For most of 2010, investors’ concerns centred on the struggles of Eurozone states like Greece, Ireland and Portugal to raise funds on capital markets, and the resulting dislocation in European sovereign debt markets. Spain was by no means immune to the effects of the debt crisis: funding costs increased, in relative terms particularly, and the country’s sovereign risk rating suffered a downgrade. Evidently this situation called for a firm and considered economic policy response.

This response arrived in the month of May when European countries approved a financial support package for Greece that would enable it to honor its obligations. But in a climate in which risk aversion was already running high, investors turned their attention to the vulnerabilities of other European Union countries, with Portugal and Ireland next in line.

In Spain’s case, the measures approved by the Council of Ministers on 20 May 2010, supplementing those included in the 2010 National Budget and the “Immediate Action Plan” of February 2010, made significant inroads into the central government funding requirement. And with the subsequent labour-market reform, the release of the stress test scores of Spanish banks and the overhaul of legislation on savings bank governing bodies, the pressures weighing on the Spanish debt market were considerably allayed. In November, however, the market was rocked once more by news that Ireland would call on the joint assistance of the European Union and the International Monetary Fund to confront the urgent restructuring of its financial system.

Against this background, and in contrast to the experience of 2009, Treasury issuance was some way below the figure contemplated in the 2010 National Budget. Specifically, while net funding in 2009 was approximately 30 billion euros more than initially projected, a combination of spending austerity and the recovery of tax revenues enabled Central Government to cut its funding requirement by 14.70 billion euros versus the sum envisaged in Tesoro Público’s January 2010 strategy document. Accordingly, the Central Government Debt stock closed the year at around 540.6 billion euros, leaving the General Government Debt ratio at 60.1% of gross domestic product.
While the auction, in its ordinary and special formats, remained the instrument of choice for Tesoro Público issuance, bank syndication came strongly to the fore in 2010. Four issues were syndicated in the year: one 5-year floating-rate Bono del Estado, two 10-year Obligaciones and one 15-year Obligación.

In the Letras del Tesoro market, non resident demand held up strongly at around 50% of total holdings. The work of our Primary Dealers has undoubtedly contributed to the dynamism of the Letras market, along with investors’ growing preference for safe, liquid assets.

The secondary market in Spanish government bonds had mixed fortunes in the year, with a weak start followed by a period of smoother trading, and then a final quarter characterised by low liquidity and heightened volatility.

Our intention now is to go on improving the funding conditions of Central Government by means of transparent, predictable policies supported on a robust, liquid market and a committed Primary Dealers group. This effort will be framed in a context of ongoing fiscal consolidation and the acceleration of structural reforms that should place us on the path of sustainable growth.
## CONTENTS

### 1. MACROECONOMIC SETTING

- 1.1. Macroeconomic setting  
  - 7
- 1.2. Financial markets in 2010  
  - 11

### 2. CENTRAL GOVERNMENT FUNDING POLICY

- 2.1. Central Government Debt issuance  
  - 25
    - 2.1.1. Overview  
      - 25
    - 2.1.2. Bonos del Estado and Obligaciones del Estado  
      - 29
    - 2.1.3. Letras del Tesoro  
      - 37

### 3. SECONDARY MARKETS IN 2010

- 3.1. Outright trades in Bonos del Estado and Obligaciones del Estado  
  - 41
- 3.2. Outright trades in Letras del Tesoro  
  - 43
- 3.3. Outright trades in stripped debt  
  - 45
- 3.4. Repo transactions  
  - 47
4. DISTRIBUTION OF THE CENTRAL GOVERNMENT DEBT PORTFOLIO

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>4.1. Distribution of unstripped Government Debt holdings</td>
<td>55</td>
</tr>
<tr>
<td>4.2. Non resident Debt holdings: geographical distribution</td>
<td>56</td>
</tr>
<tr>
<td>4.3. Fondo Tesoro</td>
<td>59</td>
</tr>
</tbody>
</table>
Museo Nacional del Prado. Madrid (19th century)
1.1. MACROECONOMIC SETTING

World economic recovery strengthened in 2010 after its tentative beginnings in the third quarter of 2009. But activity was reviving at significantly different speeds. Hence the advanced economies closed the year with an average GDP growth rate of 3% (-3.4% in 2009) against the 7.1% recorded by emerging and developing nations (+2.6% in 2009).

In the wake of the international financial crisis of 2008 and 2009, the year 2010 was characterised by the stresses affecting European sovereign debt markets, and the widespread prolongation of exceptional measures to hasten economic normalisation.
Commodity market tensions persisted over 2010 for both energy and non-energy goods. Prices were driven higher by the activity upswing among developed countries and the robust growth of the developing contingent, with China and India strongly to the fore.

The result was that the deflation fears of 2009 gave way to price rises of some intensity.

Among the advanced economies, the United States led the recovery with GDP growth of 2.9%. The Eurozone expanded by 2.0%, though with divergences between member states. And, finally, the Japanese economy managed a year-long advance of 2.5%.
Unemployment was again a major worry for the advanced economies in terms of the levels reached but also the speed of its increase. Again, however, its incidence varied from one region to the next. In the United States, unemployment rates doubled to 10%, while economies with less flexible labour markets, like the Eurozone and Japan, saw a slower progression as far as 10% and 5% of their respective active population.

The emerging nations again dominated the world economic stage, though rather less so than in 2009 and with some notable exceptions, giving further proof of the much-discussed “decoupling” that has allowed them to outperform the developed countries.

In effect, the term “decoupling” came into vogue at the start of the crisis in reference to the lesser
difficulties endured by the emerging regions. However the Lehmann Brothers collapse ushered in a period of intense contraction that pulled them back into line with the developed regions ("recoupling"). In 2009, notably as of the second quarter, the emerging economies spearheaded a strong across-the-board recovery, with the People's Republic of China as a motor force.

This growth lead over the developed countries was maintained in 2010, with emerging economies, in Asia particularly, reporting another year of solid growth, outstandingly so in the case of SE Asia and “Chindia”.

The consolidation of the growth surge among emerging economies did much to raise their profile in international forums, including the G-20, in 2009 and even more so in 2010, effectively laying to rest their “parvenu” status for the countries of the developed world.

At a time of thinning returns on developed country assets, the emerging economies were the prize destination for abundant capital flows, which forced their authorities to make considerable and, at times, fruitless efforts to keep their currencies on an even keel. Some countries took deliberate steps to stem these inflows, including taxes or entry barriers to foreign capital, or else had their monetary authorities partially intervene to defend the competitiveness of their currencies. All this, with few exceptions, in a context of economic overheating.
1. MACROECONOMIC SETTING

1.2. FINANCIAL MARKETS IN 2010

Public debt markets were in the thick of events throughout 2010, with tensions in the Eurozone erupting on two occasions. The first was the onset of the Greek crisis following revelations of the country's high debt and deficit levels. The tensions building over months were defused in May by the activation of a rescue package. The disclosure of the stress test results of European banks provided another boost to confidence on being welcomed by the markets as a transparency exercise by the financial sector, the source of the turmoil suffered in previous years. The next flashpoint was Ireland, where a similar rescue was performed in November following the partial nationalisation of debt-ridden banks. And, finally, the year's closing weeks saw a renewal of turbulence on a smaller scale, this time centred on the Portuguese economy.

