Recent Developments in the Spanish Economy & Funding Outlook

January 15th, 2019
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Highlights

- The Spanish economy will maintain robust growth path with GDP growth forecast of 2.6% in 2018 and 2.2% in 2019

- National deleveraging is progressing, enabled by sustained combination of growth and a current account surplus

- Draft Budget Law for 2019 presented to Parliament on 14 January 2019
  - Reinforces Spain’s commitment with the Stability and Growth Pact. Strong pro-European sentiment throughout the crisis
  - Strong deficit reduction: Targets 2019 deficit of 1.3% of GDP, down from 2.8% in 2018 and below 1.8% envisaged in DBP adopted last October
  - Strong debt reduction: Targets Debt-to-GDP ratio of 95.4%, down from 98.1% in 2017 and 96.9% in 2018
  - Impact on growth of additional fiscal adjustment will be marginal

- Economic policy agenda to pursue structural reforms to address inequality, increase productivity and external competitiveness

- Recent rating upgrades allow for a widening and deepening of Spain’s investor base, and for an improvement in the average quality of participants
## Macroeconomic scenario 2018-2019

### Macroeconomic scenario (YoY growth rates in percent)

<table>
<thead>
<tr>
<th></th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Private consumption expenditure</td>
<td>3.0</td>
<td>2.9</td>
<td>2.5</td>
<td>2.3</td>
<td>3.1</td>
<td>2.2</td>
<td>2.1</td>
<td>1.7</td>
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<tr>
<td>General Government consumption expenditure</td>
<td>2.0</td>
<td>1.0</td>
<td>1.9</td>
<td>1.9</td>
<td>2.2</td>
<td>1.9</td>
<td>2.1</td>
<td>1.4</td>
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<tr>
<td>Gross Fixed Capital Formation</td>
<td>6.7</td>
<td>2.9</td>
<td>4.8</td>
<td>5.7</td>
<td>3.8</td>
<td>7.0</td>
<td>5.5</td>
<td>4.4</td>
</tr>
<tr>
<td>National Demand (Contribution to GDP Growth)</td>
<td>3.9</td>
<td>2.4</td>
<td>2.9</td>
<td>2.9</td>
<td>3.1</td>
<td>3.1</td>
<td>2.8</td>
<td>2.2</td>
</tr>
<tr>
<td>Exports of goods and services</td>
<td>4.2</td>
<td>5.2</td>
<td>5.2</td>
<td>2.4</td>
<td>3.3</td>
<td>2.3</td>
<td>1.3</td>
<td>2.8</td>
</tr>
<tr>
<td>Imports of goods and services</td>
<td>5.4</td>
<td>2.9</td>
<td>5.6</td>
<td>3.5</td>
<td>4.4</td>
<td>4.6</td>
<td>2.5</td>
<td>3.1</td>
</tr>
<tr>
<td>External demand (Contribution to GDP Growth)</td>
<td>-0.3</td>
<td>0.8</td>
<td>0.1</td>
<td>-0.3</td>
<td>-0.2</td>
<td>-0.6</td>
<td>-0.4</td>
<td>-0.1</td>
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<tr>
<td>Gross Domestic Product</td>
<td>3.6</td>
<td>3.2</td>
<td>3.0</td>
<td>2.6</td>
<td>2.8</td>
<td>2.5</td>
<td>2.4</td>
<td>2.2</td>
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### Other variables

