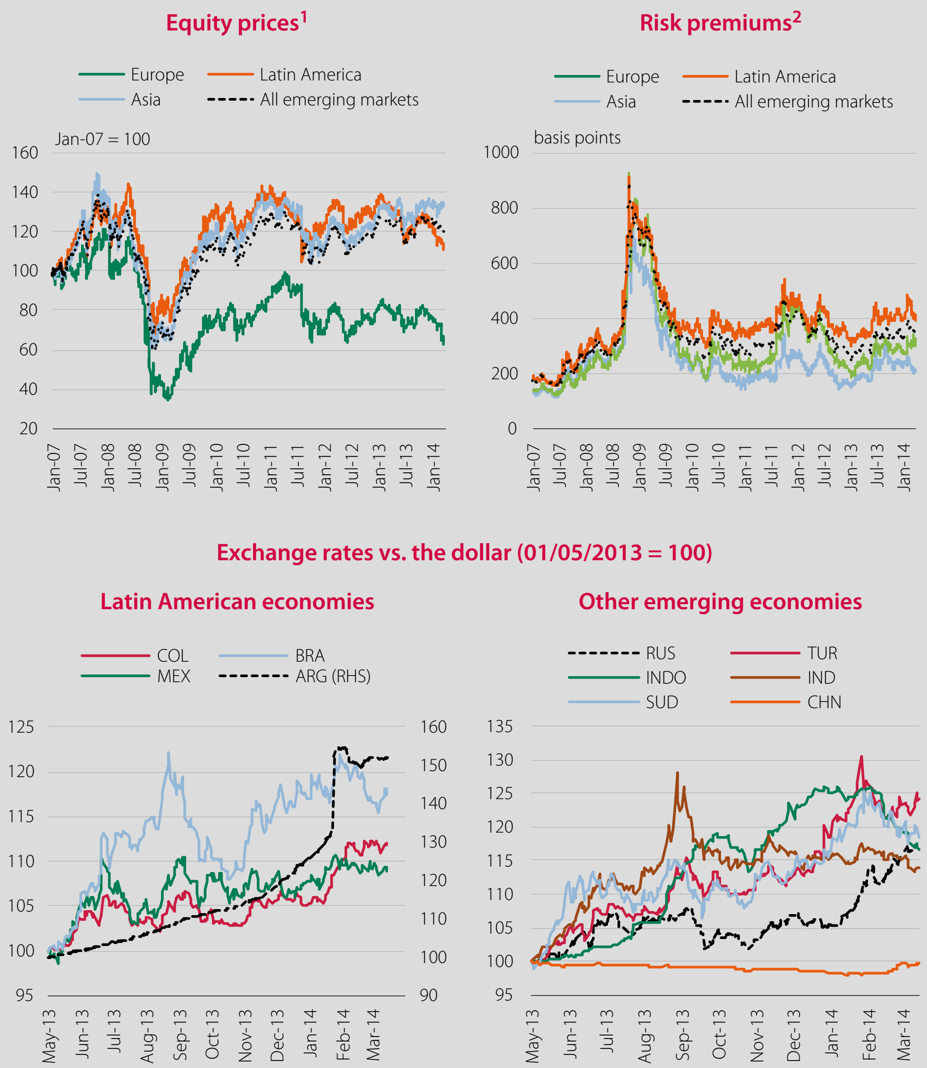
Interest rates in major advanced economies fell to historic lows during the recent economic and financial crisis. In some countries, also, the monetary authorities adopted non-conventional measures which pumped extra liquidity into global financial markets. The US Federal Reserve went so far as to plough 85 billion dollars a month into its bond-buying programme, as part of the package known as quantitative easing. Part of the surplus liquidity generated by these measures, in a reduced interest rate environment, found its way into emerging market economies, which offered attractive yields at a time when most of the advanced economies remained mired in recession.

However, things changed in May 2013, when the Federal Reserve declared its readiness to "taper" its monetary stimulus programme in line with the progress of domestic activity and employment indicators, which were just then beginning to emit positive signals. This tapering talk had a sharp negative impact on emerging regions, causing financial conditions to tighten considerably in the year's middle weeks. Capital inflows underwent a noticeable reversal,[1] with the result that stock markets fell, risk premiums rose and, graver still, some currencies depreciated sharply (see figure E.1.1).

Turbulence returned to financial markets at the start of 2014, with the news that the Fed had moved from readiness to action and would start scaling down its monthly bond purchases from January onwards.[2] The emerging economies that have suffered most from the phased withdrawal of the US monetary stimulus are those most dependent on external financing (current account deficit), though other factors that have proved decisive are reserve levels, the extent of credit expansion and the specific directions of national policies.

Brazil, Turkey, Indonesia, India, South Africa and Russia have been the worst affected so far. The depreciation of their currencies against the US dollar at the height of market tensions ranged in most cases from 10% to 15%.[3] At times, the decline in value of local currencies has reached such a pitch that central banks have had no choice but to hike interest rates to stem the outflow of capital, despite the potential dampening effect on economic activity.

Performance of emerging financial markets FIGURE E1.1



Source: Thomson Datastream.

1 FTSE indices.

2 EMBI indices.

The economic and financial outlook for emerging market economies remains generally positive despite a minor slowdown in activity, and the flow of investment to these regions should hold up reasonably well in the short and medium term. However, the switch in US monetary policy will continue to promote a natural rebalancing of investor portfolios, which may reduce the volume of financial investments in emerging nations compared to the recent past.

1 BIS (2013), *Quarterly Review*, December.
2 The Federal Reserve's initial announcement included a 10-billion-dollar reduction in bond purchases to 75 billion a month. At the end of January, it announced a further cut to 65 billion dollars a month, followed in mid-March by a third cut to 55 billion dollars.
3 Since the start of May 2013, i.e., on a broader time scale, some currencies have accumulated losses deeper than 20%.

2.2 National economic and financial developments

GDP growth of 0.2% in the fourth quarter of 2013 marked the second quarter in positive territory and contained the full-year decline at 1.2%.

According to the latest data from Quarterly National Accounts, corresponding to the fourth quarter of 2013, the Spanish economy expanded 0.2% in quarterly terms, a 0.1 point improvement on the previous quarter. This advance contained the full-year decline in GDP at 1.2%, 0.4 points less than in 2012 but also 0.8 points worse than the euro area, which contracted 0.4%.

Analysis of main GDP components reveals a better balance between domestic demand and the external sector.

Analysis of main GDP components shows a progressive realignment between domestic and external demand. Specifically, domestic demand detracted only 0.6 points from growth in the fourth quarter compared to 4.3 points in the first three months, while the positive contribution of net exports dropped from 2.4 to 0.4 points. The two main components of domestic demand gained speed in the second-half period, but not enough to deliver a positive full-year outcome. Hence final household consumption contracted by 2.1% (2.8% in 2012) and gross fixed capital formation by 5.0% (7.0% in 2012). Note the divergent progress within this last component of construction investment, down by 9.6%, and equipment investment, which expanded 2.3% in the full-year period (see table 2). In the external sector, both exports and imports increased at a faster pace in the year's closing quarter for average growth of 4.9% and 0.4% respectively (2.1% and -5.7% in 2012).

The rate of decline in most branches of activity slows towards year end.

A supply side analysis of GDP shows that all main branches of activity slowed their rate of decline, with some even registering year-on-year growth in the year's closing quarter. Finally, the average gross added value of industry shrank by 1.3% against the 0.5% of services and the 7.7% of the struggling construction sector. By contrast, the GVA of primary activities expanded 1.2% in the full-year period.

Spain's dwindling inflation rate lifts the negative differential vs. the euro area to almost one full point in February 2014.

Spanish inflation prolonged the downward course of 2013, with renewed falls in the opening months of 2014 as far as a February rate of near 0% against almost 3% twelve months before (see figure 9). Core inflation, meantime, eased from 2.3% to 0.1%. This strong drop in inflation has its origins in weak domestic demand, moderating energy prices and the unwinding of the effect of the 2012 hike in VAT. Finally, Spain's inflation differential vs. the euro area turned negative last September after starting the year at one full point, and by February 2014 was running at -0.8 points.

Spain: main macroeconomic variables (annual % change)

TABLE 2

	2010	2011	2012	2013	EC[1] 2014F	EC[1] 2015F
GDP	**-0.2**	**0.1**	**-1.6**	**-1.2**	**1.0**	**1.7**
Private consumption	0.1	-1.2	-2.8	-2.1	0.6	1.1
Government consumption	1.5	-0.5	-4.8	-2.3	-0.9	-0.2
Gross fixed capital formation, of which:	-5.5	-5.4	-7.0	-5.0	0.1	2.0
Construction	-9.9	-10.8	-9.7	-9.6	n.a.	n.a.
Equipment and others	5.0	5.6	-3.9	2.3	5.8	6.7
Exports	11.7	7.7	2.1	4.9	5.4	6.4
Imports	9.4	0.0	-5.7	0.4	3.3	4.9
Net exports (growth contribution, p.p.)	0.4	2.1	2.5	1.4	0.8	0.7
Employment[2]	**-2.3**	**-2.2**	**-4.8**	**-3.4**	**0.1**	**1.1**
Unemployment rate	**20.1**	**21.6**	**25.0**	**26.4**	**25.7**	**24.6**
Consumer price index	**1.8**	**3.2**	**2.4**	**1.4**	**0.3**	**0.9**
Current account balance (% GDP)	**-4.5**	**-3.8**	**-1.1**	**0.7**	**1.6**	**1.8**
General government balance (% GDP)[3]	**-9.6**	**-9.6**	**-10.6**	**-7.1**	**-5.8**	**-6.5**
Public debt (% GDP)	**61.7**	**70.5**	**86.0**	**93.9**	**98.9**	**103.3**
Net international investment position (% GDP)[4, 5]	**-92.0**	**-82.6**	**-67.1**	**-78.9**	**n.a.**	**n.a.**

Source: Thomson Datastream, European Commission, Banco de España and National Statistics Office (INE).

1 European Commission forecasts of February 2014.

2 In full-time equivalent jobs.

3 Figures for 2011, 2012 and 2013 include government aid to credit institutions amounting to 0.5%, 3.8% and 0.5% of GDP respectively.

4 For the third quarter in the case of 2013.

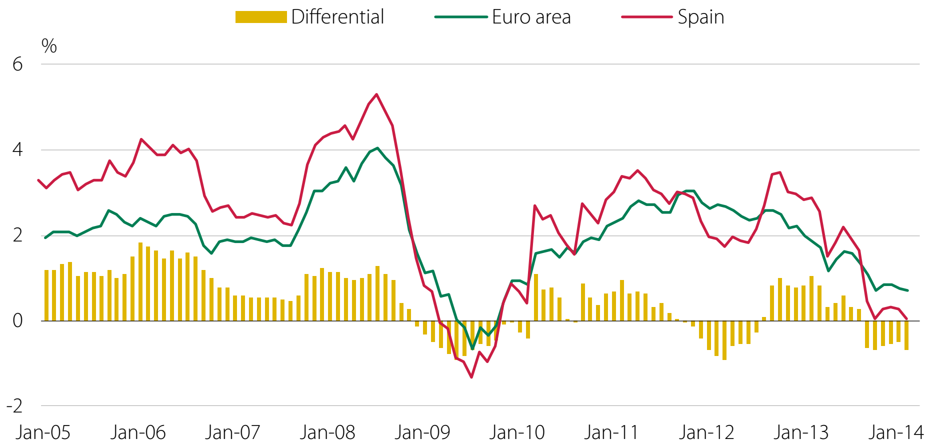
5 Ex. Banco de España.

n.a.: not available.

Recent labour-market figures hint at a change of trend.

The latest labour-market figures suggest job destruction and the advance of unemployment may be coming to an end. Jobless rates retreated from their first-quarter peak of 27.2% to 26% at the annual close, while the decline in employment slowed to a fourth-quarter rate of 1.2%. The statistic of 199,000 jobs lost in 2013 (121,400 in the public and 77,500 in the private sector) compares favourably to the 850,000 of 2012 and the 600,000 of 2011. Another positive note was the first annual increase since mid-2008 in the number of social security contributors, up by 0.38% to 16.2 million in February 2014. Unit labour costs, finally, fell by 1.5% on average, prolonging the descent initiated in 2010, on higher productivity per worker (up by 2.3%) and a small rise in employee wages (0.7%).

Harmonised index of consumer prices: Spain vs. the euro area (annual % change) FIGURE 9



Source: Thomson Datastream. Data to February.

According to available budgetary execution figures for 2013, the public deficit closed at 6.62% of GDP[3] (7.08% if we factor in aid to the financial sector), marking a bare 0.1 point overshoot of the official target. Multiannual budgetary objectives for 2014-2016 pursue additional deficit shrinkage to below 3% of GDP in 2016. Meantime, general government debt swelled from 86% at end-2012 to 93.9% in December 2013.

The general government deficit closed 2013 at 6.62% of GDP, a bare 0.1 points above the full-year target.

The Spanish banking industry remained immerse in a root-and-branch restructuring further to the terms of the Memorandum of Understanding (MoU) concluded between Spanish and European authorities in July 2012. As part of the financial assistance facility envisaged in the MoU and finalizing in January 2014, entities have stepped up their levels of provisioning, and over 50 billion euros in impaired assets have been taken off bank balance sheets and transferred to the asset management company for assets arising from bank restructuring (SAREB), starting with Group 1 entities in December 2012, and continuing with Group 2 entities in February 2013. In recent months, the focal point of activity has shifted from these restructuring and resolution management activities to others relating to the disposal of the FROB's stakes in financial institutions and the promotion of corporate transactions.

The programme of financial assistance to the Spanish banking sector finalised in January 2014, but major challenges still remain…

Even after allaying doubts about the quality of its assets, the Spanish banking sector has struggled to contend with weak economic activity at home on top of the fragmentation that characterises European financial markets. Hence the seeming discrepancies in the latest data on its economic and financial health. On the one hand, NPL ratios continued to escalate to a December 2013 high of 13.6%. But on the other, sector income statements appear to be in decidedly better shape. To the month of September, financial institutions had obtained aggregate profits of 2.13 billion euros, contrasting with the 5.80 billon losses of the same period in 2012. Although declines in net interest income and income from equity instruments took gross operating income down from 14.44 billion euros to 12.16 billion, sharply falling impairment losses on financial

…among them, a weak economy and the fragmented state of European markets.

3 The deficit of central government, the social security system and autonomous communities stood at 4.33%, 1.16% and 1.54% of GDP respectively, while local corporations turned in a surplus of 0.41%.

and other assets (down from 13.53 to 5.02 billion and 2.62 billion to 391 million respectively) did enough to propel the sector back into positive numbers.