The main vulnerability factors for these economies were concerns about the sustainability of their public finances and the health of their financial systems, which conspired to push sovereign spreads to highs not seen since the launch of the European Union.

The deployment of financial assistance mechanisms among Eurozone countries – the EFSF (European Financial Stability Facility) and, supplementarily, the ESM (European Stability Mechanism) – along with the loans made available by the IMF helped to restore calm over the year's closing months. But, ultimately, these movements in sovereign debt market indicators betray certain reservations about the viability of the single currency. Thus the yields of AAA-rated countries (primarily Germany and the U.S.) experienced a steady run-down from May to November on the back of safe haven buying. Conversely, the spreads of the southern Eurozone countries (Portugal, Spain, Italy and Greece) and Ireland headed higher in these same months by way of spikes coinciding with the Greek and Irish troubles.

We can thus distinguish two separate trends among the advanced economies. On the one hand, the government bond yields of perceivedly safer countries like the United States, Germany or the United...
Kingdom descended by around 50 basis points (bp) in the full-year period, evidencing heavy purchasing of these assets. Yields fell most steeply as of May after the Greek crisis and resultant surge in risk aversion and experienced a mild upswing after the summer months.

Greece’s sovereign debt was the hardest hit by financial instability with rises in yield of around 800 bp, while Ireland suffered a smaller run-up of 400 bp. The result was a year-long widening in the spread of peripheral over German debt. The exception here was Spain, which managed to diverge from its group in the closing months and stabilise its risk premium.
The story in emerging debt markets was one of steadily improving spreads although without matching the successes of 2009, when the index measuring the spread between emerging market and U.S. treasuries (EMBI+) dropped from 690 to 274 basis points.

Improvement in 2010 was on a more modest scale, from 274 bp to 248 bp. Though considering that in its best moments prior to the crisis (from 2005 to mid-2007) the EMBI+ was moving in an interval of 150 to 200 bp, we can see that this 2010 reduction has brought the indicator meritoriously close to its pre-crisis levels. Emerging market yields, as tracked by the EMBI+, also bear favourable comparison with the 2010 spreads of various peripheral European bonds over the German benchmark.
By early 2010, monetary authorities in the advanced economies were preparing their strategies to phase out the non-standard measures applied after the Lehman Brothers collapse. But in the second quarter, with the Greek crisis raging and the outlook worsening for the U.S. economy, the stance was switched to accommodative or even expansionary.

In the Eurozone, the ECB began the year planning the phased withdrawal of its extraordinary liquidity provisions. However, it too opted to keep conditions loose in the light of the Greek situation. In any event, much of the excess liquidity was absorbed in the course of the year, which closed with levels approaching those in place before the Lehman failure.

But the most far-reaching of the ECB’s non-standard measures was certainly the bond buying programme. Public debt purchases under its auspices were sterilised through liquidity-absorbing operations so did not amount to quantitative easing. Despite initial high volumes, purchasing was scaled down over the year with occasional spikes when debt markets tensed.

For the Federal Reserve too, 2010 was a year of changes. Like the ECB, it started the year in restrictive mode, with the phasing out of exceptional measures (including the completion of its RMBS purchasing programme), but then had to reverse its stance in the second half, in view of the worsening macro outlook for the U.S. economy and further to its duties of vigilance on inflation and unemployment rates. As part of the expansionary monetary policy adopted in August, the Fed began reinvesting the redeemed proceeds of its portfolio in order to keep its balance sheet from shrinking. And at its Jackson Hole meeting it set the stage for a possible quantitative easing that finally arrived on 4 November. Under the so-called QE2 (Quantitative Easing 2) it will buy 600 billion dollars worth of long-term U.S. government bonds over an interval of eight months.

The Bank of Japan has also embarked on a new round of quantitative easing. After a run of liquidity-facilitating measures, it decided in October to launch a “comprehensive monetary easing policy”, which...
1. MACROECONOMIC SETTING

 included a reduction in its target rate from the 0.1% in place since 2008 to the range of 0%-0.1%, and a message that it would pursue a monetary policy of near-zero rates until it felt medium- to long-term price stability was sufficiently assured. The bank also announced a temporary Asset Purchase Programme, committing it to acquire assets such as public debt, commercial paper, private debt, exchange-traded funds (ETF) and real estate investment trusts (REITs).

Finally, other central banks like those of Australia, New Zealand, Sweden and Norway initiated an interest rate upcycle. Meantime, other central banks have begun hiking rates.

### KEY CENTRAL BANK RATES

<table>
<thead>
<tr>
<th>Country</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>4.75%</td>
</tr>
<tr>
<td>New Zealand</td>
<td>3%</td>
</tr>
<tr>
<td>Norway</td>
<td>2%</td>
</tr>
<tr>
<td>Sweden</td>
<td>1.25%</td>
</tr>
<tr>
<td>Denmark</td>
<td>1.05%</td>
</tr>
<tr>
<td>Canada</td>
<td>1%</td>
</tr>
<tr>
<td>Switzerland</td>
<td>0.25%</td>
</tr>
</tbody>
</table>

Source: Bloomberg
In euro money markets, interbank rates trended steadily higher over most of the year. Meantime, credit risk fluctuated sharply in tune with the successive episodes of debt market tension. These fluctuations were tempered by compensatory shifts in rate expectations, bringing a degree of stability to interbank markets.

Euro interbank rates have moved steadily higher.

Interest rates on U.S. dollar interbank markets experienced almost no variation in the full-year period though note the bulge in the curve over the summer months. Credit risk traced a similar pattern with an upturn in the central months followed by a return to its start-out levels.

Dollar interbank rates rise in summer and ease back thereafter.
1. MACROECONOMIC SETTING

Issuance on global private debt markets trended lower in aggregate terms after the recovery of 2009. This decline, however, reflected the rising participation of speculative grade instruments at the expense of higher-rated debt.

By sector, financial entities accounted for over 60% of issue volumes, despite persisting concerns about the high indebtedness of some institutions and the heavy redemption schedules of 2011 and 2012.

A number of trends were detectable on European private debt markets with regard to markets, instruments, and types of borrower. Dominating the landscape were the droughts in primary market issuance occurring in May and December, which contributed to further tighten business lending.
Peripheral markets are worse affected...

