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Acronyms

ACGR	Annual Corporate Governance Reports
AIAF	Asociación de Intermediarios de Activos Financieros/Spanish Brokers' Association
ASCRI	Asociación Española de Entidades de Capital-riesgo/Spanish association of venture capital firms
BME	Bolsas y Mercados Españoles
CEBS	Committee of European Banking Supervisors
CESR	Committee of European Securities Regulators
CNMV	Comisión Nacional del Mercado de Valores
DAC	Directive on Capital Requirements
DSI	Directive on Investment Services
EBITDA	Earnings Before Interests, Tax, Depreciation and Amortization
EC	European Commission
EFAMA	European Fund and Asset Management Association
ESI	Investment services company
ETF	Exchange Traded Funds
EU	European Union
EVCA	European Private Equity & Venture Capital Association
FIAMM	Money market fund
FIM	Securities investment fund
FRA	Forward Rate Agreement
GDP	Gross Domestic Product
IGBM	Índice General de la Bolsa de Madrid/Madrid Stock Exchange General Index
IIC	Collective Investment Schemes
IOSCO	International Organization of Securities Commissions
IPO	Initial Public Offerings
LMV	Ley del Mercado de Valores/ Securities Markets Law
MAB	Mercado Alternativo Bursátil/Alternative Stock Market
MEFF	Mercado Español de Futuros y Opciones Financieros/Spanish market in financial futures and options
MFAO	Mercado de Futuros del Aceite de Oliva/Olive oil futures market
MiFID	Markets in Financial Instruments Directive
OECD	Organization for Economic Co-operation and Development
PER	Price Earnings Ratio
RD	Royal Decree
RDL	Royal Decree Law
ROE	Return On Equity
SENAF	Sistema Electrónico de Negociación de Activos Financieros / An electronic trading platform for Spanish public debt
SGIIC	Collective investment scheme management company
SIBE	Sistema de Interconexión Bursátil Español/Spanish electronic market
SICAV	Open-end investment company
UCITS	Undertakings for Collective Investment in Transferable Securities

Securities markets and their agents: situation and outlook

(*) This article has been prepared by the staff of the CNMV Research and Statistics Directorate.

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Introduction

The growing importance of capital markets as a channel for saving and investment flows, plus their role in the generation and spread of financial turbulence, calls for a close and constant watch on their activities and participating agents in order to assess the state of play and the factors potentially shaping their future performance. This six-monthly report, inaugurated with the present issue, provides an overview of Spanish securities markets and their participants in the frame of the relevant international context. It also looks at the factors determining volumes and prices in principal trading venues, and the activity of intermediaries and investment vehicles. In general, this analysis will extend to the six months preceding the report's publication date, except for certain aspects relating to market operators, where the reference period will be the whole of the preceding year.

With this publication, the CNMV wishes to offer a systematic analysis of the general framework of its operations; convinced that the proper functioning of financial product markets depends on the availability of reliable and timely information, so sellers, buyers and intermediaries can arrive at an informed decision. Indeed, the existence of an adequate volume of public information underpins the three objectives legally assigned to the CNMV: the transparency of securities markets, efficient price formation and the protection of investor interests.

There is currently an abundance of studies and periodic reports examining the performance of the markets and the macroeconomic framework in which they operate. The *Report on securities markets and their agents: situation and outlook* does not seek to compete with such publications, but to add to them from a supervisory perspective. It will accordingly lend much of its attention to the implications of key macro-financial developments for issuers and other securities market participants, including investment service providers and the managers of investment vehicles.

The publication of this report is especially timely, coming just a few months after the crisis unleashed in the US mortgage market, which has caused serious disruption in financial markets. Many of the developments we describe have been heavily influenced by this period of turmoil. And future prospects are, in many cases, bound in with the length and the macro and financial fallout of the international crisis. Finally, our analysis would not be complete without detailed attention to the latest legislative novelties in Europe. These have brought substantial changes in the competitive framework of the national financial industry and, as such, pose significant challenges to market agents and infrastructure managers.