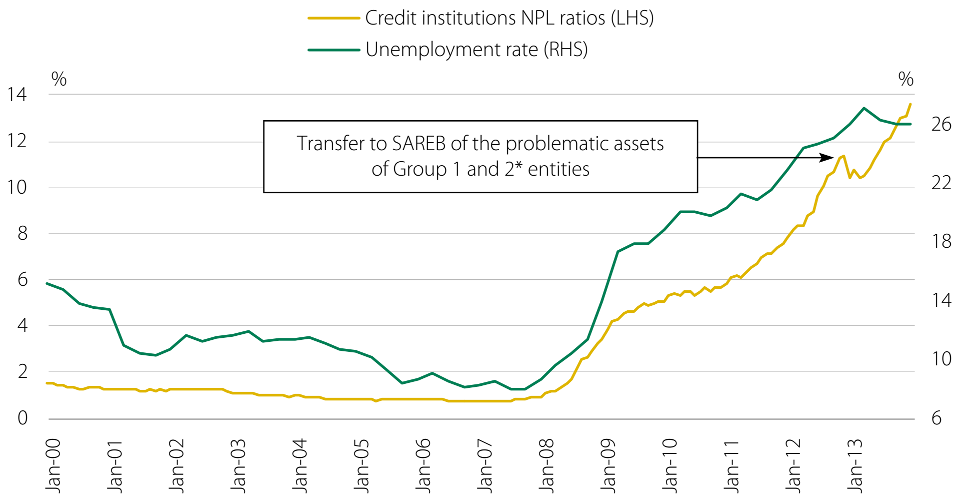
Bank lending to non-financial resident sectors starts the year down by close to 5%.

In this context, bank lending to non-financial resident sectors continued to dwindle through 2013 and the first months of 2014, albeit with large differences between sectors. Outstanding loans under this caption fell by 5.1% to December 2013 (-5.0% to December 2012) and by end-January 2014 were still 4.8% down on the year-ago amount. Although the annual decline was on a similar scale for businesses (-4.6%) and households (-5.0%), it actually slowed in the first case and accelerated in the second, reflecting the slump in consumer loans. In the euro area, lending to non-financial corporations fell by 2.9% year on year to January 2014, while lending to households receded 0.2%.

Despite easier conditions, bank sector debt issuance has tended to recede thanks to its lower funding needs.

The funding conditions of Spanish credit institutions continued to improve in line with the calmer mood of financial markets, though, again, the persisting fragmentation of Europe's markets tended to make issuance costlier for smaller banks compared to their same-sized European peers. In any event, ongoing deleveraging has sizeably reduced the sector's funding needs and made it less reliant on debt financing and Eurosystem loans.

Credit institution NPL ratios and the unemployment rate[1] FIGURE 10



Source: Banco de España and National Statistics Office (INE). Data to December 2013.

1 Percentage of the active population.

* Group 1 transfers took place in December 2012 (36.70 billion euros) and those of Group 2 in February 2013 (14.09 billion euros).

Bank asset funds EXHIBIT 2

Bank asset funds or BAFs are closed pools of assets and liabilities, without legal personality, set up as part of the restructuring of Spain's banking sector. They are instruments unique to the asset management company for assets arising from bank restructuring[1] (the SAREB, in its Spanish initials) for the purpose of helping the company to dispose of its assets. BAFs, which share some features with existing investment vehicles like securitisation funds, draw their assets and liabilities exclusively from the SAREB and may only be marketed to institutional investors.

They are regulated by Royal Decree-Law 24/2012 of 31 August, Law 9/2012 of 14 November, which reserves them the name "bank asset funds",[2] and the latter's implementing regulations (Royal Decree 1559/2012 of 15 November, establishing the legal framework for the asset management company).

Creation of BAFs and rules for the transfer of assets and liabilities

BAFs are established by public deed and entered in a register held by the CNMV. Their management and representation is entrusted, on an exclusive basis, to securitisation fund management companies that meet the requirements of Law 9/2012 and Royal Decree 1559/2012. BAFs' initial assets may comprise both assets and, where applicable, liabilities, deriving from the SAREB. It will also be possible for the SAREB to transfer assets and liabilities to an existing BAF, provided its articles of association so permit.

The transfer of assets, to be governed by the general framework for asset management companies established in Law 9/2012, will be full and unconditional, and for the entire remaining period up to maturity, as the case may be. Moreover, the transferor will not grant any guarantees to the BAF, nor insure in any other way the satisfactory outcome of the credit claims transferred or, in general, the value or quality of the assets or rights transferred. Transfers will be formalised in a contractual document. With each new incorporation of assets, the BAF management company will furnish the CNMV with a document signed by the SAREB, setting out their details and characteristics.

Securities issues and sub-funds

BAFs may issue securities[3] admissible for trading on official secondary markets. These securities can only be marketed to professional investors, and will have a minimum denomination unit of 100,000 euros. Further, the BAF's articles of association may envisage the creation of a syndicate holding securities issued by the fund, which will come under the provisions of the Corporate Enterprises Law with certain adaptations.

When contemplated in its articles of association, BAF assets may be divided into various independent sub-funds, against which securities may be issued or obligations assumed. The share of the BAF's assets assigned to each sub-fund will meet only the costs, expenses and obligations expressly attributable to that sub-fund. And likewise the creditors of a sub-fund may only enforce their claims against the sub-fund in question.

Taxation

The seventeenth additional provision of Law 9/2012 lays down a special tax regime for BAFs and their investors, to apply over the period when the Fund for Orderly Bank Sector Restructuring (FROB) is exposed to the BAFs (a period circumscribed to the life of the SAREB).[4] In this phase, BAFs will be liable for corporate income tax at a rate of 1%, and will come under the tax regime envisaged for collective investment institutions.

BAF investors who are liable for Spanish corporate income tax, personal income tax or non-resident income tax and operate a permanent establishment in Spain will be subject to the tax rules applicable to shareholders or investors in collective investment institutions. Payers of non-resident income tax who do not operate a permanent establishment in Spain can enjoy the exemption envisaged in non-resident tax legislation for the holders of Spanish public debt.

Reporting obligations

The management company must disclose any circumstances with a material bearing on the asset value or prospects of each BAF it handles. To this end, it must publish on its website the articles of association and other public deeds issued subsequently in relation to each fund, along with detailed documentation of subsequent asset contributions, significant information relating to the transfers of assets and liabilities by the SAREB and, periodically, the corresponding half-yearly and annual reports. These reporting obligations will cease the moment the securities issued by a BAF are admitted to listing on an official secondary market, to be replaced by the provisions of article 35 of Securities Market Law 24/1988 and its implementing regulations.

The content and format of these reporting obligations is enlarged upon in CNMV Circular 6/2013, which provides models for the half-yearly financial statements and annual accounts that managers must publicly disclose as well as filing with the CNMV. The circular also sets out the minimum content for each BAF's management report and notes to the annual accounts. In addition to the key financial statements regulated in the General Chart of Accounts, half-yearly reports will incorporate others offering a more detailed breakdown of BAF assets and liabilities in the interest of maximising transparency and investor information.

Number of BAFs registered and activity to date

At the time of writing, three BAFs had been set up and registered with the CNMV, following the transfer from the SAREB of 4,128 properties and four office buildings with a combined value of 326 million euros. These funds have so far carried out securities issues for the sum of 184 million euros, none of which are listed on official secondary markets.

1 Established in November 2012 pursuant to the Memorandum of Understanding (MoU) signed by the Spanish government and its European partners in July 2012.
2 Tenth additional provision.
3 FAB securities issues come under the terms of Securities Market Law 24/1988 and its implementing provisions.
4 15 years counting from its incorporation in November 2012.

Non-financial corporations grow their combined profits by 7.3% to 11.15 billion euros…

Non-financial listed companies grew their aggregate profits by 7.3% in 2013 to 11.15 billion euros. Heading the list were companies in retail and services, whose earnings swelled from 4.72 billion in 2012 to almost six billion in 2013, followed by industrial firms with a combined advance from 31 million to 609 million respectively. A positive contribution too from construction and real estate companies, which managed to reduce their losses from 4.93 billion in 2012 to 3.92 billion in 2013. Energy stands out as the only sector whose earnings fell short of the previous year's (down 19% to 8.39 billion euros), though it conserved its lead in straight-money terms (see table 3).

Earnings by sector:[1] non-financial listed companies TABLE 3

	EBITDA[2]		EBIT[3]		Net profit	
Million euros	2012	2013	2012	2013	2012	2013
Energy	27,241	24,114	16,968	13,829	10,346	8,392
Industry	3,466	3,830	1,853	2,273	31	609
Retail and services	28,647	28,378	14,045	14,213	4,716	5,990
Construction and real estate	5,540	3,445	2,199	373	-4,933	-3,921
Adjustments	51	-72	190	20	231	79
TOTAL	**64,945**	**59,695**	**35,256**	**30,709**	**10,391**	**11,149**

Source: CNMV.

1 Year to date.

2 Earnings before interest, taxes, depreciation and amortisation.

3 Earnings before interest and taxes.

…while debt levels close the year 10% lower at 270 billion.

The aggregate debt of non-financial listed companies dropped by 10% in 2013 to 270 billion euros. The largest fall was in construction and real estate, which lowered its debt to the tune of 11.10 billion euros,[4] followed by retail and services with 9.38 billion and energy with 9.09 billion. Aggregate leverage, after trending lower for several years, declined moderately from 1.41 in 2012 to 1.38 in 2013 (see table 4). Companies' debt coverage ratio, measuring the years needed to repay existing debt assuming constant EBITDA, edged up from 4.3 to 4.5, while their interest cover (EBIT/interest expenses) worsened slightly (from 2.1 to 1.8). Both indicators deteriorated in 2013 across all sectors followed with the exception of retail and services, where improvement drew on both debt reduction and higher inflows under key earning heads.[5]

Household saving rates settle at close to their pre-crisis levels (10.5% of disposable income)…

The latest indicators on the financial position of households reveal that saving rates have settled at around 10.5% of disposable income. After a strong build-up over 2008-2009, when precautionary saving drove this variable to historic highs approaching 18%, rates have more or less returned to their pre-crisis levels. Household debt-to-income and debt service ratios dropped to just under 120% and 14% of gross disposable income respectively, as households reduced their stock of liabilities.

…while their financial investments have recovered slightly with a preference for mutual funds.

Households enlarged both their volume of financial investment (0.9% of GDP[6] vs. -0.7% in 2012) and the variety of assets acquired. As we can see from figure 11, investment monies found their way into shares, cash, transferable deposits, investment funds and insurance products, while divestments centred on fixed-income instruments. The big news, however, was the renewed popularity of mutual fund investment (0.8% of GDP in 2013), which had been stuck in negative terrain since 2007 on a wave of unit-holder withdrawals.

4 The decline here relies in part on Metrovacesa's exclusion from the 2013 sample. Stripping out this effect, the reduction in debt between 2012 and 2o13 stands at nearly six billion euros.

5 Retail and services firms grew their net profits and EBIT by 27% and 1.2% respectively, while EBITDA held practically flat at -0.9%.

6 Cumulative four-quarter data to the third quarter of 2013.

Gross debt by sector: listed companies

TABLE 4

Million euros		2009	2010	2011	2012	2013
Energy	Debt	100,572	98,283	95,853	91,233	82,146
	Debt/ Equity	1.08	0.95	0.92	0.85	0.75
	Debt/ EBITDA[1]	3.46	2.81	3.27	3.26	3.41
	EBIT[2]/ Interest expenses	3.38	4.15	3.30	3.14	2.90
Industry	Debt	15,953	14,948	17,586	17,232	16,586
	Debt/ Equity	0.69	0.58	0.63	0.63	0.95
	Debt/ EBITDA	3.05	2.11	2.54	2.38	4.33
	EBIT/ Interest expenses	3.15	5.00	3.90	3.82	1.99
Retail and services	Debt	108,579	115,413	113,142	117,359	107,983
	Debt/ Equity	1.78	1.60	2.01	2.00	1.98
	Debt/ EBITDA	3.70	3.38	3.78	4.01	3.81
	EBIT/ Interest expenses	3.28	3.94	2.45	2.02	2.12
Construction and real estate	Debt	104,762	99,917	83,716	76,236	65,134
	Debt/ Equity	4.08	3.42	2.98	3.51	4.45
	Debt/ EBITDA	22.48	11.18	15.00	15.17	18.90
	EBIT/ Interest expenses	0.31	0.98	0.52	0.32	0.09
Adjustments[3]	Debt	-1,908	-1,792	-1,404	-1,429	-1,395
TOTAL	**Debt**	**327,958**	**326,769**	**308,893**	**300,633**	**270,454**
	Debt/ Equity	1.63	1.43	1.44	1.41	1.38
	Debt/ EBITDA	4.82	3.84	4.29	4.32	4.53
	EBIT/ Interest expenses	2.42	3.12	2.30	2.06	1.83

Source: CNMV.

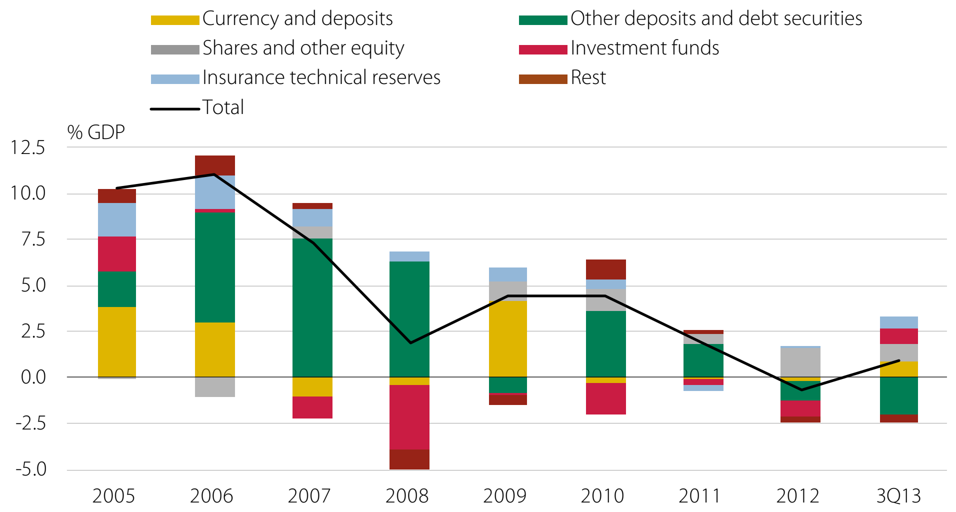
1 Earnings before interest, taxes, depreciation and amortisation.

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 include eliminations corresponding to subsidiary companies with their parent in another sector.