<table>
<thead>
<tr>
<th></th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment rate (in % of Active Population)</td>
<td>22.1</td>
<td>19.6</td>
<td>17.2</td>
<td>15.5</td>
<td>16.7</td>
<td>15.3</td>
<td>14.6</td>
<td>14.0</td>
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<tr>
<td>Full-time Equiv. Employment (YoY Growth)</td>
<td>3.3</td>
<td>3.0</td>
<td>2.9</td>
<td>2.5</td>
<td>2.6</td>
<td>2.5</td>
<td>2.5</td>
<td>1.8</td>
</tr>
<tr>
<td>Net lending(+) / borrowing(-) with RoW (% of GDP)</td>
<td>1.7</td>
<td>2.4</td>
<td>2.2</td>
<td>1.3</td>
<td>2.1</td>
<td>1.8</td>
<td>1.5</td>
<td>1.2</td>
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<tr>
<td>Private Consumption deflator (YoY Growth)</td>
<td>-0.2</td>
<td>0.0</td>
<td>1.6</td>
<td>1.6</td>
<td>1.0</td>
<td>1.5</td>
<td>2.0</td>
<td>1.1</td>
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<tr>
<td>Headline Balance General Gov’t (in % of GDP)*</td>
<td>-5.3</td>
<td>-4.5</td>
<td>-3.1</td>
<td>-2.7</td>
<td>-2.94</td>
<td>-2.67</td>
<td>-2.66</td>
<td>-1.3</td>
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<tr>
<td>USD / € exchange rate</td>
<td>1.1</td>
<td>1.1</td>
<td>1.1</td>
<td>1.18</td>
<td>1.23</td>
<td>1.19</td>
<td>1.16</td>
<td>1.15</td>
</tr>
<tr>
<td>Euro Area GDP growth (YoY growth)</td>
<td>2.0</td>
<td>1.9</td>
<td>2.5</td>
<td>2.1</td>
<td>2.4</td>
<td>2.2</td>
<td>1.6</td>
<td>1.9</td>
</tr>
<tr>
<td>Oil prices (Brent, USD / barrel)</td>
<td>52.2</td>
<td>43.3</td>
<td>54.3</td>
<td>71.3</td>
<td>66.8</td>
<td>74.5</td>
<td>75.1</td>
<td>65.0</td>
</tr>
</tbody>
</table>

* Including Financial Sector One-Offs
Sources: Ministerio de Economía y Empresa and Ministerio de Hacienda.
Shaded areas are realisations. In white, forecasts contained in the 2019 Draft Budget.
**Economic sentiment**

**IMF Growth Forecasts for 2019**
*(Year-on-Year Growth Rates)*

<table>
<thead>
<tr>
<th>Institution</th>
<th>2018</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>IMF</td>
<td>2.5</td>
<td>2.2</td>
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<tr>
<td>OECD</td>
<td>2.6</td>
<td>2.2</td>
</tr>
<tr>
<td>European Commission</td>
<td>2.6</td>
<td>2.2</td>
</tr>
<tr>
<td>Bank of Spain</td>
<td>2.5</td>
<td>2.2</td>
</tr>
<tr>
<td>FUNCAS consensus</td>
<td>2.6</td>
<td>2.2</td>
</tr>
<tr>
<td>CEOE*</td>
<td>2.6</td>
<td>2.3</td>
</tr>
<tr>
<td>BBVA**</td>
<td>2.6</td>
<td>2.4</td>
</tr>
<tr>
<td>Consensus Forecast®</td>
<td>2.6</td>
<td>2.2</td>
</tr>
<tr>
<td>Government</td>
<td>2.6</td>
<td>2.2</td>
</tr>
</tbody>
</table>

* 2.3% growth for 2019 also forecasted by Citigroup, Goldman Sachs, AFI, CEPREDE, Econ Intelligence Unit, Bankia, CEOE or Cemex.

**% of population that thinks that membership of the EU is a good thing**

Source: EUROSTAT.
Spain’s growth pattern

- Current account surplus and net lending capacity vis a vis rest of the world
- Subdued inflation and strong job creation
- Rebalancing of weight of construction sector and higher weight of services sector
- Strong investment growth converging to Euro Area average

Exports and Imports of Goods and Services & Gross Fixed Capital Formation (% of GDP)

Gross Value Added (% of GDP)

Source: Instituto Nacional de Estadística.
A recovery intensive in labour creation

- 2.5 million jobs created since 2014, equivalent to over 25% of the total employment generated in the Euro Area
- Falling unemployment fuels internal demand
- Increased real labour productivity has led to enhanced competitiveness
- Measures to increase job quality in order to fight inequality, foster stability & human capital

Unemployment Rate & Employment Creation

Source: EUROSTAT, Ministerio de Economía y Empresa.