The report is organised as follows: the second section looks at national and international economic and financial developments; the third reviews the current situation of national equity and fixed-income markets; the fourth is devoted to market agents; and the fifth examines what are seen as the main novelties in European legislation and market infrastructures. Finally, the sixth section offers some conclusions.

1 Executive summary

- The crisis emanating from the US sub-prime mortgage market was among the factors dominating the progress of international and domestic financial markets over the last quarter of 2007 and opening months of 2008. As well as generating disruption episodes of varying intensity, the crisis prompted a revise-down of global macroeconomic expectations, provoking liquidity shortages in interbank and fixed-income markets and a re-pricing of financial instrument risk. Leading central banks responded with a string of cash injections, with many also switching over to a more expansionary monetary policy.
- Six months on from the start of the crisis, the market climate is still one of relative instability. The signs of interbank market normalisation are tentative at best, structured product markets are still having to cope with high spreads and sluggish issuance and trading activity, and equity prices have experienced a sharp run-down accompanied by heightened volatility.
- The recent turbulences have laid bare a series of shortcomings in market operation. Specifically, the recent episodes evidence a lack of transparency about the nature and intrinsic risks of some complex structured products and certain institutions' exposure to the vehicles worst hit by the sub-prime crisis. Rating agencies too have to shoulder some of the blame, and the discussions now underway in international forums about refining the legal framework for their activity must be regarded as a welcome advance.
- World macroeconomic conditions continued robust in 2007, and forecasts point to full-year growth rates verging on 5%. But the picture is changing. Projections for the next few quarters of 2008 augur a moderation of GDP growth in main geographical areas, due to the prolongation of financial market disruption, rising commodity prices and the downturn in the US real estate cycle. The main risks confronting the baseline economic and financial scenario for the world economy lie in the appearance of sizeable losses on listed company balance sheets, the persistence of tight liquidity in financial markets and a sharper-than-expected correction in domestic demand growth in main developed countries, as the availability of credit constricts.
- The macroeconomic scenario in Spain has been marked by the deceleration path initiated in mid 2007. One contributory factor was the slackening pace of domestic demand, particularly in construction and consumer spending. In general, the Spanish economy confronts the same risks as any other, with an appreciable exposure to real estate as its chief vulnerability factor. However it also enjoys a reserve of strengths, like the sound balance sheets of its financial institutions or its ample room for fiscal policy manoeuvre.
- Domestic financial markets traced a similar course to their international counterparts. In equities, financial turbulence triggered a price correction that cut deepest in the financial and real estate sectors. Trading volumes expanded strongly in 2007, before falling off slightly in the first quarter of

2008¹. These movements were accompanied by an upswing in volatility, albeit from a baseline of historic lows. Spanish stock markets, which had enjoyed a bull run through 2007, commenced 2008 with significant price falls in line with European peers.

- The dominant notes on fixed-income markets have been the large rise in risk premiums, affecting even the highest quality issuers, from 20 basis points in August 2007 to more than 80 in the opening weeks of 2008², and the contraction of market liquidity extending to the instruments derived from the securitisation of bank loans. The result was an issuance stall in the last quarter of 2007 and the first of 2008, the exceptions being commercial paper³ and asset-backed securities⁴. The latter are mainly being acquired by the original seller institutions, to stock up on liquid assets available for sale or for use as collateral in Eurosystem operations.
- The near-term performance of Spanish financial markets will hinge on the pace of normalisation of international financial activity and the macroeconomic impact of the recent turmoil. The main factors in Spain's favour are its continuing growth vigour despite the slowdown, and the financial strength of most corporate issuers – with little exposure to the assets worst hit by the international crisis. Conversely, its weak points are the uncertain prospects for the real estate sector and the high leverage of certain corporate players.
- For now, financial market operators are unlikely to suffer any serious dent in their business figures, although the pace will almost certainly slow. Most Spanish investment firms posted profits growth in 2007, and are sufficiently well cushioned financially to cope with a lull in market activity. However, all providers of investment services (investment firms and credit institutions) will have to tighten up their risk control systems in a frame of acute price volatility, as well as adapting to the strictures of the MiFID and to the more intense competition building in the industry over recent years.
- Liquidity problems on certain markets may make some instruments harder to value. Listed companies should therefore redouble their efforts at transparency and information quality, in line with international accounting standards, to ensure there is no discrepancy between their published financial statements and the underlying financial reality.
- The collective investment scheme (CIS) industry has only scant exposure – either directly or through holdings in foreign schemes – to instruments linked to US sub-prime mortgages. However, assets under management have traced a downward course since the first half of 2007 as a result of rising interest rates, which have lowered the returns earned on CIS holdings, and legislative changes that removed many of their tax advantages. The financial market