Households: financial asset acquisitions

FIGURE 11



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

2.3 Outlook

In its latest forecasts, the International Monetary Fund (IMF) augurs world growth of 3.7% in 2014 and 3.9% in 2015, almost one full point above the 2013 rate. The gathering pace of global economic activity will draw on both the advanced economies, projected to grow by 2.2% in 2014 and 2.3% in 2015 (1.3% in 2013), and the emerging markets, with annual advances of 5.1% and 5.4% respectively (4.7% in 2013).

World GDP growth is set to reach 3.7% in 2014 and 3.9% in 2015, one full point more than in 2013.

Gross Domestic Product (annual % change) TABLE 5

					IMF[1]	
	2010	2011	2012	2013	2014F	2015F
World	5.3	3.9	3.1	3.0	3.7 (+0.1)	3.9 (=)
United States	2.5	1.8	2.8	1.9	2.8 (+0.2)	3.0 (-0.4)
Euro area	1.9	1.8	-0.6	-0.4	1.0 (+0.1)	1.4 (+0.1)
Germany	3.9	3.4	0.9	0.5	1.6 (+0.2)	1.4 (+0.1)
France	1.6	2.0	0.0	0.3	0.9 (=)	1.5 (=)
Italy	1.7	0.6	-2.4	-1.8	0.6 (-0.1)	1.1 (+0.1)
Spain	-0.2	0.1	-1.6	-1.2	0.6 (+0.4)	0.8 (+0.3)
United Kingdom	1.7	1.1	0.3	1.8	2.4 (+0.6)	2.2 (+0.2)
Japan	4.7	-0.4	1.5	1.5	1.7 (+0.4)	1.0 (-0.2)
Emerging economies	7.5	6.2	4.9	4.7	5.1 (=)	5.4 (+0.1)

Source: Thomson Datastream and IMF.

1 In brackets, change vs. the previous forecast. IMF, forecasts published January 2014 with respect to October 2013.

The risks confronting both groups are of an essentially different nature. Among the advanced economies, the main risk factors are still the frailty of economic activity and, in some areas, the prospect of deflation, plus, in Europe, the need to complete the financial sector clean-up and move ahead with banking union. Finally, there is the danger that financial markets may suffer new waves of turbulence in the event of an abrupt run-up in risk premiums and interest rates. For the emerging economies, the fear is that the switch in US monetary policy could reignite financial market tensions, with the corollary of capital outflows, falling share prices, rising risk premiums and currency depreciation. Some of these economies face the added task of rebalancing growth between the domestic and external sector.

Downside risks derive primarily from the economic weakness of certain zones and the impact of a rebound in risk premiums.

The IMF's projections for the Spanish economy point to growth of 0.6% in 2014 and 0.8% in 2015 after last year's 1.2% contraction. These estimates mark an upward revision of 0.3 and 0.4 points respectively, but still stand slightly below the consensus forecasts of various Spanish private institutions. Meantime, activity and employment indicators suggest the economy is slowly recovering, and should be able to exploit its improved competitiveness without losing sight of fiscal consolidation and bank sector restructuring goals. The main risks for this scenario are those deriving from prolonged labour market weakness and the constraints still weighing on private-sector credit.

The analyst consensus is that Spain's economy will expand around 1% in 2014, but major challenges remain (labour market, fiscal adjustment, bank sector restructuring…).

3 Spanish markets

3.1 Equity markets

Spanish share prices falter on signs of instability in emerging economies and the ripples from political tensions between Russia and Ukraine.

The performance of Spanish equity markets in the first quarter of 2014 was marked by minor price falls and higher trading volumes, against a backdrop of reduced volatility and strong liquidity. Initially, prices had progressed within the bull trend initiated in the second half of 2013, with the support of generally favourable activity and employment indicators. However, from the end of February they were increasingly pressured by the instabilities affecting certain emerging markets and political tensions between Russia and Ukraine. Meantime, trading volumes on Spanish markets surged by 16.6% in the opening quarter, in stark contrast to the lethargy of recent years. Trading of Spanish shares on non-domestic markets continued its ascent to almost 14% of total volumes. Equity issuance to March stood at 4.59 billion euros, below last year's figures, with two IPOs as the main events.

The Ibex 35 sheds 1.1% in the opening quarter, in contrast to the continuing advance of small and medium cap indices.

After a strong late run in 2013, the Ibex 35 began to level off in the first months of 2014 and finally ended the quarter down by 1.1%[7] due to price falls in mid-March (see table 6). Other domestic stock indices, however, managed to prolong last year's advance, with medium and small cap indices gaining 3.8% and 14.5% respectively. The indices tracking the Latin American stocks traded on domestic platforms fared decidedly worse, after the US' decision to taper its monetary stimulus caused a wave of turmoil in the region (see exhibit 1). Finally, the FTSE Latibex All-Share and FTSE Latibex Top registered quarterly losses of 17.4% and 16.7%.

Sectors end the first quarter in differing form.

The quarter's top-performing sectors were, firstly, basic materials, industry and construction (4.6%, after gains of 28.9% in 2013), followed by oil and energy (3.2% vs. 19% in 2013) and financial and real estate services (1.3% vs. 19.9% in 2013). Conversely, losses were deepest in consumer goods (-9.1% against a rise of 17.1% in 2013), technology and telecommunications (-5.9% vs. 22.8% in 2013) and consumer services (-1.1%, in contrast to the 58.9% advance of 2013).

7 Data to 14 March.

Performance of Spanish stock market indices and sectors (%)

TABLE 6

							1Q14 (to 14 March)	
Index	**2010**	**2011**	**2012**	**2013**	**3Q13**[1]	**4Q13**[1]	**% prior quarter**	**% y/y**
Ibex 35	-17.4	-13.1	-4.7	21.4	18.3	8.0	-1.1	13.3
Madrid	-19.2	-14.6	-3.8	22.7	19.4	8.4	-0.7	14.8
Ibex Medium Cap	-5.6	-20.7	13.8	52.0	22.5	12.5	3.8	48.8
Ibex Small Cap	-18.3	-25.1	-24.4	44.3	22.8	13.0	14.5	47.8
FTSE Latibex All-Share	9.0	-23.3	-10.7	-20.0	5.4	-5.4	-17.4	-32.3
FTSE Latibex Top	9.7	-17.1	-2.6	-12.4	4.2	-1.4	-16.7	-30.0
Sector[2]								
Financial and real estate services	**-31.7**	**-18.9**	**-4.7**	**19.9**	**28.1**	**10.1**	**1.3**	**17.1**
Banks	-33.1	-20.3	-4.8	18.8	28.7	9.9	1.2	16.5
Insurance	-26.4	12.5	-2.0	47.3	12.7	17.1	-1.5	20.5
Real estate and others	-53.3	-47.5	-14.4	38.3	23.6	24.0	34.2	92.6
Oil and energy	**-8.6**	**-2.7**	**-16.0**	**19.0**	**6.5**	**7.4**	**3.2**	**14.4**
Oil	10.2	14.9	-35.4	19.5	13.0	0.0	-5.1	0.1
Electricity and gas	-14.2	-10.8	-5.4	18.7	3.5	11.1	6.5	20.6
Basic materials, industry and construction	**-15.2**	**-14.3**	**-8.0**	**28.9**	**16.1**	**8.0**	**4.6**	**28.9**
Construction	-14.9	-6.9	-9.3	26.5	15.6	5.9	7.0	29.4
Manufacture and assembly of capital goods	-29.2	-12.2	-8.8	55.4	22.1	10.3	-2.3	48.5
Minerals, metals and metal processing	-9.1	-33.7	-8.7	11.5	18.4	12.3	0.9	14.8
Engineering and others	-0.1	-29.0	3.8	7.6	5.3	9.7	12.9	15.5
Technology and telecommunications	**-12.8**	**-20.9**	**-18.3**	**22.8**	**15.5**	**5.4**	**-5.9**	**3.2**
Telecommunications and others	-12.8	-20.8	-23.0	17.1	17.5	2.8	-6.3	-2.7
Electronics and software	-12.0	-21.3	39.4	56.8	7.2	17.6	-4.1	40.3
Consumer goods	**17.0**	**5.7**	**55.6**	**17.1**	**16.6**	**6.7**	**-9.1**	**5.6**
Textiles, clothing and footwear	28.6	12.7	66.2	13.5	20.1	5.2	-15.1	-2.2
Food and drink	25.3	-6.3	25.0	4.7	8.4	1.7	-7.5	1.6
Pharmaceutical products and biotechnology	-22.2	-7.3	68.3	39.6	8.4	13.6	10.5	34.4
Consumer services	**-0.1**	**-24.2**	**12.7**	**58.9**	**19.6**	**12.2**	**-1.1**	**34.1**
Motorways and car parks	-10.1	-3.7	5.7	36.5	12.6	12.4	-2.2	21.9
Transport and distribution	55.3	-34.9	29.7	116.4	30.9	19.8	3.7	67.6

Source: BME and Thomson Datastream.

1 Change vs. the previous quarter.

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

Endorsement of the Registro Mercantil as the Pre-Local Operating Unit (pre-LOU) for Spain

EXHIBIT 3

The international financial crisis brought to light difficulties caused by the lack of a centralised system of entity identification. Concerns centred on agents' inability in certain cases to identify the counterparty in financial transactions, which hinders development of effective risk management models while complicating the resolution of financial firms.

Following its discussions on the problem, the G-20 decided to endorse the rollout of a universal system of legal entity identifiers (LEIs), to be issued and managed by local operating units (LOUs). LEI codes will boost the transparency of financial markets as well as facilitating the management of counterparty exposure and the orderly resolution of failing entities. Responsibility for the performance and oversight of the global LEI system lies with the Regulatory Oversight Committee (ROC).

LEI codes are still in the development phase. However, as an interim measure, a system of pre-LEI codes has been set in train. These identifiers will be issued by organisations known as Pre-LOUs, who will provisionally act as local registries assigning and registering codes. Once the LEI system is ready for launch, these organisations will formally become LOUs, provided certain conditions are met.

In Spain's case, the Registro Mercantil (Central Mercantile Register) is the designated pre-LOU. On 23 November 2013, it obtained the prefix that the ROC grants to each prospective pre-LOU. This prefix, which occupies the first four digits of the identifiers issued, is a way of ensuring their uniqueness. The Registro Mercantil began assigning codes with this prefix on 11 February 2014, and received the ROC's formal designation as a Pre-LOU on 5 March. What this signifies is that all the pre-LEIs issued by the Registro Mercantil will be automatically accepted by all other authorities belonging to the ROC for the purpose of complying with existing regulatory requirements.[1] And also, that any entity holding a pre-LEI code from another jurisdiction can, if it chooses, apply for it to be transferred to the Registro Mercantil.

This project is framed in Europe by EU rules, in force as of 12 February 2014, specifying that the counterparties in derivative transactions must furnish a series of data to trade repositories and be unequivocally identified through the medium of a LEI code, as laid down in Regulation (EU) No. 648/2102 of the European Parliament and of the Council[2] and its implementing measures.

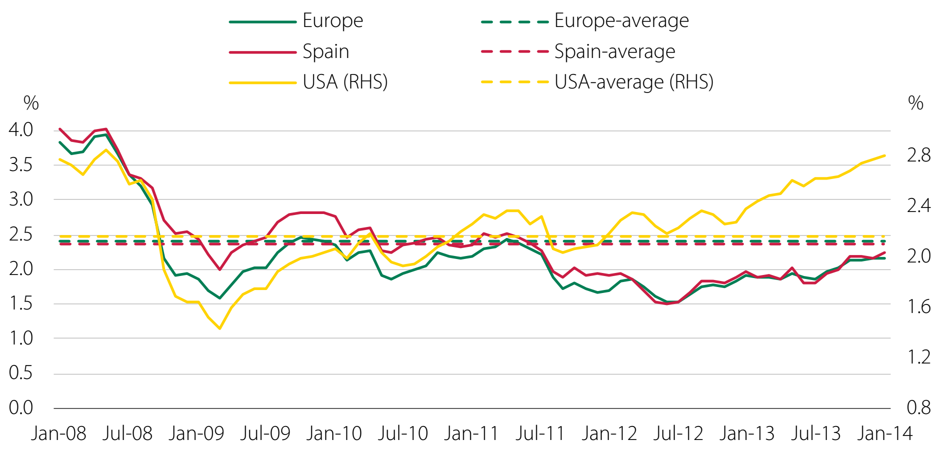
1 Further information on how to apply to the Registro Mercantil for pre-LEI codes can be found at https://www.lei.mjusticia.gob.es/es

2 Known as the EMIR.

The price/earnings ratio (P/E) of the Ibex 35, which escalating share prices had powered higher (from 11.7 to 14.2) in the second half of 2013, kept up its advance over the first quarter of 2014 as far as mid-March levels of 15.3. On a broader time frame, this earnings multiple is now zeroing in on its historical average in both its traditional formulation[8] and the more sophisticated cycle-related version[9] charted in figure 12. This performance is approximately echoed by other European indices, in contrast to certain US indices whose P/E (cycle-adjusted or otherwise) stands substantially above the average of recent years.

The P/E of the Ibex 35 climbs to levels testing its historical average.

Cycle-adjusted P/E[1] of representative stock market indices in the United States, euro area and Spain FIGURE 12



Source: Thomson Datastream and CNMV. Data to 31 January 2014.

1 The figure shows a monthly P/E adjusted using the Kalman filter, which splits the series into its cyclical and trend component. Units stated in terms of standard deviation. Monthly averages from March 1987 to January 2014 for representative indices in the United States, euro area and Spain. The index is constructed following the methodology put forward in the ESMA report.[10]

The earnings yield gap, which reflects the return premium required to be invested in equity versus long-term government bonds, narrowed sharply (from 4% to 2.8%) between mid-2013 and January 2014, as escalating P/E ratios more than offset the drop in sovereign yields. In mid-March, the gap widened again to 3.3%, in line with its historical average since 1999 (3.2%), on the levelling-off of share prices and consistently falling long bond yields. Note that not since the start of the financial crisis had this indicator come anywhere near its historical readings (see also the case of P/Es).

After narrowing significantly in second-half 2013, the equity risk premium settles in March at close to its historical average.

Ibex 35 volatility readings have kept up the settled levels of recent months, within a band running from 10% to 25%. The only incident of note was a small upswing at the end of January, when share prices dipped on the instability affecting certain emerging markets (see figure 13).