By type of market, the big distinction was between peripheral countries and the rest of Europe. By instrument, the most popular choices were those offering the widest coverage and therefore safer for the investor; primarily covered bonds. Finally, the borrowers finding the easiest markets were those considered to be financially in soundest shape.

In countries such as Germany, borrowers had it notably easier thanks to the economic recovery under way and the safe haven status of their public debt, which enabled companies to tap the markets under highly advantageous conditions. This was true of the Scandinavian countries, the Netherlands and France, among others.

...while borrowers in other jurisdictions get to access funding under better conditions.
1. MACROECONOMIC SETTING

2010 was a recovery year for asset-backed securities. An uneven performance by world stock markets, though winners outnumber losers.

Some instruments like asset-backed securities have been showing signs of recovery since late 2009 and it is thought this trend will continue through 2011. Around 81 billion euros in securitised debt was issued over 2010, with a substantial decrease in the required return, though the segment remained tight shut in certain markets due to poor macroeconomic prospects.

Equity markets, with some exceptions, served up a positive showing in 2010. Analysed globally, we can say that emerging equity markets outperformed their developed world equivalents.

Among the advanced economies, outcomes varied from the strong gains of leading indices in the German (17.80%), American (12.80%) and British markets (9%) to the steep losses (-41.08%) of the Greek index.
Emerging markets again outperformed developed world bourses in 2010. The Ibex-35 lost half of the ground regained in 2009.

We can see this clearly from looking at the Morgan Stanley emerging market index (MSCI EM) which climbed by 16.36% against the 12.78% of the S&P index, in contrast to the 5.81% slide of the Eurostoxx-50. Focusing on emerging market indices, we find that geographical areas performed more or less in line, with gains of 16.56% for Emerging Asia, 13.72% for Emerging Europe and 12.07% for Latin America.

In the case of Spain, the Ibex-35 was penalised for both sovereign debt episodes and the weakness of the European financial sector, closing 17.42% in losses after the 29.84% advance of 2009. Turnover on the Spanish stock exchanges again topped one trillion euros, so we can see that the price falls of most shares had little overall impact on trading activity. Finally, the Spanish market ended the year with
capitalisation of 1,071.63 billion euros, 3.2% down versus the 2009 close, with financial and real estate sectors accounting for around 55% of the decline.

In currency markets, movements in euro exchange rates were primarily driven by events in Eurozone sovereign debt markets, to the relative exclusion of other factors like the growth outlook and expectations of interest rate hikes. The result was that Europe’s currency lost an annual 6.55% against the dollar, to close the year priced at 1.3380 USD.

2010 had started out with a depreciating euro, under pressure from profit taking and the progressive improvement of economic indicators in the United States. The downtrend received more fuel in the opening months from the Greek debt crisis, which occupied the forefront of investor concerns. These concerns quickly spread to other Eurozone countries and would not ease significantly until mid June and the EU’s launch of its financial support package. European governments’ austerity plans also served initially to buoy the euro.

In a second phase lasting to early November, the euro regained ground amid occasional faltering. Macroeconomic indicators turned out better than expected in the case of Europe and below the consensus in the United States. And this, allied with the stress test scores of European banks and the prospect of more quantitative easing by the Federal Reserve, lent renewed strength to Europe’s currency.

However, the euro’s ascent was promptly cut short by problems at Ireland’s banks, which very soon spilled over to its public accounts and began bearing down on other countries’ sovereign paper. The rising yields of U.S. fixed-income securities, and monetary tightening by China’s central bank were other factors contributing to the depreciation of the European currency.
A common problem; inflows of speculative capital inducing currency appreciation...

...is tackled different ways by the emerging nations.

A more flexible renminbi as of mid-2010.

The currencies of top emerging nations ended the year without the depreciation, though with alternative measures proliferating in many cases. The People's Republic of China, for instance, raised its bank reserve requirements on no fewer than six occasions, as far as 19%. And Brazil, which had introduced foreign capital taxes in late 2009 to rein in the appreciating real, was forced to tighten up the rules on banks' currency holdings on evidence of the failure of this measure to stem inflows of speculative cash. Another example is Chile, which had to intervene heavily to halt the peso's ascent against the U.S. dollar, and the list continues with countries such as South Korea, Thailand, Indonesia, Taiwan, Mexico, Colombia and Peru.

The renminbi, meantime, returned in June 2010 to the managed float system in place from July 2005 to July 2008, when the Chinese authorities opted to use exchange rates to attenuate the impact of

Source: Reuters
the economic crisis. This policy attracted a barrage of criticism, especially from the United States, as well as prompting defensive reactions from other Asian countries. In 2010, renewed flexibility took the renminbi 3.59% higher against the dollar – more in real terms given China’s high inflation differential vis-à-vis the United States.
Fundació Gala-Salvador Dalí, Galatea Tower. Figueres, Gerona (opened 1974)
2. CENTRAL GOVERNMENT FUNDING POLICY

2.1. CENTRAL GOVERNMENT DEBT ISSUANCE

2.1.1. OVERVIEW

Tesoro Público reduced its gross and net issuance with respect to the amounts announced at the start of the fiscal year, thanks to government spending cutbacks and the positive progress of tax revenues.

At 207.56 billion euros, total gross issuance was 20.44 billion euros down on the figure of 228 billion projected in January 2010. The steepest falls corresponded to Letras del Tesoro, with issue volumes 17.92 billion down on forecast. Issuance of Bonos del Estado, Obligaciones del Estado and other debt instruments was down by 2.52 billion, with only 94.48 billion issued against the 97 billion euros initially planned.

The following figure charts the decrease in Tesoro Público issuance over 2010. We can see that the Treasury's net funding came to 62.10 billion euros against the 76.80 billion pre-announced. Redemptions too were below forecast due to the year's lower sales of short-term Letras del Tesoro. Summing these issuance figures with the debt taken on from Radiotelevisión Española, now in liquidation, we arrive at an eventual increase of some 65.20 billion in the Central Government Debt stock.
2. CENTRAL GOVERNMENT FUNDING POLICY

Table 2.1.1 2010 ISSUANCE: AGGREGATE FIGURES
(In billion euros)

<table>
<thead>
<tr>
<th></th>
<th>Projection January 2010</th>
<th>2010 close</th>
</tr>
</thead>
<tbody>
<tr>
<td>Funding requirement (net issuance)</td>
<td>76.8</td>
<td>62.1</td>
</tr>
<tr>
<td>Gross issuance of bonds and long-term loans*</td>
<td>97.0</td>
<td>94.5</td>
</tr>
<tr>
<td>Redemptions of bonds and long-term loans*</td>
<td>-35.4</td>
<td>-35.8</td>
</tr>
<tr>
<td>Net issuance of bonds and long-term loans*</td>
<td>61.6</td>
<td>58.7</td>
</tr>
<tr>
<td>Increase in outstanding balance of Letras del Tesoro</td>
<td>15.2</td>
<td>3.4</td>
</tr>
<tr>
<td>Assumption of RTVE debt</td>
<td>1.5</td>
<td>1.5</td>
</tr>
<tr>
<td>Net change in Debt stock</td>
<td>78.3</td>
<td>65.2</td>
</tr>
<tr>
<td>Total Debt stock at end 2010</td>
<td>553.5</td>
<td>540.6</td>
</tr>
</tbody>
</table>

(*) Includes foreign-currency debt, Bonos and Obligaciones and assumed debt.
In effective terms except Debt stock (nominal).
Source: Directorate-General of the Treasury and Financial Policy.