1 Turnover on the Spanish stock market moved up 44% in 2007 (see table 9). In the first quarter of 2008, it recorded an 8.4% decline in year-on-year terms.

2 Aggregate risk premium based on the five-year CDS of Spanish issuers.

3 Commercial paper issuance was €442,000 million in 2007 against the €334,000 million of 2006.

4 Asset-backed security issuance exceeded €141,600 million in 2007 vs. €91,600 million in 2006.

disruption of the closing months of 2007 only aggravated these trends, due to investors' heightened risk perception and, especially, a crowding-out effect as the banks engaged in a battle for deposits to cover their liquidity needs⁵.

- The percentage of illiquid assets in CIS portfolios is reasonably low (a little over 6%). However, the decline in trading on some fixed-income markets means management companies must keep a close eye on portfolio liquidity and utilise suitable valuation benchmarks for instruments that can no longer count on a reliable market reference. Also, mounting competition from bank deposits means they must make doubly sure that the mechanisms to prevent conflicts of interest between managers and the bank groups many of them belong to are operating effectively.
- Regulatory changes are also high on the sectoral agenda. The biggest challenges derive from the implementation of the MiFID and recent initiatives in post-trade services that may affect the internal organisation and competitive framework of Spanish intermediaries and infrastructures. The goal, in the latter case, is to ensure the full integration of Spanish clearing and settlement facilities within the European system, and this may call for the removal of singularities that hinder interoperability with other countries.

2 Macro-financial conditions

2.1 International economic and financial developments

Summer 2007 marked the start of a period of disruption on international financial markets with the detection of a large wave of defaults in the US sub-prime segment (of high-risk mortgages). The first signs of crisis were a sudden slump in the value of the securities backed by these loans and the resulting capital losses of the invested institutions. Next came a brusque revise-down of the ratings assigned to certain structured financial products, causing solvency difficulties among the monolines insuring their credit risk. These episodes shook agents' confidence in the information being given out on the credit quality of bank sector asset-backed securities, fuelling doubts about how deeply exposed each institution might be to the financial products worst hit by the turbulence. Among the immediate results were a major contraction in medium and long trades in non collateralised interbank markets, a large reduction in liquidity in structured product markets and other private fixed-income segments, and steeply rising credit spreads. Equity markets lasted out 2007 in fairly good form but suffered sharp corrections in the opening weeks of 2008 accompanied by an upswing in volatility.

Leading central banks stepped in with a string of cash injections in interbank markets, and some switched to a more expansionary monetary stance for fear that financial instability might hold back economic growth. In particular, the US Federal

⁵ The combined assets of the collective investment industry closed the year 2007 at €255 billion, 5.7% less than in 2006.

The US mortgage crisis causes successive waves of market turbulence...

... leading main central banks to adopt a more expansionary monetary stance, and to undertake a string of liquidity injections.

Reserve has applied an additional three cuts in 2008, one of an extraordinary nature, leaving its funds rate at 2.25%⁶. The European Central Bank (ECB) has so far kept its main refinancing rate at 4%⁷ with inflation creeping higher in recent months. However, the weakness betrayed by the latest euro area indicators has led the markets to discount a near-term easing move.

No signs yet of normalisation on interbank markets...