Despite a small upswing at the end of January, Ibex 35 volatility remains subdued…

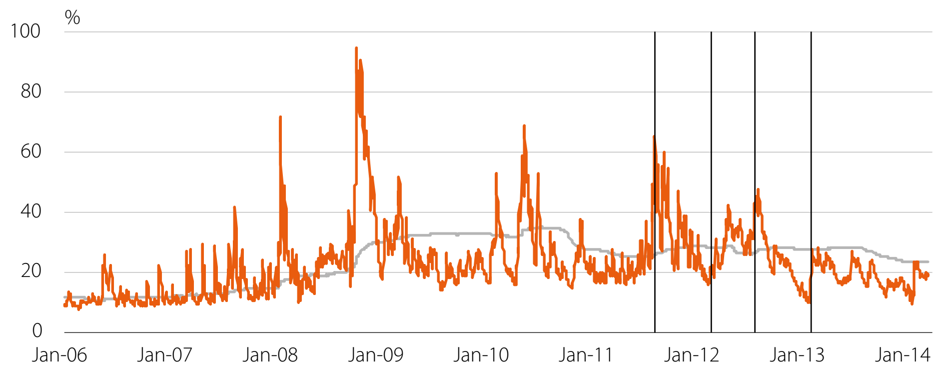
8 Calculated as the ratio between share price and expected earnings per share (based on historical earnings on some occasions).

9 A more detailed explanation is provided in the footnote to figure 12.

10 ESMA (2013). *Trends, Risks and Vulnerabilities No. 2*, September. Available from http://www.esma.europa.eu/system/files/2013-1138_trends_risks_vulnerabilities_no._2_2013_0.pdf

Historical volatility of the Ibex 35

FIGURE 13



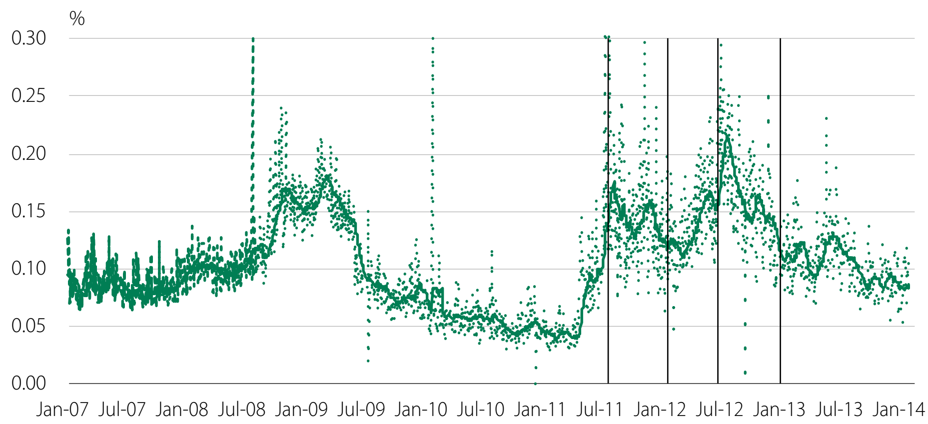
Source: Thomson Datastream and CNMV. Data to 14 March. The red line shows conditional volatility and the grey line unconditional volatility. The vertical lines refer to the introduction and lifting of the short-selling ban running from 11 August 2011 to 16 February 2012, and the later ban starting on 23 July 2012 and ending on 1 February 2013.

…while liquidity continues to improve.

Improvement in Ibex 35 liquidity conditions carried over into this year's opening months, as evidenced by the small decrease in the bid-ask spread. This indicator has been heading lower almost uninterruptedly since mid-2012 and by end-March was down to 0.08%, below the 0.11% of the 2013 close and in line with its historical average since 2003 (see figure 14).

Ibex 35 liquidity. Bid-ask spread

FIGURE 14

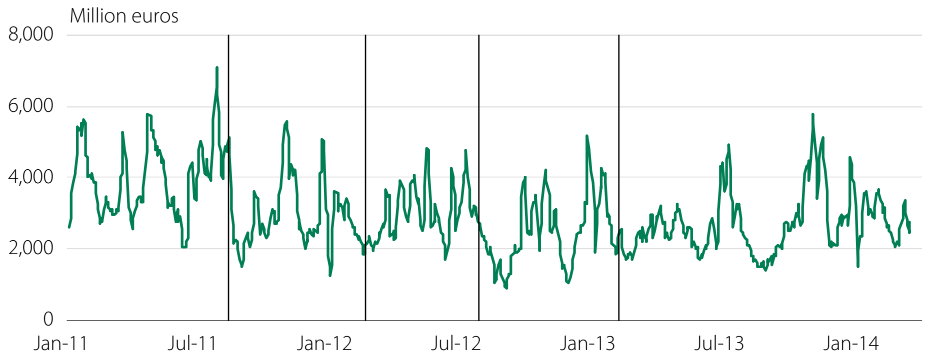


Source: Thomson Datastream and CNMV. Data to 14 March. The curve represents the bid-ask spread of the Ibex 35 along with the average of the last month. The vertical lines refer to the introduction and lifting of the short-selling ban running from 11 August 2011 to 16 February 2012, and the later ban starting on 23 July 2012 and ending on 1 February 2013.

Trading on national exchanges surged by 16.6% in the first quarter, an increase matched by Spanish share trades in non-domestic venues.

Trading volumes on Spanish stock markets swelled by 16.6% year on year to 155 billion euros in the first quarter of 2014. The daily average, at just under three billion euros, was slightly down versus last year's closing months but sizeably above the average figure for both 2013 (2.76 billion) and 2012 (2.73 billion). This upswing in trading in Spanish stocks, in contrast to the dwindling volumes of the past few years, was mirrored moreover on other regulated markets, MTFs and alternative trading platforms. As we can see from table 7, trades in non-domestic venues summed 23.77 billion euros in the first quarter of 2014, giving them a 13.8% share of the total amount (10.1% en 2013). Among the most prominent of these alternative venues were Chi-X and BATS.

Daily trading on the Spanish stock market[1] FIGURE 15



Source: CNMV. Data to 14 March 2014. The vertical lines refer to the introduction and lifting of the short-selling ban running from 11 August 2011 to 16 February 2012, and the later ban starting on 23 July 2012 and ending on 1 February 2013.

1 Moving average of five trading days.

Trading in Spanish shares listed on Spanish exchanges[1] TABLE 7

Million euros	2010	2011	2012	2013	1Q14[3]
Total	**1,030,498.6**	**926,873.7**	**709,902.0**	**764,986.6**	**172,839.4**
Listed on SIBE (electronic market)	**1,030,330.2**	**926,828.6**	**709,851.7**	**764,933.4**	**172,818.9**
BME	1,020,063.2	912,176.9	687,456.1	687,527.6	149,047.9
Chi-X	8,383.6	11,120.3	16,601.3	53,396.7	17,341.4
Turquoise	269.1	707.7	3,519.6	11,707.9	1,904.0
BATS	272.4	1,276.4	2,261.9	10,632.1	3,587.0
Others[2]	1,341.9	1,547.3	12.8	1,669.2	938.6
Open outcry	**165.4**	**42.8**	**49.9**	**51.4**	**20.3**
Madrid	15.7	16.1	3.0	7.3	0.9
Bilbao	3.9	0.1	8.5	0.1	14.2
Barcelona	143.9	26.4	37.7	44.1	5.1
Valencia	1.9	0.3	0.7	0.0	0.0
Second market	**3.0**	**2.3**	**0.4**	**1.7**	**0.2**
Pro memoria					
BME trading of foreign shares[1]	6,415	5,206	4,102	5,640	2,090
MAB	4,147.9	4,379.9	4,329.6	5,896.3	1,662.6
Latibex	521.2	357.7	313.2	367.3	115.5
ETFs	5,968.2	3,495.4	2,736.0	4,283.9	2,276.6
Total BME trading	1,037,284.3	925,661.3	698,987.5	703,768.7	155,213.5
% Spanish shares on BME vs. total SIBE	99.0	98.4	96.8	89.9	86.2

Source: Bloomberg and CNMV.

1 Spanish shares listed on Spanish exchanges are those with a Spanish ISIN that are admitted to trading in the regulated market of Bolsas y Mercados Españoles, i.e., not including alternative investment market MAB. Foreign shares are those admitted to trading in the regulated market of Bolsas y Mercados Españoles whose ISIN is not Spanish.

2 Difference between the turnover of the EU Composite estimated by Bloomberg for each share and the turnover of the markets and MTFs listed in the table, i.e. including trading on other regulated markets, MTFs and OTC systems.

3 Data to 14 March.

Equity issuance contracts 40% in the first quarter, with two IPOs as the main events.

Equity issuance on domestic markets amounted to almost 4.60 billion euros in the first quarter of 2014, 39.4% less than in the year-ago period. Around 91% of this total corresponded to just six companies: Banco Santander, Banco Popular, Iberdrola, Repsol, Lar España Real Estate, Socimi and Hispania Activos Inmobiliarios. The last two cases were initial public offerings (IPOs) timed to take advantage of the period's more buoyant markets (two similar operations are currently in the pipeline). Together, the financial institutions on the list raised more than 2.50 billion euros, while capital increases to cover scrip dividend payments accounted for 57% (2.63 billion) of the quarterly total (see table 8).

Capital increases and public offerings

TABLE 8

	2010	2011	2012	2013	3Q13	4Q13	1Q14[1]
CASH AMOUNTS (million euros)	**17,542.4**	**20,970.3**	**29,557.4**	**39,171.9**	**8,010.3**	**4,982.5**	**4,589.7**
Capital increases	16,932.8	20,843.3	28,326.0	39,171.9	8,010.3	4,982.5	4,589.7
Of which, scrip dividend alternative	2,021.2	3,862.0	8,357.8	9,869.4	2,607.9	2,466.6	2,629.4
Of which, through IPO	958.7	6,238.8	2,457.3	1,744.6	689.8	0.0	900.0
National tranche	61.6	5,827.1	2,457.3	1,744.6	689.8	0.0	98.7
International tranche	897.2	411.7	0.0	0.0	0.0	0.0	801.3
Public offering of shares	609.5	127.0	1,231.4	0.0	0.0	0.0	0.0
National tranche	79.1	124.7	1,231.4	0.0	0.0	0.0	0.0
International tranche	530.4	2.3	0.0	0.0	0.0	0.0	0.0
NUMBER OF FILINGS	**69**	**90**	**106**	**159**	**43**	**49**	**33**
Capital increases	66	90	103	159	43	49	33
Of which, bonus issues	16	24	24	38	13	7	6
Of which, through IPO	11	8	7	6	3	0	2
Public offering of shares	3	1	3	0	0	0	0
NUMBER OF ISSUERS	**46**	**44**	**39**	**47**	**27**	**23**	**21**
Capital increases	45	44	39	47	27	23	21
Of which, through IPO	11	8	7	6	3	0	2
Public offering of shares	2	1	3	0	0	0	0

Source: CNMV.

1 Data to 15 March 2014.

CNMV's adoption of ESMA guidelines on the assessment of interoperability arrangements between central counterparties

EXHIBIT 4

On 10 June 2013, the European Securities and Markets Authority (ESMA) published a consultation paper[1] on the European Market Infrastructures Regulation (EMIR),[2] in order to clarify the responsibilities of the competent national authorities in defining standards and requirements for existing or new interoperability arrangements between central counterparties (CCP). Central counterparties enter into this type of agreement so users are able to execute trades with counterparties choosing a different CCP. On 12 September, the CNMV announced its intention to adopt the ESMA guidelines and recommendations.

The EMIR stipulates that, as of 2013, all CCPs must seek authorisation to operate in the European Union. And the rigor and uniformity provided by common guidelines or standards for CCP interoperability arrangements will serve to promote "equal conditions of competition" for clearing activity in the internal market.

The guidelines provide a checklist for national competent authorities to assess interoperability arrangements in the interests of their safety and prudent management. The report, specifically, outlines five areas which the regulator should verify:

1. **Legal risk**

   In order to properly manage and mitigate legal risk, it is vital that all rights and obligations arising from interoperabilty arrangements, and all processes and procedures followed by CCPs, can be easily identified at any time. National competent authorities should accordingly assess that the interoperability arrangement is clearly defined, transparent, valid and enforceable in all relevant jurisdictions.

2. **Fair and open access**

   The future expansion of interoperability arrangements to other CCPs may not be restricted other than on grounds of risk, which should also be considered sufficient grounds for the arrangement's termination. To this end, national authorities should check that denial or restrictions on entering into an interoperability arrangement are based exclusively on risk grounds.

3. **Risk identification, monitoring and management**

   These functions are critical to ensure the prudent management of the interoperability arrangement and thereby guarantee the safety of interoperable CCPs, whose agreements mean they end up sharing exposures. National competent authorities should assess that a CCP has put in place a general framework to identify, monitor and manage the potential risks before entering into an interoperability arrangement and thereafter on a regular basis.

4. **Deposit of collateral**

   Collateral should be ring-fenced and available in all circumstances, including upon the default of an interoperable CCP. National competent authorities should assess that an interoperable CCP deposits collateral in a way that satisfies these conditions.

5. **Cooperation**

   Cooperation between national competent authorities is considered vital to ensure a smooth approval process for interoperability arrangements.

The report includes two annexes, the first comprising the relevant excerpts from the EMIR, and the second a cost/benefit analysis.

1 Report available from http://www.esma.europa.eu/system/files/2013-323_annex_1_esma_final_report_on_guidelines_on_interoperability.pdf
http://www.esma.europa.eu/es/system/files/esma_2013_00080000_es_tra.pdf (Spanish version)

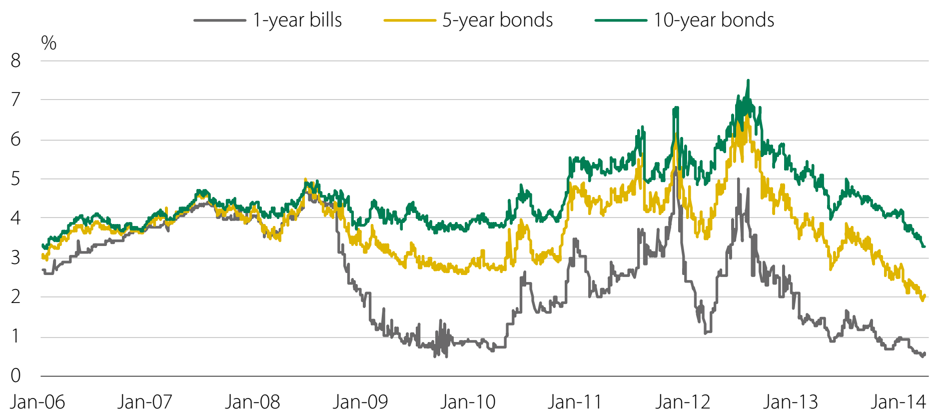
2 Regulation (EU) No. 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties and trade repositories.

3.2 Fixed-income markets

The dying-down of European debt market tensions and lesser perceptions of country risk prolong the period of calm in domestic fixed-income markets.