Table 2.1.2 below provides this same information with a breakdown by market instrument, showing that the decrease in issuance responded primarily to Letras del Tesoro.

Table 2.1.2 2010 ISSUANCE (In billion euros)

* Including redemptions of Bonos and Obligaciones, Letras, foreign-currency debt, assumed debt and other debt.
** Including gross issuance in foreign currencies and other debts.
Source: Directorate-General of the Treasury and Financial Policy. Issuance figures in effective terms and change in the Debt stock in nominal terms.
2. CENTRAL GOVERNMENT FUNDING POLICY

The year ended with a 65.20 billion increase in the Debt stock.

Table 2.1.3 tracks the progress of outstanding debt over the last few years. We can see that the gross amount of Central Government Debt has increased in each of the last three years after the dip of 2006 and 2007.

<table>
<thead>
<tr>
<th>Year</th>
<th>Letras</th>
<th>Bonos and Obligaciones</th>
<th>Others</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>70.6</td>
<td>116.6</td>
<td>42.1</td>
<td>229.4</td>
</tr>
<tr>
<td>% total</td>
<td>30.8</td>
<td>50.8</td>
<td>18.4</td>
<td>100.0</td>
</tr>
<tr>
<td>1999</td>
<td>53.1</td>
<td>205.3</td>
<td>36.3</td>
<td>294.7</td>
</tr>
<tr>
<td>2002</td>
<td>35.8</td>
<td>247.1</td>
<td>29.0</td>
<td>312.0</td>
</tr>
<tr>
<td>2003</td>
<td>38.8</td>
<td>246.0</td>
<td>24.4</td>
<td>309.1</td>
</tr>
<tr>
<td>2004</td>
<td>37.0</td>
<td>255.9</td>
<td>26.3</td>
<td>319.2</td>
</tr>
<tr>
<td>2005</td>
<td>33.3</td>
<td>264.7</td>
<td>21.2</td>
<td>319.2</td>
</tr>
<tr>
<td>2006</td>
<td>31.3</td>
<td>264.1</td>
<td>17.1</td>
<td>312.5</td>
</tr>
<tr>
<td>2007</td>
<td>32.4</td>
<td>260.9</td>
<td>13.8</td>
<td>307.2</td>
</tr>
<tr>
<td>2008</td>
<td>52.1</td>
<td>293.0</td>
<td>13.3</td>
<td>358.4</td>
</tr>
<tr>
<td>2009</td>
<td>85.5</td>
<td>376.6</td>
<td>13.3</td>
<td>475.4</td>
</tr>
<tr>
<td>2010</td>
<td>89.8</td>
<td>437.2</td>
<td>13.7</td>
<td>540.6</td>
</tr>
<tr>
<td>% total</td>
<td>16.6</td>
<td>80.9</td>
<td>2.5</td>
<td>100.0</td>
</tr>
</tbody>
</table>

(*) Central Government Debt in gross nominal terms at the end of each year. Without deducting the Debt held by government authorities or the balance of the Treasury's account at Banco de España. Source: Directorate-General of the Treasury and Financial Policy. Ministry of Economy and Finance.

Auctions were again the procedure of choice for Tesoro Público issuance, channelling around 81% of Bono and Obligación sales, the same proportion as in 2009. Auctions were resolved by the "modified Dutch procedure" meaning sales went through at the average price in the case of bids above this average, and at the price actually stated in the case of all other accepted bids. Their dates adhered to the pre-set annual calendar: namely Letras auctions on the third and fourth Tuesday of each month and auctions of Bonos and Obligaciones on the first and third Thursday respectively. The specific references to be sold are announced ten days before the start of each quarter, with target placement volumes announced the Monday before the auction is held.
The year saw fewer reopenings of off-the-run Bonos and Obligaciones with tenors in between the benchmark terms – a total of three only compared to the thirteen of 2009, with the resulting increase in liquidity. Again, various references were placed on the same auction date to cater for investor demand across all maturities.

Despite the year’s lower funding requirements, auctions increased in size as a consequence of their smaller number versus 2009. The sections that follow analyse the progress of auctions in the year.

Tesoro Público continued the custom of using bank syndication to issue new references. Four bonds were syndicated in the year: one 5-year floating-rate Bono del Estado, two ten-year Obligaciones and one 15-year Obligación.

In Letras del Tesoro, the year’s main novelty was the issue of 18-month bills beginning in February, widening investors’ choice of maturities to 3, 6, 12 and 18 months.

### Table 2.1.4 REOPENINGS AND SYNDICATIONS 2010

<table>
<thead>
<tr>
<th>Bonos and Obligaciones del Estado</th>
<th>Coupon (%)</th>
<th>Maturing</th>
<th>Auction date</th>
<th>Type of auction</th>
<th>Amount allotted (mill. euros)</th>
</tr>
</thead>
<tbody>
<tr>
<td>4.00</td>
<td>04/30/2020</td>
<td>01/13/2010</td>
<td>syndication</td>
<td>5,000.0</td>
<td></td>
</tr>
<tr>
<td>6.00</td>
<td>01/31/2029</td>
<td>01/21/2010</td>
<td>reopening</td>
<td>1,513.1</td>
<td></td>
</tr>
<tr>
<td>4.65</td>
<td>07/30/2025</td>
<td>02/13/2010</td>
<td>syndication</td>
<td>5,000.0</td>
<td></td>
</tr>
<tr>
<td>4.20</td>
<td>01/31/2037</td>
<td>02/18/2010</td>
<td>reopening</td>
<td>958.6</td>
<td></td>
</tr>
<tr>
<td>Floating</td>
<td>03/17/2015</td>
<td>03/10/2010</td>
<td>syndication</td>
<td>1,500.0</td>
<td></td>
</tr>
<tr>
<td>4.85</td>
<td>10/31/2020</td>
<td>07/06/2010</td>
<td>syndication</td>
<td>6,000.0</td>
<td></td>
</tr>
<tr>
<td>5.75</td>
<td>07/30/2032</td>
<td>10/21/2010</td>
<td>reopening</td>
<td>941.3</td>
<td></td>
</tr>
</tbody>
</table>

18-month Letras return to the fold.