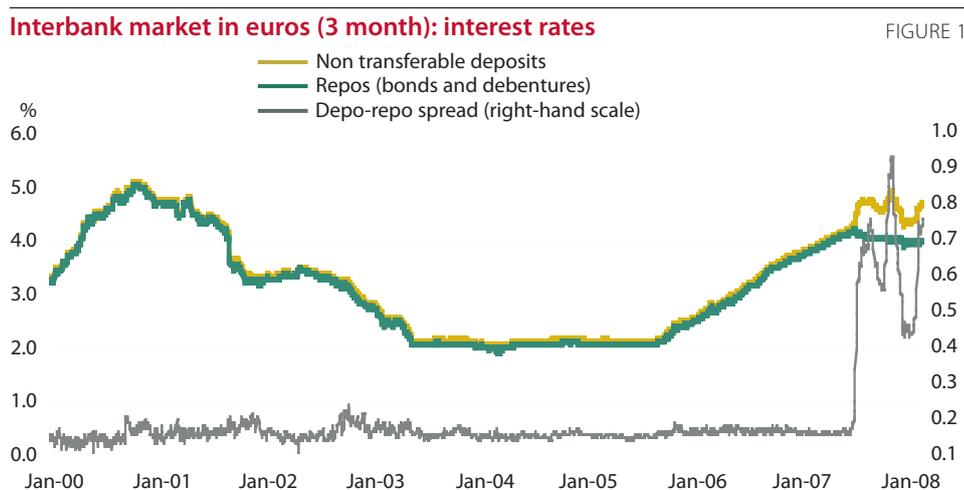
In forex markets, the US mortgage market debacle sent the dollar heading lower against main world currencies through 2007. This helped the Federal Reserve with its monetary expansiveness, but hindered the monetary policy execution of the economies most dependent on dollar imports. Also, financial market turbulence caused a re-pricing of the risk of financial instruments, which translated as the widespread unwinding of carry trades.

Financial markets have yet to show firm signs of normalisation. Hence the spread between the three-month rates of non transferable deposits and repos, which had eased to 40 basis points in February (see figure 1) from the highs of December 2007 (over 90 bp), rebounded sharply in March to over 70bp, significantly above its long-term average (below 10 bp). Turnover, meantime, staged a small recovery in the second half of March, with short instruments the most actively traded.

Meantime, structured product markets have continued sluggish, while the risk premiums of international bonds, as measured by various indicators (see figure 2), resumed an upward course in mid-October that has lifted them well above the levels of last August, coinciding with the start of crisis. For top-rated corporates, market turbulence has added around 130 bp to risk premiums in the US and 85 bp in Europe.

... while problems persist in structured product and international fixed-income markets, joined by high levels of stock market volatility.

Finally, stock markets followed up a fairly robust 2007 performance with a significant run-down in the first three months of 2008 (the more so in Europe). The other dominant note was the upswing in volatility, to the extent that the implied volatilities of main world bourses (especially in the United States) have reached levels unmatched since 2003 (see figure 3).



⁶ The Federal Reserve agreed the following 2007 reductions in its official interest rates: from 5.25% to 4.75% on 18 September, from 4.75% to 4.5% on 31 October and from 4.5% to 4.25% on 11 December.

⁷ The ECB raised its rates on two occasions in 2007: from 3.5% to 3.75% on 14 March and from 3.75% to 4.0% on 13 June.

Credit risk indices

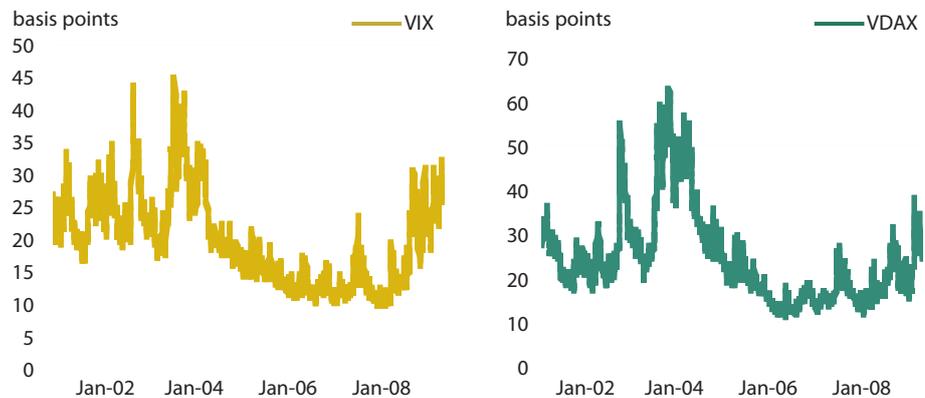
FIGURE 2



Source: Thomson Datastream. To 31 March.