Spanish fixed-income markets again felt the benefit of dwindling debt market tensions and inflation expectations in Europe, along with decreased perceptions of country risk. Heavy government bond purchasing in the first quarter by resident and non-residents investors helped to further ease the financing conditions of domestic borrowers. Public and private debt yields and sovereign spreads prolonged their now lengthy downward trend while contagion indicators stayed subdued (see figures 16, 17 and 18). Rating agency Moody's weighed all these factors in its late February upgrade of Spanish debt from Baa3 to Baa2 (with a positive outlook). This upward revision, the first since the eruption of the sovereign debt crisis, endorses the country's changing macroeconomic and financial outlook.

Spanish government debt yields FIGURE 16



Source: Thomson Datastream. Data to 14 March.

Yields continue heading lower in short-dated instruments…

Against this backdrop, short-term treasury yields closed the year at 0.54%, 0.70% and 0.91% in three-month, six-month and twelve-month tenors respectively, then went on falling over the first quarter of 2014 as far as March averages of 0.25%, 0.40% and 0.54% (see table 9). This first-quarter decrease was fairly evenly paced across curve segments, in the range of 29 bp to 37 bp. Private debt instruments broadly mirrored the downtrend, which has continued, almost without interruption, since the end of 2012. Hence commercial paper yields, which fell more swiftly in the first half of 2013, continued heading lower, at the long end primarily, over the first months of 2014 (with average falls of 15 bp).

…and in longer maturities, for both public and private borrowers.

Medium and long-term bond yields moved sharply lower in the opening months in both the public and the private sector. As we can see from table 10, the average March rates of three, five and ten-year government bonds were 1.3%, 2.0% and 3.3% respectively, substantially below the year-end levels of 2011, 2012 and 2013. Long corporate bond yields also decreased as far as 2.0%, 2.3% and 3.7% in three, five and ten-year tenors respectively, to stand an average 4.7 points below the peak levels of mid-2012.

Short-term interest rates[1] (%) TABLE 9

	Dec 11	Dec 12	Dec 13	Sep 13	Dec 13	Mar 14[3]
Letras del Tesoro						
3 month	2.20	1.14	0.54	0.26	0.54	0.25
6 month	3.47	1.68	0.70	0.92	0.70	0.40
12 month	3.27	2.23	0.91	1.23	0.91	0.54
Commercial paper[2]						
3 month	2.74	2.83	1.09	1.28	1.09	0.94
6 month	3.52	3.58	1.36	1.49	1.36	1.25
12 month	3.77	3.83	1.59	1.77	1.59	1.39

Source: Thomson Datastream and CNMV.

1 Monthly average of daily data.

2 Interest rates at issue.

3 Data to 14 March.

Medium and long bond yields[1] (%) TABLE 10

	Dec 11	Dec 12	Dec 13	Sep 13	Dec 13	Mar 14[2]
Government bonds						
3 year	4.01	3.40	2.00	2.45	2.00	1.28
5 year	4.65	4.22	2.68	3.21	2.68	2.00
10 year	5.50	5.33	4.14	4.42	4.14	3.35
Corporate bonds						
3 year	5.43	4.19	2.63	2.71	2.63	1.96
5 year	5.91	4.66	2.84	3.58	2.84	2.26
10 year	8.06	6.79	4.46	5.26	4.46	3.70

Source: Thomson Datastream, Reuters and CNMV.

1 Monthly average of daily data.

2 Data to 14 March.

Sovereign spreads continued to tighten in the year's opening stretch…

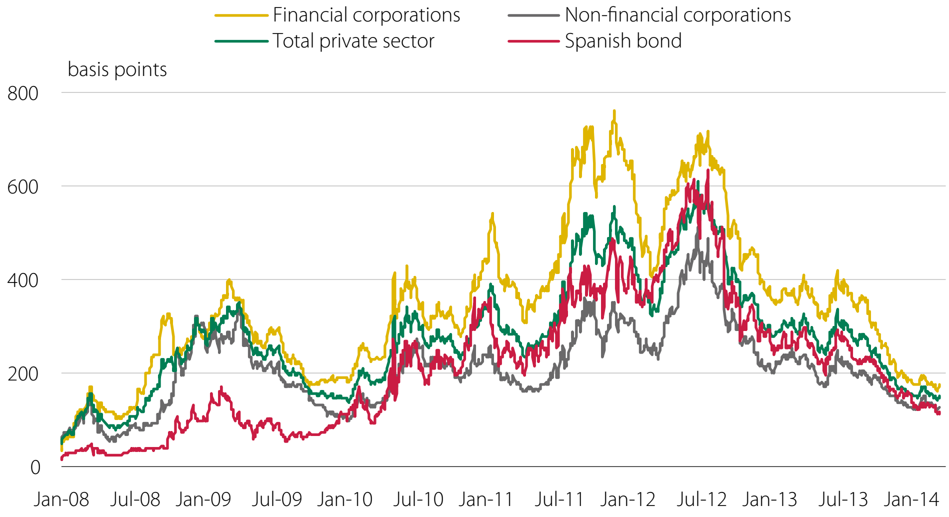
Spain's sovereign risk premium, as derived from five-year CDS spreads and the yield spread between the Spanish and German benchmarks, held to a narrowing trend over the first quarter of 2014, in tune with the better risk tone of domestic debt markets and an improved macroeconomic outlook. CDS spreads, specifically were down to 115 bp by mid-March compared to 153 bp at the 2013 close (see figure 17), while the Spanish/German spread narrowed in the period from 220 bp to 180 bp.

…while the narrowing movement in corporate spreads was accompanied by a gathering convergence between financial and non-financial issuers.

Corporate bond spreads inched higher in January only to fall back thereafter, with financial paper to the fore. The average CDS spreads of Spanish corporate borrowers narrowed from 158 bp at the 2013 close to 154 bp in mid-March, just slightly above the sovereign CDS (see figure 17). Note that the average credit spreads of financial and non-financial issuers have increasingly converged with respect to the 400 bp gap observable at the height of market turbulence. So while the average CDS spreads of financial corporations dropped from 186 bp in December last to mid-March levels of 178 bp, those of non-financial corporations held broadly flat at just under 130 bp.

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

FIGURE 17

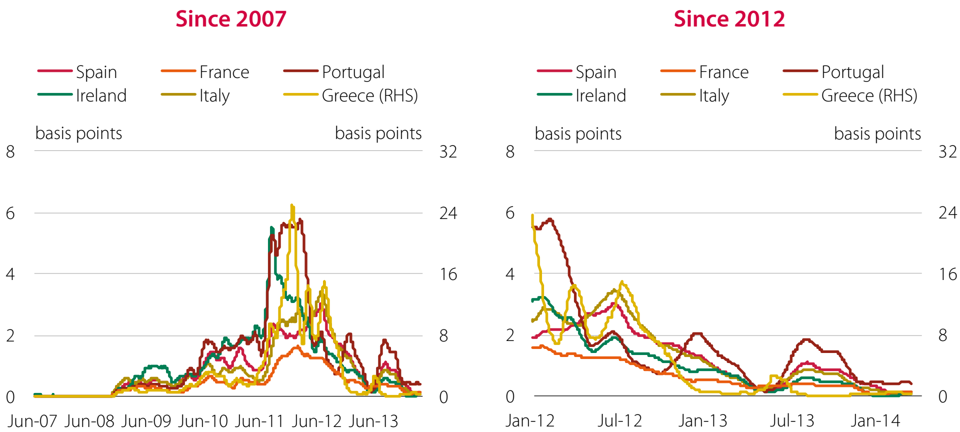


Source: Thomson Datastream and CNMV.

1 Simple average. Data to 14 March.

Indicators of sovereign credit risk contagion in the euro area[1]

FIGURE 18



Source: Thomson Datastream and CNMV. Data to 10 March 2014.

1 Defined as the impact on German sovereign CDS of contemporaneous shocks in the CDS of Spain, Italy, Ireland, Portugal, Greece and France equivalent to 1% of the CDS spread at that point in time. Results are the product of two components. The first measures the degree of contagion from one country to another taken as the percentage change in the German sovereign CDS that is exclusively explained by a contemporaneous variation in the CDS spread of one of the above six countries. This percentage is based on the decomposition of the variance of the estimated prediction error using an autoregressive vector model (ARV) with two variables – the impacted variable (change in the German sovereign CDS) and the shock-generating variable (change in the sovereign CDS of Spain, Italy, Ireland, Portugal, Greece or France) – and two retardations. Estimates are implemented through a moving window of the 100 periods prior to the first prediction period. The second component measures the credit risk of the shock emitter, as approximated from its CDS. Finally, the resulting series is smoothed using a moving average of 30 trading sessions.

Reduced funding needs drive issuance down by 61% despite the cheaper financing available…

Private-sector issuance activity slowed considerably in 2013, despite the easier financial conditions available, due to generally reduced funding needs, especially in the banking sector. Overall, the gross volume of fixed-income issues registered with the CNMV came to 138.84 billion euros, 61.2% less than in 2012 (see table 11).

Non-financial corporations again accounted for a small share of the annual total, but were considerably more active than in 2012, with non-resident subsidiaries, in particular, stepping up their issuance. Note also that inter-year comparison is distorted by the atypically high figures for 2012.[11] The shrinkage in issuance extended to all fixed-income products except asset-backed securities, whose sales climbed by 20.1%.

…a trend that has persisted through the first months of 2014.

Most of these trends persisted through the opening quarter of 2014, with issuance still contracting despite increasingly benevolent debt financing conditions. The volume of debt issues registered with the CNMV totalled 16.40 billion to mid-March, compared to the 40.80 billion euros of the same period in 2013.

The 28% decrease to March in commercial paper sales may be partially offset by higher issuance abroad.

Commercial paper sales dropped by 28% year on year to 6.65 billion euros. Among possible reasons, aside from lower borrowing needs, is that issuers are placing more short-term issues on foreign markets (see table 11) and/or are switching to longer-dated instruments in order to lock into lower rates.

Lower issuance of non-convertible bonds (traceable partly to the SAREB), asset-backed securities…

Issuance of non-convertible bonds and asset-backed securities also fell sharply in the opening quarter. Non-convertible bond sales to mid-March summed 5.65 billion, 64% less than in the same period in 2013, with some of the decline attributable to lower issuance by the SAREB.[12] Meantime, activity in asset-backed securities died down considerably, with the quarter's 1.85 billion paling in comparison to the 7.38 billion euros of the same period in 2013.

…and mortgage covered bonds.

Mortgage bond sales in the first quarter of 2014, at 2.25 billion euros, were 73% down vs. the year-ago period. No issues were reported of either territorial bonds (secured on loans to public authorities) or hybrid debt instruments (convertible bonds and preference shares).

International issuance also retreats due to reduced sales of longer-term instruments.

Finally, the 10.92 billion placed abroad by Spanish issuers to February 2014 represented a 16% decline with respect to the same period in 2013 (13.04 billion euros). The reduction owed exclusively to sales of longer-dated instruments, down by 34% to 7.22 billion, while short-term sales expanded from 2.09 billion to 3.71 billion euros.

11 For instance, government-backed issues summed 42.64 billion in 2012, but dried up entirely in 2013.

12 SAREB issues came to 14.09 billion in the first quarter of 2013 vs. 4.09 billion in the first quarter of 2014.

Gross fixed-income issues

TABLE 11

filed[1] with the CNMV	2010	2011	2012	2013	2013 3Q	2013 4Q	2014 1Q[2]
NUMBER OF ISSUES	**349**	**353**	**334**	**277**	**50**	**92**	**66**
Mortgage bonds	88	115	94	40	6	5	4
Territorial bonds	9	42	18	6	2	1	0
Non-convertible bonds and debentures	154	87	134	170	33	63	54
Convertible/exchangeable bonds and debentures	3	9	7	8	0	4	0
Asset-backed securities	36	45	35	33	3	14	3
Commercial paper facilities	59	53	46	20	6	5	5
Securitised	2	2	1	0	0	0	1
Other commercial paper	57	51	45	20	6	5	4
Other fixed-income issues	0	0	0	0	0	0	0
Preference shares	0	2	0	0	0	0	0
NOMINAL AMOUNT (million euros)	**226,449**	**288,992**	**357,830**	**138,839**	**21,545**	**42,425**	**16,399**
Mortgage bonds	34,378	67,227	102,170	24,800	6,015	2,250	2,250
Territorial bonds	5,900	22,334	8,974	8,115	4,000	2,500	0
Non-convertible bonds and debentures	24,356	20,192	86,442	32,537	172	12,633	5,647
Convertible/exchangeable bonds and debentures	968	7,126	3,563	803	0	363	0
Asset-backed securities	63,261	68,413	23,800	28,593	904	14,695	1,850
Domestic tranche	62,743	63,456	20,627	24,980	904	12,802	1,389
International tranche	518	4,957	3,173	3,613	0	1,893	461
Commercial paper[3]	97,586	103,501	132,882	43,991	10,455	9,983	6,652
Securitised	5,057	2,366	1,821	1,410	440	400	200
Other commercial paper	92,529	101,135	131,061	42,581	10,015	9,583	6,452
Other fixed-income issues	0	0	0	0	0	0	0
Preference shares	0	200	0	0	0	0	0
Pro memoria:							
Subordinated issues	9,154	29,199	7,633	4,776	92	2,149	0
Covered issues	299	10	0	193	0	0	196

abroad by Spanish issuers	2010	2011	2012	2013	2013 3Q	2013 4Q	2014 1Q[4]
NOMINAL AMOUNT (million euros)	**127,731**	**120,043**	**91,882**	**47,852**	**7,081**	**10,366**	**10,924**
Long-term	51,107	51,365	50,312	34,452	3,494	7,436	7,215
Preference shares	0	0	0	1,653	0	500	1,500
Subordinated debt	0	242	307	750	0	750	0
Bonds and debentures	50,807	51,123	50,005	32,049	3,494	6,186	5,715
Asset-backed securities	300	0	0	0	0	0	0
Short-term	76,624	68,677	41,570	13,400	3,587	2,930	3,708
Commercial paper	76,624	68,677	41,570	13,400	3,587	2,930	3,708
Securitised	248	322	11,590	0	0	0	0

Pro memoria: Gross issuance by subsidiaries of Spanish companies resident in the rest of the world

	2010	2011	2012	2013	2013 3Q	2013 4Q	2014 1Q[4]
NOMINAL AMOUNT (million euros)	**191,266**	**108,396**	**49,123**	**48,271**	**10,312**	**12,497**	**6,626**
Financial corporations	161,897	79,199	18,389	8,071	953	3,443	2,435
Non-financial corporations	29,369	29,197	30,734	40,200	9,359	9,053	4,192

Source: CNMV and Banco de España.