Fewer off-the-run bonds were reopened while a series of new references were placed by syndication.
2.1.2. BONOS AND OBLIGACIONES DEL ESTADO

Issuance of euro-denominated Bonos and Obligaciones closed the year at 92.68 billion.

Bonos del Estado (42.50 billion) accounted for around 46% of medium- and long-term sales. Three new Bonos were issued in the year in three- and five-year tenors. The Bono 2.50% October 2013 was issued in June and auctioned four times in 2010 to take it to an outstanding balance of 14.29 billion euros. Earlier, in April, the Treasury had issued a five-year Bono with coupon 3.0% maturing April 2015 which was auctioned on a further three occasions as far as a year-end nominal value of 14.24 billion. Finally, the Bono 3.25% April 2016 had its initial placement in the month of November. Still in the short bond segment, the Treasury placed a further two tranches of the 3-year Bono 2.30% April 2013 and the 5-year Bono 3.30% October 2014.

Separate mention must go to the five-year floating-rate Bono March 2015, syndicated in March, which raised a nominal amount of 1.50 billion. A fuller description of this issue is provided further on in the chapter.

Two new references launched in the ten-year tenor were placed by bank syndication: the first in January, with a 4.00% coupon maturing 30 April 2020, which was also auctioned on three occasions as far as an outstanding balance of 15.50 billion euros, and the second in July, coupon 4.85% maturing October 2020, which was issued three times more as far as 13.09 billion. These issues too are described in detail at the end of this chapter.

In the 15-year tenor, the Treasury syndicated a new Obligación 4.65% maturing July 2025 in the month of January 2024, with four more issues following in the year. This reference ended the year with an outstanding balance of 14.24 billion euros.

Further along the curve, the 30-year Obligación 4.70% July 2041 was auctioned on four occasions and...
the Treasury placed an additional tranche of the following off-the-run bonds; the 6.00% January 2029, the 5.75% July 2032 and the 4.20% January 2037.

Figure 3.1.3 shows the volumes sold through auctions, second rounds and syndicated placements, along with the associated bid-to-cover ratio. The bid-to-cover reflects the relationship between the bids made at each auction and the final amount issued by the Treasury. It accordingly serves as an indicator of demand strength on each auction date. The average 1.94 ratio of 2010 denotes robust demand on a par with the levels of 2009 (ratio of 1.93). Note also that amounts allotted in non-competitive bidding summed 162.3 million euros.

Second rounds are an option reserved for Primary Dealers who meet the minimum Debt quotation requirements established in the regulations. Those entering the second round have their bids allotted at the weighted average price of the competitive auction. As such, their use by Primarily Dealers depends on the market conditions prevailing. Basically, they will only be interested if the market price on the date in question (two business days after the auction, almost always a Monday) is higher than the auction average. The total issued in second rounds came to 4.62 billion euros.
In March 2010, Tesoro Público syndicated a five-year floating-rate Bono del Estado for 1.5 billion euros, marking its second venture into this kind of issue.

The new instrument served the Treasury in the following ways:

- Taking pressure off on-the-run references.
- Targeting current investor preferences with the pay-off of diversifying its investor base.
- Achieving a small financial saving with respect to fixed-rate Bonos del Estado.
The new Bono, paying a quarterly coupon equivalent to the 3-month Euribor rate plus 40 basis points, fetched a yield at issuance of Euribor 3 months plus 45 basis points. Interest was keen, with 86 orders received from investors for a total book exceeding 2 billion euros.

Although most of the new bond (38%) was sold in Spain, a good proportion found its way to Italy (22%), Germany (14%) and the Middle East (11%), with investors in the rest of the world taking a combined 15%. By investor type, the list ran from credit institutions (40%) and investment funds (27%) to insurance corporations and pension funds (18%) and central banks (15%).

This syndicated transaction supplemented the year’s three placements in euros: two ten-year Obligaciones (4.00% April 2020 and 4.85% October 2020) and one 15-year Obligación (4.65% July 2025). BNP Paribas, Deutsche Bank and Caja Madrid acted as leaders of the syndicate.

Source: Directorate-General of the Treasury and Financial Policy
In 2010, Tesoro Público syndicated two new 10-year Obligaciones. Its motives in issuing these new references were the year’s hefty funding requirements and the existence of keen demand in this maturity band.

The first of these issues went ahead in January, a 10-year Obligación del Estado 4.00% maturing April 2020. The bond was placed at 4.096%, equating to a 56 bp spread over the mid swap curve and 75.9 bp over the corresponding German benchmark. Tesoro Público took in 180 orders worth 8 billion euros and placed an eventual volume of 5 billion euros.

Over half the sales of the new Obligación were outside Spain, which accounted for 43%, notably in the United Kingdom and Ireland (12%), Portugal (12%) and France (10%). Credit institutions were the single biggest investor group (66%), though real money investors also took a large share, with 17% going to investment funds and 11% to insurance corporations and pension funds.

The placement was led by Barclays Capital, Banco Bilbao Vizcaya Argentaria (BBVA), Citi, Santander and Société Générale. The rest of the Primary Dealers group were also actively involved in sales of the new Treasury security.

In July 2010, it was decided to syndicate a new reference in the same tenor in view of the 15.50 billion balance attained by its predecessor in six short months. In this case, Tesoro Público took in over 250 orders totalling 14.50 billion euros.
Non residents featured prominently, accounting for 66% of total sales, while investor countries of origin were primarily Spain (34%), the United Kingdom (20.3%), Asia (13.3%), Scandinavia (6.2%) France (6%), Benelux (5%), Germany and Austria (4.8%) and the Middle East (2.7%).

A large part of the issue went to end investors with a medium- to long-term horizon: 24.3% to asset managers, 19.3% to central banks and other official institutions and 16.5% to pension funds and insurers. Credit institutions again headed the investor list with 37.2%.

Barclays Capital, Banco Bilbao Vizcaya Argentaria (BBVA), Caja Madrid, Crédit Agricole, Deutsche Bank and Santander were leaders of the placement with remaining Primary Dealers joining in as co-leads.

Source: Directorate-General of the Treasury and Financial Policy
In February 2010, Tesoro Público syndicated a new 15-year Obligación for 5 billion euros.

The issue was priced at 4.668%, equivalent to 21.8 bp over the Obligación del Estado coupon 4.65% maturing July 2025 and 85 bp over the mid swap curve.

Tesoro Público took in 270 investor orders totalling 14 billion euros. The main investor countries of origin were Spain (33%), France (23%) and the United Kingdom and Ireland (16%), though the issue also found buyers in strategic areas like the Scandinavian countries (8%). By type of investor, the list was headed by bank treasury departments (36%), investment funds (35%) and insurance corporations and pension funds (20%).
Banco Bilbao Vizcaya Argentaria (BBVA), Crédit Agricole CIB, HSBC, Société Générale and Santander led the issue, with remaining Primary Dealers also taking part.