Implied volatility

FIGURE 3



Source: Thomson Datastream. To 31 March.

VIX. Implied volatility of S&P 500 .

VDAX. Implied volatility of DAX.

World macroeconomic forecasts point to an appreciable growth slowdown in main economic areas...

World macroeconomic conditions continued robust in 2007, and forecasts point to full-year growth rates verging on 5%. But the picture is changing. Projections for the next few quarters of 2008 augur a moderation of GDP growth in main geographical areas due, among other factors, to the prolongation of financial market disruption. In particular, tougher borrowing conditions for households and companies could make serious inroads into domestic demand.

...with a significant degree of downside risk

This is not to say that the world economy will not stay reasonably vigorous for another year (see table 1), though the forecasts for some countries are highly uncertain, with estimate risk tilting to the downside. Of the risk factors for macroeconomic performance two loom largest: (i) a sharper than expected contraction of the US real estate market dragging the economy into recession and (ii) a prolonged liquidity shortage in world markets leading to a graver-than-expected credit constriction.

Gross Domestic Product (% annual change)

TABLE 1

	2004	2005	2006	2007	IMF(*) (**)		OECD(*)	
					2008F	2009F	2008F	2009F
World	4.9	4.4	5.0	4.9	3.7 (-0.5)	3.8 (-0.5)	-	-
United States	3.6	3.1	2.9	2.2	0.5 (-1.0)	0.6 (-1.2)	2.0 (-0.5)	2.2
Euro area	2.1	1.6	2.8	2.6	1.4 (-0.2)	1.2 (-0.7)	1.9 (-0.4)	2.0
Germany	1.1	0.8	2.9	2.5	1.4 (-0.1)	1.0 (-0.7)	1.8 (-0.4)	1.6
France	2.5	1.7	2.0	1.9	1.4 (-0.1)	1.2 (-1.0)	1.8 (-0.4)	2.0
Italy	1.5	0.6	1.8	1.5	0.3 (-0.5)	0.3 (-0.7)	1.3 (-0.4)	1.3
Spain	3.3	3.6	3.9	3.8	1.8 (-0.6)	1.7 (-0.8)	2.5 (-0.2)	2.4
United Kingdom	3.3	1.8	2.9	3.1	1.6 (-0.2)	1.6 (-0.8)	2.0 (-0.5)	2.4
Japan	2.7	1.9	2.4	2.1	1.4 (-0.1)	1.5 (-0.2)	1.6 (-0.5)	1.8
Emerging	7.5	7.1	7.8	7.9	6.7 (-0.2)	6.6 (-0.4)	-	-

Source: IMF and OECD.

(*) In brackets, percentage change versus the last published forecast. IMF, forecasts published April 2008 vs. January 2008. OECD, forecasts published December 2007 vs. June 2007.

(**)The national weightings used in January 2008 to calculate the aggregate growth of groups of countries were revised with respect to those presented in October in line with the new exchange rates used in the World Bank's PPP measure.

Performance of main stock market indices¹ (%)

TABLE 2

%	2008 (to 31 March)								
	2005	2006	2007	I 07 ²	II 07 ²	III 07 ²	IV 07 ²	%/Dec	% annual
World									
MSCI World	7.6	18.0	7.1	2.1	5.8	1.9	-2.7	-9.5	-5.1
Euro area									
Euro Stoxx 50	21.3	15.1	6.8	1.5	7.4	-2.4	0.4	-17.5	-13.2
Euronext 100	23.2	18.8	3.4	3.1	7.4	-4.8	-2.0	-16.2	-16.0
Dax 30	27.1	22.0	22.3	4.9	15.8	-1.8	2.6	-19.0	-5.5
Cac 40	23.4	17.5	1.3	1.7	7.5	-5.6	-1.8	-16.2	-16.5
Mib 30	13.3	17.5	-6.5	0.3	1.3	-4.4	-3.7	-17.3	-22.9
Ibex 35	18.2	31.8	7.3	3.5	1.7	-2.1	4.2	-12.6	-9.4
United Kingdom									
FT 100	16.7	10.7	3.8	1.4	4.8	-2.1	-0.2	-11.7	-9.6
United States									
Dow Jones	-0.6	16.3	6.4	-0.9	8.5	3.6	-4.5	-7.6	-0.7
S&P 500	3.0	13.6	3.5	0.2	5.8	1.6	-3.8	-9.9	-6.9
Nasdaq-Cpte	1.4	9.5	9.8	0.3	7.5	3.8	-1.8	-14.1	-5.9
Japan									
Nikkei 225	40.2	6.9	-11.1	0.4	4.9	-7.5	-8.8	-18.2	-27.5
Topix	43.5	1.9	-12.2	1.9	3.6	-8.9	-8.7	-17.8	-29.2