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

2 Data to 15 March.

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

4 Data to 28 February.

Rules and obligations of Regulation (EU) No. 648/2012 (EMIR)

EXHIBIT 5

Regulation (EU) No. 648/2012 of the European Parliament and of the Council on OTC derivatives, central counterparties (CCPs) and trade repositories (hereafter EMIR) came into force on 16 August 2012. Its obligations extend to all investors trading in derivatives, regardless of their degree of expertise and whether they are financial or non-financial corporations. Their force, however, tends to be proportional to the use made of derivative instruments and the corresponding volume of activity. Also, certain transactions are exempt from its provisions, such as the hedging of risks inherent to the conduct of a company's business and contracts entered into with counterparties within the same group. The regulatory technical standards supplementing EMIR and permitting its effective application are being drawn up by the European Securities and Markets Authority (ESMA). Most of these standards were published on 23 February 2013 and became effective on 15 March. European institutions continue to work on the remainder of EMIR's implementing measures, which mainly affect the exchange of collateral for non-centrally cleared derivatives.

Main requirements under the EMIR framework

1. CCP clearing will be mandatory for certain derivative contracts. The entry to force of this rule will depend on the final authorisation of CCPs and on whether the European authorities decide in favour of its application. At a rough estimate, it should become effective as of mid-2014. Meantime, non-financial counterparties exceeding any of the clearing thresholds set in the technical standards have been required to report this fact to the competent national authorities and ESMA since 15 March 2013.

2. All derivate contracts traded by financial and non-financial counterparties should be reported to trade repositories authorised or recognised by ESMA. This obligation accordingly starts with the existence of an ESMA-approved trade repository. On 7 November 2013, the European regulator authorised four entities to act as trade repositories, and the associated reporting requirement took effect on 12 February 2014.

3. Use of risk mitigation techniques for the trading of non-centrally cleared derivate contracts, including:

   – Timely confirmation of the terms of the contract and the existence of formalised processes for the early identification and resolution of disputes between the parties.

   – Portfolio reconciliation or compression, regular marking-to-market of contracts, and exchange of collateral, when certain clearing thresholds are exceeded.

   These obligations came into force on 16 August 2012. Note, however, that since 15 March 2013, the risk mitigation techniques used by financial and non-financial counterparties must comply in full with the technical standards published to date.

4. Establishment of stringent organisational, business conduct and prudential requirements to be complied with by CCPs.

   Issue of new ESMA rules for the authorisation and operation of trade repositories. On 7 November 2013, ESMA authorised the following EMIR trade repositories: four in the United Kingdom: CME Trade Repository Ltd. (CME TR), DTCC Derivatives Repository Ltd. (DDRL), ICE Trade Vault Europe Ltd. (ICE TVEL), UnaVista Ltd.; one in Poland: Krajowy Depozyt Papierów Wartosciowych S.A. (KDPW); and one in Luxembourg (Regis-TR S.A.), a joint venture between Clearstream and Iberclear.

Scope of application

All OTC derivate contracts – that is, derivative contracts the execution of which does not take place on a regulated market as defined by the MiFID – will be subject to central clearing requirements as of the date decided by the European authorities. In remaining cases, transactions should be subject to risk mitigation techniques.

All derivative contracts, whether traded OTC or on regulated markets, should be reported to a trade repository authorised or recognised by ESMA.

Financial counterparties are defined as: investment firms, credit institutions, insurance and reinsurance undertakings, UCITS and their management companies, pension funds enjoying certain temporary exemptions and alternative investment funds.

Non-financial counterparties are defined as any undertaking other than those listed above. Non-financial counterparties are deemed to have exceeded the clearing threshold when the gross notional value of their OTC derivative contracts is above one of the following limits, taken individually: one billion euros for credit and equity derivatives and three billion euros for derivatives based on foreign exchange, interest rates, commodities or any other underlying asset.

In aggregating the value of their contracts, non-financial counterparties should include all OTC derivative contracts entered into by them or entities within their group, other than those employed to reduce risks directly related to their commercial activity or treasury financing activity.

4 Market agents

4.1 Investment vehicles

Financial UCITS[13]

After five years of non-stop decline, investment funds grew their combined assets by 26.3% to 156.68 billion euros at the 2013 close (see table 13). Around three-quarters of the increase owed to net subscriptions, which summed over 24 billion in the full-year period (see table 12), with almost 15 billion entering in the second half. Fixed-income and passively managed funds were those registering the largest inflows (13.41 and 12.68 billion respectively), followed at a distance by balanced equity and balanced fixed-income products (2.67 and 2.37 billion euros respectively). The only categories experiencing net outflows were guaranteed funds, in both their fixed-income and equity variants, where net redemptions summed 6.72 and 2.69 billion euros respectively. This marks a sea change with respect to preceding years, when guaranteed funds, especially fixed-income products, attracted in most subscriptions at the expense of fixed-income funds.

After five years' decline, assets under management in investment funds expand 26% in 2013 on the strength of net unit-holder subscriptions…

Net investment fund subscriptions TABLE 12

				2013			
Million euros	2011	2012	2013	1Q	2Q	3Q	4Q
Total investment funds	**-10,853.1**	**-14,597.3**	**24,086.2**	**4,224.4**	**5,205.5**	**5,847.4**	**8,808.9**
Fixed income[1]	-10,423.6	-7,739.7	13,405.0	1,729.5	3,934.9	3,329.4	4,411.2
Balanced fixed income[2]	-1,980.4	-18.8	2,369.7	419.0	668.7	132.6	1,149.4
Balanced equity[3]	-375.5	35.8	2,673.3	349.0	315.7	668.0	1,340.6
Euro equity [4]	142.0	-115.4	1,733.5	275.0	104.6	328.0	1,025.9
International equity[5]	-796.0	-425.3	865.9	122.3	133.3	175.4	434.9
Guaranteed fixed-income guaranteed	7,809.3	-338.8	-6,717.5	537.8	-602.6	-2,334.0	-4,318.7
Guaranteed equity[6]	-4,053.9	-4,225.9	-2,689.1	-651.9	-952.7	-593.3	-491.2
Global funds	972.2	-1,021.0	-176.7	-61.0	-197.9	42.0	40.2
Passively managed[7]	60.8	823.8	12,675.2	1,477.0	1,851.1	4,150.7	5,196.4
Absolute return[7]	-2,207.9	-1,571.9	-53.2	27.7	-49.5	-51.4	20.0

Source: CNMV. Estimates only.

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

2 Includes: Euro and international balanced fixed income.

3 Includes: Euro and international balanced equity.

4 Includes: Euro equity.

5 Includes: International equity.

6 Includes: Guaranteed and partial protection equity funds.

7 New categories as of 2Q 09. Absolute return funds were previously classed as global funds.

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

Main investment fund variables*

TABLE 13

Number	2011	2012	2013	2013 1Q	2013 2Q	2013 3Q	2013 4Q
Total investment funds inversión	**2,310**	**2,185**	**2,045**	**2,185**	**2,117**	**2,070**	**2,045**
Fixed income[1]	508	454	384	448	408	388	384
Balanced fixed income[2]	140	125	122	126	129	125	122
Balanced equity[3]	128	117	128	120	124	128	128
Euro equity[4]	148	127	108	126	116	113	108
International equity[5]	220	211	193	209	198	192	193
Guaranteed fixed-income	351	398	374	409	402	391	374
Guaranteed equity[6]	420	361	308	348	336	316	308
Global funds	203	192	162	182	174	168	162
Passively managed[7]	59	85	169	103	126	148	169
Absolute return[7]	133	115	97	114	104	101	97
Assets (million euros)							
Total investment funds	**132,368.6**	**124,040.4**	**156,680.1**	**130,295.4**	**135,933.5**	**145,168.5**	**156,680.1**
Fixed income[1]	46,945.5	40,664.6	55,058.9	42,690.3	46,736.8	50,381.0	55,058.9
Balanced fixed income[2]	5,253.6	5,500.9	8,138.0	5,965.6	6,618.4	6,873.4	8,138.0
Balanced equity[3]	2,906.1	3,179.9	6,312.4	3,593.6	3,911.9	4,783.4	6,312.4
Euro equity[4]	4,829.2	5,270.2	8,632.8	5,691.8	5,867.8	7,021.5	8,632.8
International equity[5]	6,281.2	6,615.0	8,849.0	7,224.0	7,297.3	7,967.6	8,849.0
Guaranteed fixed-income	35,058.0	36,445.0	31,481.2	37,653.1	37,316.1	35,504.7	31,481.2
Guaranteed equity[6]	18,014.5	14,413.2	12,503.8	13,925.5	13,032.2	12,767,2	12,503.8
Global funds	5,104.7	4,358.6	4,528.1	4,366.9	4,157.3	4,352.8	4,528.1
Passively managed[7]	1,986.2	2,991.2	16,515.9	4,511.4	6,402.4	10,926.5	16,515.9
Absolute return[7]	5,989.7	4,601.9	4,659.9	4,673.3	4,593.4	4,590.4	4,659.9
Unit-holders							
Total investment funds	**4,835,193**	**4,410,771**	**5,050,719**	**4,523,140**	**4,646,619**	**4,799,719**	**5,050,719**
Fixed income[1]	1,384,946	1,261,634	1,508,009	1,283,052	1,347,295	1,410,867	1,508,009
Balanced fixed income[2]	206,938	188,574	240,676	194,084	203,705	205,034	240,676
Balanced equity[3]	145,150	138,096	182,223	140,132	141,715	161,099	182,223
Euro equity[4]	237,815	220,450	293,193	231,881	239,309	254,009	293,193
International equity[5]	448,539	398,664	457,606	409,552	427,789	435,571	457,606
Guaranteed fixed-income	1,042,658	1,075,852	1,002,458	1,114,875	1,124,209	1,091,051	1,002,458
Guaranteed equity[6]	912,298	727,880	608,051	703,587	655,760	628,100	608,051
Global funds	127,336	101,321	128,741	104,718	111,567	117,838	128,741
Passively managed[7]	100,416	125,003	441,705	170,399	224,481	321,669	441,705
Absolute return[7]	229,097	173,297	188,057	170,860	170,789	174,481	188,057
Return[8] (%)							
Total investment funds	**-0.08**	**5.50**	**6.50**	**1.65**	**0.36**	**2.50**	**1.85**
Fixed income[1]	1.56	3.54	2.28	0.76	0.31	0.65	0.54
Balanced fixed income[2]	-1.34	4.95	4.16	0.83	-0.19	1.85	1.62
Balanced equity[3]	-5.64	7.83	10.85	2.02	0.17	4.78	3.52
Euro equity[4]	-11.71	12.31	28.06	2.95	1.30	13.71	7.99
International equity[5]	-10.83	13.05	20.30	7.40	-0.69	6.87	5.54
Guaranteed fixed-income	3.28	4.85	4.96	1.82	0.70	1.46	0.89
Guaranteed equity[6]	0.14	5.07	6.15	1.16	0.42	2.62	1.83
Global funds	-4.64	7.44	8.71	1.70	-0.26	3.80	3.25
Passively managed[7]	-7.33	7.10	8.88	1.06	0.86	4.13	2.58
Absolute return[7]	-1.87	3.84	2.77	0.96	-0.32	1.07	1.04

Source: CNMV.

* 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 (as of 3Q 2011, money-market funds encompass those engaging in money market and short-term money market investments, Circular 3/2011).

2 Includes: Euro and international balanced fixed income.

3 Includes: Euro and international balanced equity.

4 Includes: Euro equity

5 Includes: International equity.

6 Includes: Guaranteed equity and partial protection equity funds.

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

8 Annual return for 2011, 2012 and 2013. Quarterly data comprise non-annualised quarterly returns.

Advancing returns provided a quarter of the increase in industry assets, with gains of 6.5% in the full-year period, and 4.4% in the second half (see table 13). In a year of rising stock markets, the strongest performers were euro equity and international equity funds, whose portfolios gained 28.1% and 20.3% respectively (22.8% and 12.8% in the last six months). Despite the expansion in their assets, fund numbers shrank once more in 2013, as management companies' prolonged drive to rationalise their offerings received fresh impetus from the restructuring of the Spanish financial system. At year-end, a total of 2,045 funds remained in operation, 140 fewer than at end-2012. Leading the decline were fixed-income and guaranteed equity funds, whose numbers dropped by 70 and 53 respectively. Passively managed funds were a notable exception, doubling their numbers from 85 at the 2012 close to 169 in 2013.

…and, in smaller measure, increased portfolio returns.

The industry's improved fortunes were also apparent in unit-holder numbers. These climbed by 640,000 to over five million at year-end 2013, with passively managed and fixed-income funds as the principal beneficiaries (an additional 317,000 and 246,000 unit-holders respectively). The sole exception was the guaranteed funds category, which lost 200,000 unit-holders overall in the course of 2013.

Unit-holder numbers climb to over five million at the 2013 close.

Preliminary data for January suggest the expansion trend has lasted into 2014. Assets under management are estimated to have risen by 2.4% in the month to 160.4 billion euros, accompanied by a 120,000 increase in unit-holder numbers to almost 5.2 million. Meantime, fund mergers have continued to take their course.

Preliminary data for January 2014 point to continuing expansion.

Estimated liquidity of investment fund assets TABLE 14

	Less-liquid investments					
	Million euros			% total portfolio		
Type of asset	**Jun 13**	**Sep 13**	**Dec 13**	**Jun 13**	**Sep 13**	**Dec 13**
Financial fixed income rated AAA/AA	210	185	177	21	18	18
Financial fixed income rated below AAA/AA	3,114	2,696	2,457	17	16	15
Non-financial fixed income	186	179	177	8	7	6
Securitisations	541	489	509	30	24	23
AAA-rated securitisations	35	31	33	99	100	100
Other securitisations	506	458	476	28	23	22
Total	**4,051**	**3,549**	**3,320**	**17**	**16**	**15**
% of investment fund assets	**3.0**	**2.5**	**2.1**			

Source: CNMV.

The liquidity conditions of fund fixed-income portfolios prolonged the improvement of the two previous years, with the amount of less-liquid assets down by two billion euros (700 million in the second-half period) to just over 3.30 billion (see table 14). On this showing, the ratio of less-liquid assets dropped from 4.4% of total fund assets in 2012 to 2.1% in 2013. Note also that the least liquid assets made up less of the total in both fixed-income and asset-backed securities.

A renewed decline in the balance of less-liquid assets as far as 2.1% of the industry total.

Real estate schemes

The ongoing adjustment in Spanish construction and real estate continued to weigh on the sector throughout 2013. That said, the year also saw a widening performance

In a year marked by the ongoing adjustment in Spanish real estate…

gap between funds, whose main variables continued in decline, and investment companies, which managed a solid advance.