**DISTRIBUTION OF 15-YEAR OBLIGACIÓN BY GEOGRAPHICAL MARKET**

- Spain 33%
- France 23%
- United Kingdom/Ireland 16%
- Germany/Austria 8%
- Scandinavia 8%
- Benelux 4%
- Others 8%

**DISTRIBUTION OF 15-YEAR OBLIGACIÓN BY TYPE OF INVESTOR**

- Credit institutions 35%
- Investment funds 35%
- Insurance corporations and pension funds 20%
- Others 7%
- Central banks 3%
- Others 7%

Source: Directorate-General of the Treasury and Financial Policy
2. CENTRAL GOVERNMENT FUNDING POLICY

2.1.3. LETRAS DEL TESORO

Letras del Tesoro were issued at 3-, 6-, 12- and 18-month tenors in every month but January, when 18-month bills were not sold. Each reference grew its outstanding balance in the year. As well as putting more liquidity behind on-the-run references, shorter-dated issues add flexibility to Central Government cash management by bringing in short-term funds.

Issue size was largest in the 12-month maturity, with 4.4 billion raised in the year compared to average sales of around 1.7 billion across all remaining tenors.

Total annual issuance was sizeably below the projection made in January 2010, with an eventual 133 billion placed against the pre-announced amount of 113 billion euros. The volume of outstanding Letras accordingly contracted from 18.0% of the Debt stock in 2009 (10.5% in 2007) to 16.6% in 2010.

Our next figure gives the results of Letras auctions in the year and the second round offered to Primary Dealers (generally organised for the second business day after the auction with sales of up to 10% of the auction allocation at the corresponding stop-out price). Of the total shown, second rounds accounted for 6.48 billion euros, while the sum of 2.55 billion was allotted in non competitive bids.
2. CENTRAL GOVERNMENT FUNDING POLICY

AUCTIONS OF BONOS AND OBLIGACIONES DEL ESTADO IN 2010
(In million euros)
3. SECONDARY MARKETS IN 2010

Secondary markets in European sovereign debt were the centre of attention over most of 2010, due to the crisis aftershocks sweeping Greece and Ireland and the two countries’ subsequent financial rescues. Spanish bonds were caught up in the turmoil on both occasions, on perceived similarities in vulnerability between these countries’ economies and that of Spain. But investors, it should be said, were clear-sighted enough to recognize and later reward the efforts made by the Spanish authorities in budgetary consolidation and structural reform.

Secondary market liquidity again strengthened progressively from the end of the first quarter, thanks to the active quoting and trading of outstanding Debt. The more or less flat turnover of electronic platforms (Senaf and MTS Spain) with respect to 2009, contrasted with an upswing in trading among account holders and, especially, with end clients. This liquidity increase worked in the market’s favour by facilitating the entry of both resident and foreign investors.

Primary Dealers were instrumental in this respect through their efforts to distribute and provide liquidity to Public Debt securities in conditions of heightened volatility. The Resolution of 18 November 2008 of the Directorate-General of the Treasury and Financial Policy, which recasts the operating rules for Primary Dealers in Kingdom of Spain Debt, has proved to be a flexible instrument for boosting the liquidity of outstanding bonds.

Our next section looks in greater detail at secondary market trading in 2010, with a split by underlying assets (bonds and bills) and type of transaction (outright and repo trades).
3. SECONDARY MARKETS IN 2010

3.1. OUTRIGHT TRADES IN BONOS AND OBLIGACIONES DEL ESTADO

After the trading slump on the Bonos and Obligaciones market in 2008 and 2009, average daily volumes in outright trades (spot and forward) closed at 16.72 billion euros, a 79% increase with respect to the previous year. This strong recovery rested on the growth of account-holder trading (up by 57% versus 2009 as far as a daily average of 3.38 billion euros), but, above all, on the surge in third-party trading (up by 86% for a 2010 daily average of 13.33 billion).

Focusing on spot trades between account holders (the sum of first-tier trades on electronic platforms and bilateral second-tier or OTC transactions), we find that turnover rose by 58% in 2010. All trading segments shared in the advance, with electronic platforms particularly reporting turnover growth of 71.5% with respect to the year before.

Source: Banco de España

The average daily volume of outright trades in Bonos and Obligaciones moves up sharply versus 2009.

Strong advance in account-holder spot trading, with all trading segments pulling in line.
These turnover developments produced a slight shift in market share from the second tier to the electronic market, where SENAF and MTS each hung on to their respective custom.

No major changes in the trading shares of different trading segments.
The bond most keenly traded on the wholesale market in 2010 was the 10-year Obligación (coupon 4.00% maturing April 2020), the benchmark in its term to June 2010, which accounted for almost 11% of total spot trading on the electronic market and second tier, followed by the 10-year Obligación (coupon 4.85% maturing October 2020, and benchmark from July to December 2010) with 7.5%, and the benchmark 5-year Bono (coupon 3.0% maturing April 2015) with 7.0%.

3.2. OUTRIGHT TRADES IN LETRAS DEL TESORO

The Letras market experienced a surge in activity that carried average daily volumes in outright trades to 1.66 billion euros, a full 109% more than in 2009. The increase was especially pronounced in business-to-consumer trading, which climbed 184% in the year, while wholesale trading progressed by a considerably humbler 4%. This marks a continuation of the run-up in Letras trading that began in 2008 as a consequence of the more volatile conditions prevailing on financial markets.
The increase in account-holder trading was mainly localised in the second tier while electronic platforms kept up a level of activity comparable to that of 2009, with the 20% downturn in Senaf turnover offset by higher trading on MTS.

The result was a small gain in share for the second tier, while electronic platform MTS scaled up from 7% to 7.9% at the expense of Senaf, whose 2010 share dropped to 3.7% of account-holder spot trades.
3. SECONDARY MARKETS IN 2010

3.3. OUTRIGHT TRADES IN STRIPPED DEBT

The strips market in Spanish debt commenced in 1998 with the first-time authorisation of bond stripping and reconstitution. A total of seven bonds were declared strippable in 2010 (2.30% April 2013; 2.50% October 2013; 3.30% April 2015; 4.0% April 2020; 4.85% October 2020; 4.65% July 2025 and 4.70% July 2041) while another two were redeemed (4.00% January 2010 and 3.25% July 2010). This left an end-2010 total of 30 principal strips with their respective coupon strips, covering a spectrum of maturities from 2011 to 2041, and with a total strippable volume of 596.50 billion euros, between principal (425.63 billion) and coupons (170.87 billion). As at 31 December stripped debt outstanding came to 37.64 billion.

The figure below tracks the progress of stripping since the year 2002. We can see that strips market activity has held generally stable, with its peak levels of 2007 followed by some tailing-off in 2008 and 2009. The outstanding balance, however, has kept growing steadily over the length of the period. Stripping activity moves up a gear in 2010, after staying broadly stable since 2002.
In 2010, this pattern changed with a spurt in stripping and reconstitution activity that carried the outstanding balance from 28.30 billion to 37.64 billion euros.