Minimum Wage & Productivity/Minimum Wage (Euros and ratio)

Source: EUROSTAT.
Banking sector adjustment

- Adjustment of the banking sector:
  - Downsizing & loss recognition
  - Enhanced capitalisation and profitability
- Strong improvement in NPLs: harmonised NPL ratio below Euro Area average
- EBA-2018 stress tests reveal reduced average impact under adverse scenario for Spanish banks

### Loan-to-Deposits & Equity to Assets (In %)

- Domestic Lending (Excl. Fin. & Public Sectors) to Deposits (LHS)
- Equity to Assets (RHS)

Source: Bank of Spain.

### Harmonised NPL Ratio (In % of Total Loans)

Source: EBA. Risk Dashboard Interactive Tool.

### Adjustment in Deposit Taking Institutions (Number of Employees and Branches)

- Employees (LHS)
- Branches (RHS)

Source: Bank of Spain.
private sector debt decreased by 62.1 pp of GDP → households & nonfinancial corporations’ leverage below Euro Area average
Inflation broadly in line with Euro Area average

- Core inflation remains well below ECB objective
- Energy remains a major contributor to shifts in headline inflation

**Harmonised Inflation of Consumer Prices**
*(Year-on-Year Growth Rate and Differential)*

**Core Inflation**
*(Year-on-Year Growth Rate and Differential)*

Source: EUROSTAT.
Result: persistent growth with current account surplus

Nominal GDP Growth vs. Current Account/GDP

Source: Instituto Nacional de Estadística and Bank of Spain.
## Fiscal policy framework

### Net Lending(+)/Borrowing. (% of GDP)

<table>
<thead>
<tr>
<th></th>
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<th></th>
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<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Central Government</strong></td>
<td>-3,6</td>
<td>-7,9</td>
<td>-4,8</td>
<td>-3,7</td>
<td>-2,8</td>
<td>-2,6</td>
<td>-1,89</td>
<td>-1,5</td>
<td>-0,3</td>
<td>0,0</td>
<td>0,0</td>
</tr>
<tr>
<td><strong>Autonomous Regions</strong></td>
<td>-5,1</td>
<td>-1,9</td>
<td>-1,6</td>
<td>-1,8</td>
<td>-1,7</td>
<td>-0,9</td>
<td>-0,36</td>
<td>-0,3</td>
<td>-0,1</td>
<td>0,0</td>
<td>0,0</td>
</tr>
<tr>
<td><strong>Local Governments</strong></td>
<td>-0,8</td>
<td>0,3</td>
<td>0,6</td>
<td>0,5</td>
<td>0,4</td>
<td>0,6</td>
<td>0,61</td>
<td>0,6</td>
<td>0,0</td>
<td>0,0</td>
<td>0,0</td>
</tr>
<tr>
<td><strong>Social Security</strong></td>
<td>-0,1</td>
<td>-1,0</td>
<td>-1,1</td>
<td>-1,0</td>
<td>-1,2</td>
<td>-1,6</td>
<td>-1,44</td>
<td>-1,5</td>
<td>-0,9</td>
<td>-0,5</td>
<td>-0,4</td>
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<tr>
<td><strong>General Government</strong></td>
<td>-9,64</td>
<td>-10,47</td>
<td>-6,99</td>
<td>-5,97</td>
<td>-5,27</td>
<td>-4,47</td>
<td>-3,08</td>
<td>-2,7</td>
<td>-1,3</td>
<td>-0,5</td>
<td>-0,4</td>
</tr>
</tbody>
</table>

*Source: Ministerio de Hacienda.*

*Forecasts are those contained in the Draft Budget for 2019 presented in January.*

### Debt-to-GDP ratio

*Source: Secretaría General del Tesoro y Financiación Internacional.*
The Treasury’s funding programme in 2019

- The Government’s commitment to fiscal consolidation will allow the Treasury to continue to reduce its recourse to the capital markets in 2019.
- Net issuance forecasted at €35 bn in 2019; to be attained exclusively through the issuance of medium and long-term instruments.
- Expected gross medium and long-term issuance of 126.9 billion euros, 3.8% less than in 2018.