…funds continued to struggle, with all main variables in decline…

The year ended with six real estate funds in operation, the same number as at end-2012. Only four, however, can be regarded as active, with the other two in the process of winding up. Main fund variables performed in line with the previous years, that is, with further decline in assets, investors and portfolio returns. Specifically, assets under management contracted 12.4% to less than 3.7 billion euros, while unit-holder numbers dropped below six thousand, a fall of 77.2%. The scale of this slide is due to investors in one fund redeeming their holdings in the fourth-quarter period, in the course of the last liquidity window preceding its de-merger. Fund returns, finally, were again negative in every quarter delivering an annual loss of 11.28% (see table 15).

…in contrast to real estate investment companies, which kept up their expansion trend.

Conversely, the number of real estate investment companies increased from eight to ten in 2013 (see table 15), accompanied by a leap in assets from 284 to 854 million euros between December 2012 and 2013. This increase, however, was exclusively due to the entry of one company, which changed its form in January 2013 from that of a public limited company. Shareholder numbers, finally, closed at 1,023, after an increase of 86.

Main real estate scheme variables[1] TABLE 15

					2013			
	2010	2011	2012	2013	1Q	2Q	3Q	4Q
FUNDS								
Number[1]	7	6	6	6	6	6	6	6
Unit-holders	75,280	29,735	25,218	5,750	24,048	21,541	21,466	5,750
Assets (million euros)	6,116	4,495	4,202	3,683	4,071	3,986	3,899	3,683
Return (%)	-4.74	-3.23	-5.53	-11.28	-2.59	-1.88	-2.13	-5.15
COMPANIES								
Number	8	8	8	10	9	10	10	10
Shareholders	943	943	937	1,023	1,021	1,017	1,018	1,055
Assets (million euros)	322	313	284	854	844	854	860	855

Source: CNMV.

1 Schemes filing financial statements.

Hedge funds

Funds of hedge funds lose further business in 2013, while hedge fund expansion falters.

This category includes both funds of hedge funds and hedge funds *per se*. By and large, the trends dominating the industry landscape throughout the crisis persisted over 2013, with the funds of hedge funds segment contracting sharply and the recent-year expansion in the hedge funds segment apparently running out of steam. Also, the number of schemes in operation fell from 60 to 51, with the fund of funds segment losing two competitors (both de-registrations) and the pure hedge funds segment losing seven (ten de-registrations and three new entries). A significant number of funds were in the process of liquidation at the end of the year (13 funds of hedge funds and three hedge funds).

Fund of hedge fund assets fell by 21.6% to 423 million euros in the first 11 months of 2013, while unit-holder numbers decreased by 6.7% to 3,114 (see table 16). Despite this contraction, portfolio returns in the same period were a positive 4.2%.

Funds of hedge funds lose 22% of their assets but manage positive returns…

Pure hedge funds, by way of contrast, grew their assets 10.9% to over one billion euros between December 2012 and November 2013, with expansion driven by both net subscriptions and a surge in portfolio returns (14.6%) that was most intense from July to November (9.4%). Unit-holder numbers, finally, slipped by 1.8% to close the year at 2,383.

…while hedge funds grow their assets 11% on net subscriptions and portfolio gains.

Main hedge fund and fund of hedge fund variables TABLE 16

				2013			
	2010	2011	2012	1Q	2Q	3Q	4Q[2]
FUNDS OF HEDGE FUNDS							
Number[1]	28	27	24	24	22	22	22
Unit-holders	4,404	3,805	3,338	3,211	3,230	3,218	3,114
Assets (million euros)	694.9	573.0	540.0	536.2	468.0	418.3	423.3
Return (%)	3.15	-1.70	0.60	2.73	-0.52	0.25	1.75
HEDGE FUNDS							
Number[1]	33	36	36	33	33	33	29
Unit-holders	1,852	2,047	2,427	2,384	2,374	2,323	2,383
Assets (million euros)	646.2	728.1	918.6	964.8	981.3	993.2	1,018.7
Return (%)	5.37	-2.60	3.03	3.72	1.03	5.34	3.81

Source: CNMV.

1 Schemes filing financial statements.

2 Data to November 2013.

Foreign UCITS marketed in Spain

This segment kept up the strong expansion initiated in 2012, with a fresh surge that propelled assets under management to almost 55 billion euros, an increase of 43.7%. Both funds and companies shared in the advance with growth of 35.9% and 45.3% as far as 8.5 and 46 billion euros respectively. Investor numbers topped the one million mark after climbing 30.3% in the year. Finally, the number of companies rose by a hefty 39 to 372, while fund numbers declined by 13 to 408.

Foreign UCITS marketed in Spain grow their assets 44% in 2013, as far as 55 billion euros.

Outlook

It appears that the collective investment industry may finally be clear of the slump endured since the start of the crisis, whose principal symptom was a continuous outpouring of investor funds. This is especially true in the case of financial UCITS, whose key variables (assets and unit-holder numbers), to judge from the data available at the time of writing, have kept up their improvement through the first months of 2014. A series of factors could help sustain the recovery going forward, particularly investors' renewed confidence in this kind of product now financial markets have effectively stabilised. Support may also come from the fading appeal of other lower-risk investment products like bank deposits, whose yields have been declining in the past few months.

Hope for a firming recovery in 2014 as investors regain confidence in collective investment products.

ESMA opinion on investment firm practices in the sale of complex products

EXHIBIT 6

On 7 February 2014, ESMA issued an opinion pursuant to the terms of article 29, paragraph 1, point (a) of Regulation (EU) No. 1095/2010 setting out the minimum standards of conduct it would expect from firms selling complex products. ESMA expressed concern that although the existing requirements of the Investment Services Directive (MiFID) should be sufficient to this purpose, it appeared that compliance with conduct of business rules may have fallen short in some cases. Accordingly, without prejudice to any other legislative initiatives, ESMA has delivered this opinion to remind supervisors about the relevant MiFID provisions governing selling practices, which they should monitor with special care in the course of their supervisory duties.

The opinion covers a series of points regulated in the MiFID, with special attention to the following:

- **Organisation and internal controls.** Firms should implement adequate internal controls over product development. If analysis reveals that a particular product will never meet clients' best interests, or there is insufficient information to determine its real features and risks, the product in question should not be recommended or sold. Firms should ensure that those responsible for establishing the target market, drafting marketing material and providing financial services to clients fully understand the nature and workings of complex products, and that staff are properly trained in their use. They should also weigh up whether complex products should be sold on an advised or a non-advised basis. ESMA urges firms to identify and manage possible conflicts of interest, especially when the selling entity is the issuer or is acting as the counterparty of the transaction. In particular, the compliance function should check whether incentives relating to the product (including remuneration) create conflicts of interest, with special attention to whether such incentives are more lucrative than those for standard investments.

- **Assessment of the product's suitability for the client.** Firms should carry out a detailed evaluation of the product before deciding to recommend it. They should also consider the degree of additional information to be sought from clients, over and above that required for less complex products, so they can correctly assess their ability to understand the investment and bear the related risks. As examples of the kind of data firms should gather, the report suggests investment objectives and attitude to risk, the investment time horizon, and whether the client can afford potential investment losses and foreseeable future commitments as well as the charges and costs involved, all the time considering the possibility that an alternative, cheaper and less complex investment might better serve his or her needs. Firms should also guard against being over-reliant on clients' self-assessment, and ensure that the information they have is correct and up-to-date. At the sale stage, firms using standardised processes to assess appropriateness should not use this process as a self-certifying exercise. Finally, when a firm judges that a product is not appropriate or lacks sufficient information, yet is still making it available, ESMA stresses that it should warn the client specifically that he or she is unlikely to understand the risks involved.

– **Disclosure.** All communication to the client should be fair, clear and not misleading. ESMA insists particularly that clients should be informed of the total amount of applicable costs and charges (to include estimated cash values, impact on investment performance and an indication of disinvestment value immediately after the transaction), as well as the potential consequences of seeking to sell or exit early. It also lays down certain principles firms should follow in explaining products to their clients, with reference, for instance, to the impact of any leveraging or embedded derivatives, and the scope and nature of any guarantee or capital protection. Finally, non-advised sales of complex products should be accompanied by a clear and specific warning on their main risk characteristics.

– **Monitoring and assessment**. The sale of complex products should be identified as a priority for firms' compliance function – the more complex the product the greater the scrutiny. Assessments should also focus on the issues brought up in customer complaints.

4.2 Investment firms

The better performance of financial markets through 2013…

The greater buoyancy of financial markets in 2013 provided a more favourable climate for the investment firm sector, whose aggregate earnings responded accordingly. The year ended with 82[14] firms, five fewer than in 2012, listed on the CNMV registers, which also recorded six changes of control (affecting four broker-dealers and two brokers). The number of operators engaging in cross-border business was practically unchanged with respect to the previous year, with seven passported to operate in other EU countries via a branch and 40 doing so under the free provision of services (one fewer than in 2012). It bears mention too that 284 firms registered in other Member States informed the CNMV in 2013 of their intention to provide investment services in Spain (most of them under the free provision of services).

…powers investment firm earnings four times higher to 217 million euros.

Investment firms reported aggregate pre-tax profits of 217.4 million euros in 2013 (see figure 19), four times more than the figure for 2012 (50.1 million euros). Note that the scale of increase here is due to one broker-dealer's 2012 losses, without which the difference drops to a more modest 19%.

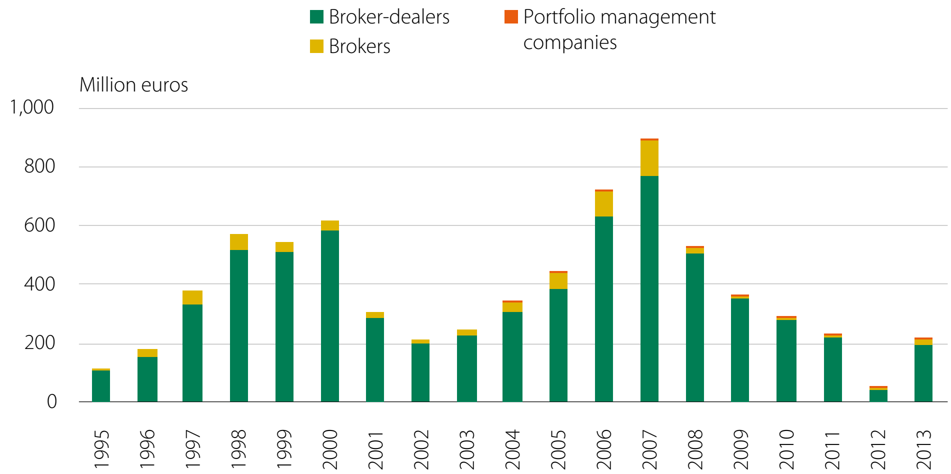
Broker-dealer profits are boosted by income from financial investments and lower depreciation charges and asset impairment losses.

The pre-tax profits of broker-dealers, which accounted for almost 90% of the sector total, stood almost 153 million higher than in 2012 at 194.5 million euros. Improvement was driven by higher net inflows at some income statement lines – outstandingly the results of financial investments – coupled with falling depreciation charges and financial asset impairment losses. Gross income rose by 27.8% in aggregate terms to 572 million euros, though not all items contributed to the same extent,

14 Excluding investment advisory firms, which are dealt with separately in a later section in view of their different characteristics.

while both income from financial investments and net interest income climbed sharply in the year. However, firms also registered copious exchange losses, while fees on investment services, broker-dealers' biggest earning item above the gross income line, receded 3.9% to 565.8 million euros. Operating expenses, finally, increased by 2.3% to 384.6 million euros.

Investment firm pre-tax profits[1] FIGURE 19



Source: CNMV.

1 Except investment advisory firms.

Brokers too manage to grow their profits on the revival of fee income from investment services and operating cost contention.

Brokers managed pre-tax profits of 19.3 million euros, substantially ahead of the less than seven million reported in 2012. By contrast to broker-dealers, fee inflows were the main source of this improvement, with net fee income from the provision of investment services up by 18.4% vs. the previous year to 130.7 million euros. Importantly, all key investment services played a part in the advance, with order processing fees up by 5.5%, UCITS marketing fees up 38.1%, portfolio management fees up 12.4%, and those from investment advice and issue placement and underwriting swelling by 85% and 50.7% respectively (see table 17). Overall, brokers' gross margin closed the year at 110.6 million euros, 16.5% more than in 2012, while operating expenses rose by a subdued 2.4% to 89.7 million euros.

Portfolio management companies also raise their earnings thanks to fee income growth and lower operating expenses.

Finally, the aggregate pre-tax profits of portfolio management companies closed the year at 3.56 million, almost two million euros more than in 2012 (see table 17). Behind the advance was a sturdy increase in net fee income (up by 18.8%) accompanied by a 10.3% reduction in operating expenses. Portfolio management companies, whose numbers, according to CNMV registers, were down to five at the 2013 close,[15] have endured growing competition in recent years from the likes of investment advisory firms and UCITS management companies.