Average daily trading in the strips market stood significantly above the levels of 2009. The advance was common to both account holder and third-party trades.

Stripped debt turnover rises sharply with respect to the previous year.
3. SECONDARY MARKETS IN 2010

By reference, the most actively traded was the principal component (PO) of the Obligación 4.90% July 2040, which accounted for 11.0% of all strips traded in the account-holder segment. Next in line, with a share of 7.5%, was the PO of Obligación 5.00% July 2012.

3.4. REPO TRANSACTIONS

Before looking at the performance of the repos market we must distinguish between two types of admissible transactions, that is, buy-sell backs and blocked repos. Buy-sell backs are more liquid – the security acquired can be sold at any time – and, as such, have traditionally featured larger in account-holder trading. Blocked repos, however, can only be sold up to the repurchase date set in the original transaction. This makes them more suited for account-holder to client trades, since there is no risk of the third party failing to return the security on the preset date.

Turnover in buy-sell backs headed higher in the year (7.99 trillion euros against 7.30 trillion in 2009).
Of the total, 93% fell to account-holder trades and the rest to trades with third parties. Bonos and Obligaciones were by far the most popular underlying asset, accounting for 84% of buy-sell back transactions against the 16% of Letras and the residual share of strips. Terms again tended to the shortest end, with overnight transactions dominating strongly.

Meantime, blocked repo trading was down 33% with respect to 2009 (5.77 compared to 8.64 trillion euros). This instrument is the exclusive preserve of third-party trades. In effect, the scant wholesale activity in repos apparent since 2006 urged the Banco de España in its Circular 2/2007 of 26 January to prohibit this trading modality among account holders. Demand was again strongest for transactions based on Bonos and Obligaciones, which accounted for 69% of total trading ahead of Letras (27%) and strips (4%). Short terms were also the most prevalent in this trading segment.
3. SECONDARY MARKETS IN 2010

Source: Banco de España
Museo Würth La Rioja. La Rioja (opened 2007)
4. DISTRIBUTION OF THE CENTRAL GOVERNMENT DEBT PORTFOLIO

4.1 DISTRIBUTION OF GOVERNMENT DEBT HOLDINGS

The distribution of unstripped Government Debt in held-to-maturity portfolios has undergone major changes since 1999 (year of the euro’s debut), when credit institutions were the biggest owners. Since then, they have steadily lost ground to non resident investors, who have raised their share of Debt holdings from 27% in 1999 to 45.5% in 2010. Households, companies and public authorities have also enlarged their portfolio share against the declining weight of investment funds, pension funds and insurance corporations. Note that the Spanish public authorities group includes the Social Security Reserve Fund, while non financial companies include the Wages Guarantee Fund.

The salient development of 2010 was the four-point decline in the ownership share of credit institutions, in contrast to the slightly higher weight of investment and pension funds and insurance corporations. Non residents were yet again the single biggest owner group, accounting for 45.5% of Central Government Debt holdings.
At the short end of the maturities range, we observe that non resident investors have since 2009 supplanted credit institutions as the main holders of Letras del Tesoro, completing their run-up from 4% in 2002 to around 50% at the 2010 close. This increase, plus the higher shares falling to public authorities, insurance corporations and pension funds, coincided with a decline in resident credit institution ownership in both absolute and relative terms. The work of the Primary Dealers group in the Letras market has much to do with their improved distribution outside Spain, alongside their growing appeal to European investors as diversification instruments in their short-term government securities portfolios.
Since 1999, non resident investors have headed the Bonos and Obligaciones ownership list. And they retained this lead at end-2010 with 44.5% of total holdings, reversing the small decline of prior years. Households, companies and public authorities worked up from a 6% share in the year 2002 to 16% at the 2010 close. Public authorities were the prime movers within this group, accounting for 13% of total Debt holdings.
A look at the distribution of the stripped Debt held-to-maturity portfolio (principal plus coupons) reveals that non residents’ share fell by 10 points in 2010 after the preceding surge in ownership (from 23% in 2003 to 44% in 2009). The result is that leadership of this segment has passed to insurance corporations and pension funds with 35% of holdings at the 2010 close.

Investment funds, meantime, kept up their 8% share after a sharp fall in ownership since 2003, while non financial companies moved up to 11% to stand neck in neck with credit institutions.

On a principal and coupon split, we find that in 2010 resident insurance corporations and investment funds retained their preference for principal strips, while non residents invested in principal and coupons in approximately equal measure. Credit institutions, again, opted primarily for coupon strips, due perhaps to their intermediation role with end investors with a preference for principal.
The foregoing analysis refers to Debt holdings to maturity. But it is also worth looking at movements in registered Debt holdings (the held-to-maturity portfolio minus repo sales plus repo purchases).

At the 2010 close, 69% of Letras holdings to maturity in credit institution portfolios had been ceded via repos or buy-sell backs, primarily to insurance corporations, investment and pension funds, non financial companies and public authorities. Similarly, in Bonos and Obligaciones, 52% of credit entity holdings to maturity had been assigned via these same instruments mainly to investment funds, pension funds, non financial companies and non residents.

Turning to stripped Debt, around 36% of the coupon instruments held to maturity by credit institutions were subject to repo or buy-sell back arrangements with investment or pension funds. Insurance corporations made similar use of principal-only strips, with 40% of their portfolio assigned under these

Credit institutions refinance their portfolios via repo transactions with investment funds, pension funds, non financial companies and public authorities.
arrangements to investment funds and credit institutions. Non residents, finally, stayed true to their custom of retaining Spanish Debt holdings to maturity.

The conclusion is that credit institutions maintained large held-to-maturity portfolios of Public Debt, which they refinanced through repo arrangements with investment funds, pension funds, non financial companies and public authorities. The latter, in exchange, were facilitated access to very short-term securities of superior credit quality.

4.2 NON RESIDENT DEBT HOLDINGS: GEOGRAPHICAL DISTRIBUTION

The geographical distribution of non resident Spanish Debt holdings is a matter of considerable interest. By area, the largest shares in 2010 corresponded to France (25%), Asia, Africa and others (19%), Benelux (14%) and Germany (7.5%).

The main long-term changes in distribution have been, firstly, the declining share of the United Kingdom, which was the largest source of foreign ownership until 1999 but has since reduced its share dramatically, from 42% to 7%, and, secondly, growing investment from Asia, Africa and other areas, which have raised their combined participation from 2.5% in 2000 to 19% at end-2010.

European Union investment accounted for around 68.5% of the year-end total. Outside the EU, the top investor regions were Asia, Africa and others followed by Japan, with a year-end share of 6.5%.
By type of investor, a salient development has been the growing share of central banks and international organisations, from just 2.4% of non resident ownership in 1999 to 33% of the total in 2010. Households and companies also grew their share to 28%, thanks to increased investment by the latter group. We can see from the figure below that non resident holdings by investor group were along similar lines to the year 2009.