The Treasury’s Funding Programmes since 2012

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Issuance</th>
<th>Amortisation</th>
<th>Net Issuance</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>249.6</td>
<td>36.8</td>
<td>212.8</td>
</tr>
<tr>
<td>2013</td>
<td>238.6</td>
<td>71.0</td>
<td>167.6</td>
</tr>
<tr>
<td>2014</td>
<td>241.3</td>
<td>65.0</td>
<td>176.3</td>
</tr>
<tr>
<td>2015</td>
<td>236.8</td>
<td>55.0</td>
<td>181.8</td>
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<tr>
<td>2016</td>
<td>221.4</td>
<td>47.7</td>
<td>173.7</td>
</tr>
<tr>
<td>2017</td>
<td>233.9</td>
<td>45</td>
<td>188.9</td>
</tr>
<tr>
<td>2018</td>
<td>213.0</td>
<td>40</td>
<td>173.0</td>
</tr>
<tr>
<td>2019</td>
<td>209.5</td>
<td>35</td>
<td>174.5</td>
</tr>
</tbody>
</table>

*Forecast Net Issuance

Source: Secretaría General del Tesoro y Financiación Internacional.

Funding Programme in 2019

<table>
<thead>
<tr>
<th>(In billion euros and in effective terms)</th>
<th>End 2018</th>
<th>Forecast 2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Net Issuance</td>
<td>34,277</td>
<td>35,000</td>
</tr>
<tr>
<td>Total Gross Issuance</td>
<td>212,964</td>
<td>209,526</td>
</tr>
<tr>
<td>Medium- and Long-term Gross Issuance</td>
<td>131,979</td>
<td>126,933</td>
</tr>
<tr>
<td>Amortisation 1</td>
<td>89,310</td>
<td>91,933</td>
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<tr>
<td>Net Issuance 1</td>
<td>42,669</td>
<td>35,000</td>
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<tr>
<td>Letras del Tesoro</td>
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<tr>
<td>Gross Issuance</td>
<td>80,984</td>
<td>82,592</td>
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<tr>
<td>Amortisation</td>
<td>89,377</td>
<td>82,592</td>
</tr>
<tr>
<td>Net Issuance</td>
<td>-8,393</td>
<td>0,000</td>
</tr>
</tbody>
</table>

1Includes Bonos & Obligaciones, debt in other currencies, loans and assumed debts.

Source: Secretaría General del Tesoro y Financiación Internacional.
Cost and life of debt: a longer portfolio at historically low rates

- Average cost of debt outstanding at historic low (2.39%)
- Slight increase in cost of issuance in 2018 due to the issuance of longer tenors
- Since 2013 average life of debt outstanding has increased from 6.20 to 7.45 years

Source: Secretaría General del Tesoro y Financiación Internacional.

*As of 15/01/2019
Recent trends in investor base

- Non-residents continue to be the leading investors with a share around 44.8%
- Spanish banks have been reducing their absolute and relative holdings of Spanish bonds
- This move has been compensated by the increase in Bank of Spain’s holdings to 22.3%

**Holdings of Letras & Bonos and Obligaciones del Estado**

- 45%
- 33%
- 22%


**Government bond holdings as % of Spanish bank's balance sheet.**

*Source: ECB.*
Ratings

- Expecting more foreign investors after recent upgrades: A stable outlook (DBRS), A-positive outlook (S&P), A-stable outlook (Fitch), Baa1 stable (Moody’s)
Thank you for your attention

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