15 Compared to the more than 20 registered in 2004.

Aggregate income statement (Dec 13)

TABLE 17

	Broker-dealers			Brokers			Portfolio managers		
Thousand euros	Dec 12	Dec 13	% var.	Dec 12	Dec 13	% var.	Dec 12	Dec 13	% var.
1. Net interest income	56,161	67,333	19.9	1,912	1,799	-5.9	733	667	-9.0
2. Net fee income	410,740	387,216	-5.7	93,246	110,422	18.4	7,879	9,362	18.8
2.1. Fee income	589,027	565,787	-3.9	108,198	130,738	20.8	17,887	18,603	4.0
2.1.1. Order processing and execution	348,403	347,522	-0.3	38,112	40,196	5.5	–	–	–
2.1.2. Issue placement and underwriting	6,869	4,824	-29.8	3,128	4,715	50.7	–	–	–
2.1.3. Securities custody and administration	19,775	17,987	-9.0	576	505	-12.3	–	–	–
2.1.4. Portfolio management	14,883	15,581	4.7	14,476	16,267	12.4	16,307	17,028	4.4
2.1.5. Investment advising	5,137	10,500	104.4	3,092	5,707	84.6	1,579	1,575	-0.3
2.1.6. Search and placement	50	8,659	17,218.0	88	55	-37.5	–	–	–
2.1.7. Margin trading	8	22	175.0	30	11	-63.3	–	–	–
2.1.8. UCITS marketing	45,050	51,766	14.9	25,949	35,823	38.1	0	0	–
2.1.9. Others	148,854	108,926	-26.8	22,746	27,459	20.7	1	0	-100.0
2.2. Fee expense	178,287	178,571	0.2	14,952	20,316	35.9	10,008	9,241	-7.7
3. Result of financial investments	9,403	256,110	2,623.7	1,255	5	-99.6	4	9	125.0
4. Net exchange income	-37,363	-149,033	-298.9	-105	-237	-125.7	-30	-24	20.0
5. Other operating income and expense	8,841	10,566	19.5	-1,354	-1,396	-3.1	29	-8	–
GROSS INCOME	**447,782**	**572,192**	**27.8**	**94,954**	**110,593**	**16.5**	**8,615**	**10,006**	**16.1**
6. Operating expenses	376,019	384,638	2.3	87,587	89,726	2.4	7,122	6,388	-10.3
7. Depreciation and other charges	23,556	-609	–	2,781	2,420	-13.0	87	64	-26.4
8. Impairment losses	12,903	3,123	-75.8	-12	25	–	0	0	–
NET OPERATING INCOME	**35,304**	**185,040**	**424.1**	**4,598**	**18,422**	**300.7**	**1,406**	**3,554**	**152.8**
9. Other profit and loss	6,449	9,529	47.8	2,371	854	-64.0	5	9	80.0
PROFITS BEFORE TAXES	**41,753**	**194,569**	**366.0**	**6,969**	**19,276**	**176.6**	**1,411**	**3,563**	**152.5**
10. Corporate income tax	53,810	53,764	-0.1	3,386	4,955	46.3	458	1,091	138.2
PROFITS FROM ONGOING ACTIVITIES	**-12,057**	**140,805**	**–**	**3,583**	**14,321**	**299.7**	**953**	**2,472**	**159.4**
11. Profits from discontinued activities	0	0	–	0	0	–	0	0	–
NET PROFIT FOR THE YEAR	**-12,057**	**140,805**	**–**	**3,583**	**14,321**	**299.7**	**953**	**2,472**	**159.4**

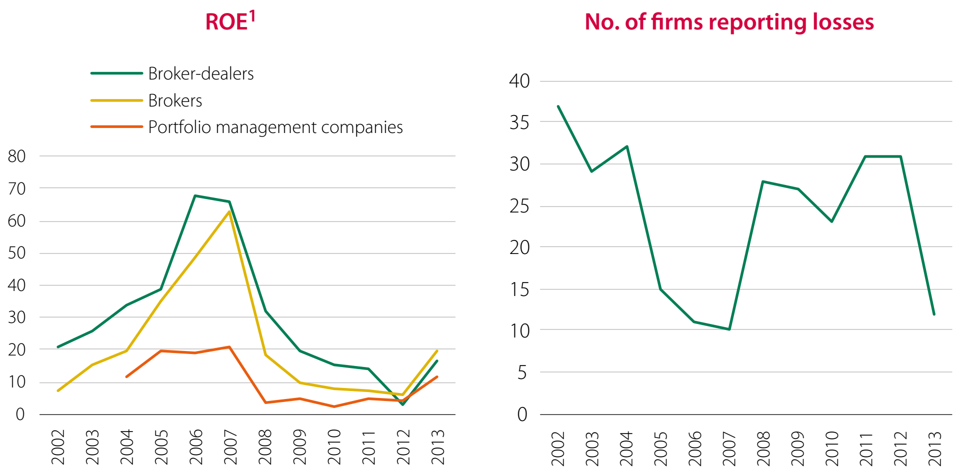
Source: CNMV.

The investment sector's profits growth in 2013 boosted profitability ratios while making sizeable inroads into the number of loss-making firms. Hence the return on equity (ROE) of broker-dealers jumped from 3% in 2012 to 16.4% in 2013, that of brokerage firms from 6.3% to 19.3% and that of portfolio management companies from 4.2% to 11.4%. The number of firms reporting losses dropped from 31 in December 2012 to 12 at the 2013 close, of which five were broker-dealers (15 in 2012) and seven brokers (14 in 2012). Two portfolio managers posting losses in 2012 entered profit in 2013. The result was eight million euros aggregate losses in 2013 compared to 155.4 million the year before (31.3 million stripping out the heavy losses of one broker-dealer).

Sector ROE expands on profits growth and the smaller number of loss-making firms.

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

FIGURE 20



Source: CNMV.

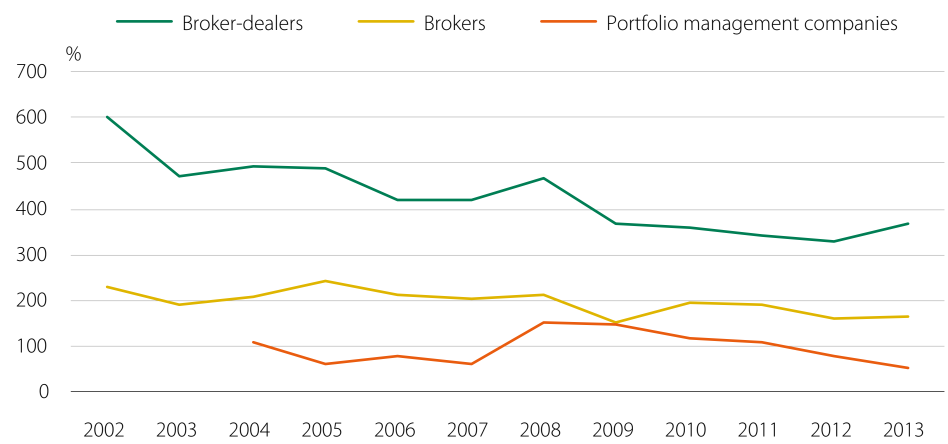
1 ROE based on pre-tax earnings.

Firms remain comfortably compliant with capital standards albeit with certain disparities.

Investment firms remained comfortably compliant with capital standards throughout 2013, albeit with some disparities between sub-sectors (see figure 21). Hence the surplus of qualifying equity funds to the minimum requirement rose from 3.3 to 3.7 among broker-dealers, held at a flat 1.6 in the case of brokers, and slipped back slightly in the portfolio management sub-sector, from 0.8 to 0.5. The one broker-dealer presenting an equity shortfall at the 2013 close is in the process of liquidation.

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

FIGURE 21



Source: CNMV.

IAF business resumes expansion after the lull of 2012, with assets under advice up by almost 20% to 17.6 billion euros.

Investment advisory firms (IAFs) came back strongly after their 2012 contraction, due to that year's turbulent markets. The number of IAFs registered rose from 101 to 126, while assets under advice climbed to 17.6 billion euros from the 14.8 billion of 2012. One notable development was the 52.8% increase in the assets corresponding to retail clients (see table 18), which lifted their share to 28% of the IAF sector total compared to 22% in 2012. Fee income advanced in parallel with the above noted growth in assets under advice as far as 33.3 million euros, 27.1% more than in 2012.

Main investment advisory firm variables

TABLE 18

Thousand euros	2011	2012	2013	2012 2H	2013 1H	2013 2H	% var. in year
NUMBER OF FIRMS	**82**	**101**	**126**	**101**	**112**	**126**	**24.8**
ASSETS UNDER ADVICE[1]	**16,033,108**	**14,776,498**	**17,630,081**	**14,776,498**	**15,442,297**	**17,630,081**	**19.3**
Retail customers	2,181,943	3,267,079	4,991,653	3,267,079	3,975,400	4,991,653	52.8
Professional customers	3,151,565	3,594,287	3,947,782	3,594,287	3,476,305	3,947,782	9.8
Others	10,699,600	7,915,132	8,690,646	7,915,132	7,990,593	8,690,646	9.8
NUMBER OF CONTRACTS[1]	**3,677**	**3,484**	**4,002**	**3,484**	**3,672**	**4,002**	**14.9**
Retail customers	3,542	3,285	3,738	3,285	3,446	3,738	13.8
Professional customers	119	175	235	175	195	235	34.3
Others	16	24	29	24	31	29	20.8
FEE INCOME[2]	**31,053**	**26,177**	**33,273**	**26,177**	**14,700**	**33,273**	**27.1**
Fees received	**30,844**	**26,065**	**33,066**	**26,065**	**14,676**	**33,066**	**26.9**
From customers	26,037	20,977	26,530	20,977	12,074	26,530	26.5
From other entities	4,807	5,088	6,537	5,088	2,601	6,537	28.5
Other income	209	112	206	112	25	206	83.9
EQUITY	**12,320**	**13,402**	**21,498**	**13,402**	**15,119**	**21,498**	**60.4**
Share capital	3,895	4,365	5,156	4,365	4,820	5,156	18.1
Reserves and retained earnings	950	4,798	9,453	4,798	7,251	9,453	97.0
Profit/loss for the year[2]	7,474	4,239	6,890	4,239	3,048	6,890	62.5

1 Period-end data at market value.
2 Cumulative data for the period.

Outlook

A better outlook for investment firms, anchored on the recovery of their main business lines.

The outlook for investment firms is brighter than for some time, thanks to the improved tone of their main business lines including order processing and execution, UCITS marketing, financial advice and portfolio management. But a new threat has emerged in the form of growing competition from, among others, foreign investment firms authorised to operate in Spain and domestic banks, which continue to rake in the lion's share of investment service fees.[16]

4.3 UCITS management companies

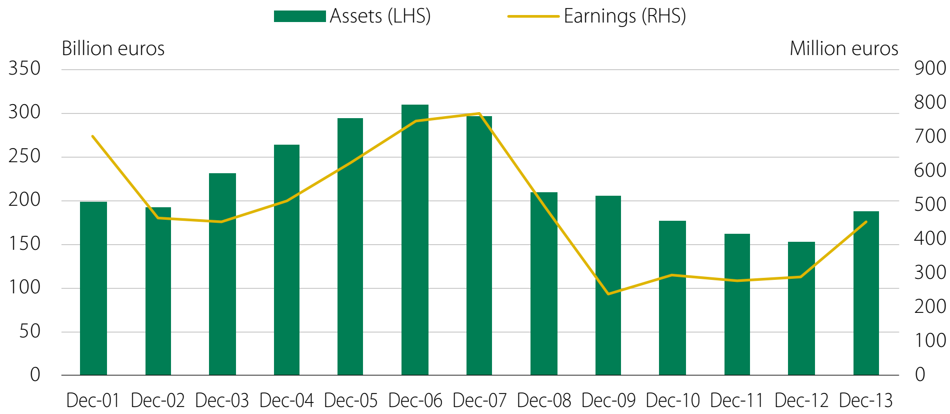
Assets under management in UCITS management companies rise by 22.5% in 2013 to 187 billion euros…

UCITS management companies returned to growth for the first time since the start of the crisis in 2007, with a 22.5% rise in assets under management to over 187 billion euros (see figure 22). Over 90% of the advance was sourced from the mutual fund segment, though investment companies too contributed on the upside.

16 From January to September 2013, credit institutions took in 77% of total fees from the provision of investment services, against the 22% going to brokers and broker-dealers and the 1% to portfolio management companies.

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

FIGURE 22



Source: CNMV.

…delivering an advance in income and, therefore, earnings to 453 million euros, 58% more than in 2012.

This increase in assets under management helped boost management companies' pre-tax profits by 58.4% to 453 million euros. The largest income statement caption, fee income from UCITS management, climbed 12.5% to just under 1.60 billion euros (see table 19), despite the average management fee dropping from 0.93% to 0.87% – a decline due partly to asset growth in fixed-income funds, where management charges tend to be lower. Meantime, sector-wide return on equity (ROE) jumped from 23.1% in 2012 to 38.7% in 2013, in line with the annual advance in earnings. The improved landscape for UCITS managers was also apparent in the smaller number of loss-making entities, down by 17 to 11, and the reduced volume of their losses, at 2.1 million, a full 79.3% less than at year-end 2012.

Bank sector restructuring continues to thin the ranks of UCITS managers, whose numbers drop to 96, nine fewer than in 2012.

Although the sector now seems to be recovering steadily after the bad patch of the past few years, its reorganization, much of it tied in with credit institution restructuring, shows no signs of letting up. Specifically, the year's one new entrant versus ten retirals, five of them due to changes in the banking sector, reduced the number of operators to 96 at the 2013 close.

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

TABLE 19

Million euros

	Assets under management	UCITS management fee income	Average UCITS management fee (%)	Fee ratio (%)[1]
2006	308,476	3,281	1.06	71.50
2007	295,922	3,194	1.08	70.50
2008	209,014	2,302	1.10	70.80
2009	203,730	1,717	0.84	68.08
2010	177,055	1,639	0.93	67.24
2011	161,481	1,503	0.93	65.60
2012	152,959	1,416	0.93	64.62
2013	187,347	1,594	0.85	61.94

Source: CNMV.

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

4.4 Other intermediaries: venture capital

The number of venture capital entities (VCEs) on the CNMV register fell from 340 in 2012 to 334 at the 2013 close. Of this number, 126 were funds (VCFs), 130 were companies (VCCs) and the remaining 78 were VCE management companies. In all, 19 entities joined the register in 2013 (nine VCFs, nine VCCs and one VCE manager) against 25 retirals (two VCFs, 18 VCCs and five VCE managers).

In 2013, the number of venture capital entities decreases slightly, from 340 to 334…

Movements in the VCE register in 2012 TABLE 20

	Situation at 31/12/2012	Entries	Retirals	Situation at 31/12/2013
Entities	**340**	**19**	**25**	**334**
Venture capital funds	119	9	2	126
Venture capital companies	139	9	18	130
Venture capital management companies	82	1	5	78

Source: CNMV.

According to preliminary data furnished by industry association Asociación Española de Entidades de Capital Riesgo (ASCRI), venture capital investment in Spain receded 31% in 2013 to 1.70 billion euros. As much as 91% of this total corresponded to transactions of under five million euros, and 74% to those of under one million euros. This evidences the scale of the investment effort being made in Spanish SMEs, especially at the early development stage. Specifically, 96% of the year's transactions involved early-stage concerns, breaking down 60% in capital expansion investments and 36% in seed and start-up finance. International funds were again prominent, as the source of 51% of the total invested (60% in the same period last year). The sectors attracting most investment were industrial products and services (43%), followed at a distance by "other services" (11.6%), medicine and health (11.5%) and information technology (11%). The IT sector, once again, was first on the list by reference to transaction numbers (36.4%). Finally, the venture capital sector raised 1.35 billion euros for its investments, 33.5% less than in 2011, of which 64% corresponded to international funds investing in Spain.

…while sector investment recedes by 31% to 1.70 billion euros…

The short-term outlook for the venture capital sector remains generally unsettled, though it seems activity has been reviving of late in line with the slowly improving performance of the domestic economy. What the industry needs to grow, however, is the revival of credit and an end to the current obstacles to bank lending. One step in this direction is the launch of the FOND-ICO Global fund of funds, a government initiative that would bring a welcome injection of liquidity – provided the sector can persuade private investors to contribute between 50% and 70% of the funds required. Already its start-up has encouraged many management companies to take the first steps in setting up new venture capital funds.

The mild recovery in domestic activity should favour venture capital business this year, though growth will continue to be constrained by the credit shortage.