Source: Datastream.

¹ In local currency.

² Change over previous quarter.

³ Year-on-year change to the reference date.

2.2 Economic and financial developments in Spain

The Spanish economy entered a deceleration path in mid 2007. One contributory factor was the more subdued pace of domestic demand, especially in construction and consumer spending. Rising inflation and interest rates, plus the swelling household indebtedness of recent years eroded the growth of disposable income, causing a slowdown in private consumption and housing investment. However economic growth exhibited a more balanced mix, with less dependence on domestic demand and an improved contribution from the net exports side. Slower growth also meant a slower pace of job creation, especially in branches

The Spanish economy is experiencing a growth slowdown and an upturn in inflation.

linked to the construction and real estate sectors. On the inflation front, rising processed food and energy prices helped drive the headline rate above 4%, restoring the differential vs. the euro area to more than one percentage point. General government accounts again closed the year with a comfortable surplus. Current forecasts suggest that the uncertainty prevailing on financial markets and tougher corporate borrowing conditions will accentuate the consumption and investment slowdown in 2008⁸ (see table 3).

Spain: main macroeconomic variables (% annual change)

TABLE 3

	2004	2005	2006	2007	European Commission			
					2008S	2008A	2009S	2009A
PIB	3.3	3.6	3.9	3.8	3.4	3.0	--	2.3
Private consumption	4.2	4.2	3.7	3.1	3.3	2.7	--	2.4
Government consumption	6.3	5.5	4.8	5.2	4.8	5.0	--	4.9
Gross Fixed Capital Formation, of which:	5.1	6.9	6.8	5.9	5.0	3.0	--	0.6
Equipment	5.1	9.2	10.4	11.6	7.7	5.9	--	5.8
Exports	4.2	2.6	5.1	5.3	5.4	4.7	--	4.6
Imports	9.6	7.7	8.3	6.6	7.0	5.2	--	4.2
Net exports (growth contribution, pp)	-1.6	-1.7	-1.2	-0.7	-0.9	-0.5	--	-0.1
Employment	2.6	3.1	3.1	3.0	2.5	2.1	--	1.7
Unemployment rate¹	11.0	9.2	8.5	8.3	7.8	8.5	--	9.1
HICP	3.1	3.4	3.6	4.3	2.6	2.9	--	2.7
Current account (% GDP)	-5.9	-7.5	-8.8	-10.0	-9.7	-9.6	--	-9.8
General government (% GDP)	-0.3	1.0	1.8	2.2	1.2	1.2	--	0.6

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

S: Spring Report forecasts. A: Autumn Report forecasts.

1 Eurostat definition.

Spanish financial institutions start from a position of capital strength and above par profitability ratios...

In any case, Spanish financial institutions start from a sound financial position supported on high profitability ratios, strong capital adequacy and NPLs at historic lows. The Spanish mortgage market has no equivalent to the US sub-prime segment and loan-book quality is impressively solid. Also, their balance sheets are almost entirely free of assets linked to US sub-prime mortgages, and possible exposure via credit lines with other financial intermediaries invested in such products is on a negligible scale¹⁰. The liquidity shortages on the interbank market have caused less harm than in other countries, because most institutions have stocked up on funds in recent years through securitisation and medium- and long-term debt issues.

...as do a majority of Spanish non financial issuers. A small number are rather more vulnerable due to the build-up of debt.