33% of non resident ownership corresponded to central banks and 28% to households and companies. The remaining 39% was split between investment and pension funds and financial institutions.
4. DISTRIBUTION OF THE CENTRAL GOVERNMENT DEBT PORTFOLIO

4.3 FONDTESORO

Fondtesoro are investment funds holding most of their assets in Central Government securities. They are run by management companies bound by a collaboration agreement with Tesoro Público to fulfill certain specifications.

Since their start-up in 1990, Fondtesoro have served as a demand source for Central Government Debt. They had something of a boom year in 1997 with 652,839 unitholders and 13.45 billion euros in assets under management. However, except for a brief revival in 2008, they have tended to lose out since to competition from equity investment and other rival products (primarily guaranteed funds and high-yield deposits).

<table>
<thead>
<tr>
<th>Year</th>
<th>No. of unitholders</th>
<th>Assets under management</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Long term</td>
<td>Short term</td>
</tr>
<tr>
<td>1995</td>
<td>111,751</td>
<td>254,127</td>
</tr>
<tr>
<td>1996</td>
<td>197,485</td>
<td>345,876</td>
</tr>
<tr>
<td>1997</td>
<td>233,640</td>
<td>419,199</td>
</tr>
<tr>
<td>1998</td>
<td>253,630</td>
<td>391,011</td>
</tr>
<tr>
<td>1999</td>
<td>208,396</td>
<td>350,393</td>
</tr>
<tr>
<td>2000</td>
<td>122,542</td>
<td>283,461</td>
</tr>
<tr>
<td>2001</td>
<td>114,980</td>
<td>348,305</td>
</tr>
<tr>
<td>2002</td>
<td>110,419</td>
<td>393,474</td>
</tr>
<tr>
<td>2003</td>
<td>95,856</td>
<td>379,831</td>
</tr>
<tr>
<td>2004</td>
<td>82,906</td>
<td>325,534</td>
</tr>
<tr>
<td>2005</td>
<td>81,614</td>
<td>304,680</td>
</tr>
<tr>
<td>2006</td>
<td>70,245</td>
<td>288,941</td>
</tr>
<tr>
<td>2007</td>
<td>60,609</td>
<td>267,566</td>
</tr>
<tr>
<td>2008</td>
<td>53,383</td>
<td>273,651</td>
</tr>
<tr>
<td>2009</td>
<td>50,533</td>
<td>183,631</td>
</tr>
<tr>
<td>2010</td>
<td>44,509</td>
<td>116,006</td>
</tr>
</tbody>
</table>

(*) Percentage invested in Fondtesoro out of total assets under management in investment funds
There are three types of Fondestoro product: short-term Fondestoro, long-term Fondestoro and Fondestoro Plus. Their main features are as shown in the table below. Short-term Fondestoro invest in money-market assets so their risk is near to zero. Long-term Fondestoro can also invest in longer-term bonds, so tend to offer a higher return in exchange for the investor taking on rather more risk. Fondestoro Plus are fixed-income balanced funds authorised to invest up to 30% of their assets in equity securities. They are accordingly a riskier product than the previous two, but also offer more return. All of them must hold at least 70% of their assets in Central Government Debt, but are free to invest part of the remainder in other high quality fixed-income instruments. The fees fund managers can charge are also capped at a specified percentage, as shown in the table below.

<table>
<thead>
<tr>
<th>Type</th>
<th>Minimum investment in Central Government Debt</th>
<th>Maximum investment in other fixed-income securities</th>
<th>Maximum investment in other fixed income and equity</th>
<th>Maximum management and custody fees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Short-term Fondestoro</td>
<td>70%</td>
<td>30%</td>
<td></td>
<td>1.05%</td>
</tr>
<tr>
<td>Long-term Fondestoro</td>
<td>70%</td>
<td>30%</td>
<td></td>
<td>1.25%</td>
</tr>
<tr>
<td>Fondestoro Plus</td>
<td>70%</td>
<td></td>
<td>30%</td>
<td>1.35%</td>
</tr>
</tbody>
</table>

The regulations governing Fondestoro have been modernised in recent years. The latest reform of agreements was instrumented through Order EHA/3465/2008 of 26 November, amending Order EHA/2688/2006 of 28 July on collaboration agreements with investment funds specialising in Spanish Government Debt. The goal once more was to widen the choice available to fund managers by allowing them to compute the asset-backed securities issued by FTVPO (with ICO warranty) towards the 70% minimum to be invested in government debt, according them the same treatment in this respect as the securities issued by FTPymes.

The current rules, then, give Fondestoro managers more leeway in deciding their investment policies. Our next table shows how this has translated as a decline in their Debt holdings, from almost
98% to 73% in 2010. In contrast, they have increased their investment in asset-backed securities (FTPymes) with a government guarantee, and other fixed-income products.

Recent trends in the Fondtesoro universe have been towards heavier investment in Letras del Tesoro, though the scale has reduced somewhat in 2010, and a progressive shift out of repos into longer-dated instruments, above all bonds maturing between 2012 and 2016.
### DISTRIBUTION OF FONDTESORO INVESTMENT IN CENTRAL GOVERNMENT DEBT

<table>
<thead>
<tr>
<th>Year</th>
<th>Letras del Tesoro</th>
<th>Bonos and Obligaciones</th>
<th>Repos</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>18.96</td>
<td>34.01</td>
<td>47.03</td>
</tr>
<tr>
<td>2001</td>
<td>21.12</td>
<td>26.73</td>
<td>52.14</td>
</tr>
<tr>
<td>2002</td>
<td>24.46</td>
<td>19.17</td>
<td>56.38</td>
</tr>
<tr>
<td>2003</td>
<td>25.66</td>
<td>16.45</td>
<td>57.90</td>
</tr>
<tr>
<td>2004</td>
<td>17.59</td>
<td>24.87</td>
<td>57.54</td>
</tr>
<tr>
<td>2005</td>
<td>16.03</td>
<td>28.05</td>
<td>55.92</td>
</tr>
<tr>
<td>2006</td>
<td>13.24</td>
<td>26.98</td>
<td>59.78</td>
</tr>
<tr>
<td>2007</td>
<td>15.16</td>
<td>23.38</td>
<td>61.45</td>
</tr>
<tr>
<td>2008</td>
<td>41.08</td>
<td>15.19</td>
<td>43.73</td>
</tr>
<tr>
<td>2009</td>
<td>41.20</td>
<td>35.28</td>
<td>23.52</td>
</tr>
<tr>
<td>2010</td>
<td>38.61</td>
<td>44.81</td>
<td>16.58</td>
</tr>
</tbody>
</table>