Spanish non financial issuers also start from a comfortable position, endorsed by their high (though moderately contracting) profitability ratios. That said, some companies are considerably more exposed to adverse shocks by way of the large debt accumulated in the past few years, much of it going to finance corporate transactions.

The debt of non financial listed companies¹⁰ stood at 1.6 times equity in full-year 2007. This was a little less than at end-2006 (1.7 times), but well above the ratios of the start of the decade (1.06 times in 2001). As we can see from table 4, the debt

⁸ Table 3 offers the growth forecasts published by the European Commission in spring and autumn 2007. More recent activity, price and employment indicators set the growth consensus closer to 2.5% than the 3.0% shown in the table.

⁹ See Banco de España Financial Stability Report, November 2007.

¹⁰ Measured as debt (bonds and other marketable securities plus bank finance) to equity.

run-up was especially pronounced in “construction and real estate”, which accounted for over 47% of the total (against 10% at the start of the decade).

Despite this growth, interest expense on corporate debt has held at 33% of EBIT (earnings before interest and taxes) thanks to low interest rates, so the financial pressure weighing on the sector is still moderate in most cases. Also, the fact this debt has been arranged with relatively long maturities buffers firms from the worst effects of financial market turmoil¹¹.

The ratings assigned to Spanish companies also suggest a globally favourable outlook. These are generally high and recent reviews have concluded in upgrades in a majority of cases¹².

On the investor side, the first point to note is the conservative bent of their portfolios; far more pronounced than in other developed economies and quite possibly accentuated in recent months. Specifically, figures for the first three quarters of 2007¹³ show a mild contraction in the total assets acquired with respect to 2006, accompanied by portfolio reallocation towards low-risk financial instruments stronger on liquidity. Changes in the tax treatment of saving, effective from 1 January 2007¹⁴, and the sustained rise in interest rates have enhanced the attractiveness of more liquid assets, bank deposits particularly, to the detriment of investment funds. Indeed, banks deposits accounted for almost three quarters of household asset acquisitions to September 2007¹⁵. Fixed-income investment (both public and private) also gained some ground from riskier alternatives, with stock markets increasingly in the grip of uncertainty.

The conservative bias of Spanish investors has been accentuated by the international mortgage and financial crisis, driving more of them into banks deposits.....

¹¹Approximately 80% of the debt of non financial listed companies is classified as long term.

¹²Of the 14 revisions of Spanish companies' long-term ratings effected since June 2007 (by Moody's, S&P or Fitch), eight were upgrades.

¹³Banco de España financial accounts.

¹⁴Taxation of savings has become more neutral across instruments, terms and income brackets: (i) the term “special income” has been replaced by “saving income”, taking in all financial income regardless of the time over which it was generated, (ii) the same tax treatment is given to capital income and all other capital gains and losses. The standard 15% rate has been raised to 18%, whatever the income of the contributor. Withholding tax is also raised from 15% to 18%.

¹⁵Banco de España financial accounts. Cumulative four-quarter data.

Gross debt by sector: listed companies

TABLE 4

Million euros		2003	2004	2005	2006	2007
Energy	Debt	54,159	54,776	58,586	59,191	69,172
	Debt/Equity	0.98	1.06	0.93	0.89	0.78
	Debt/EBITDA ¹	2.92	2.78	2.41	2.17	2.48
	Interest expenses /EBIT ²	0.49	0.28	0.25	0.22	0.24
Construction and Real estate ³	Debt	24,552	32,293	48,324	111,000	138,933
	Debt/Equity	1.59	1.93	2.16	3.10	3.08
	Debt/EBITDA	5.91	5.71	6.51	11.52	10.83
	Interest expenses /EBIT	0.30	0.35	0.36	0.49	0.85
Industry	Debt	10,507	10,397	12,760	15,684	13,312
	Debt/Equity	0.61	0.69	0.75	0.78	0.61
	Debt/EBITDA	1.98	1.91	2.07	2.07	1.82
	Interest expenses /EBIT	0.25	0.15	0.15	0.18	0.17
Services	Debt	34,956	44,505	55,710	91,522	90,785
	Debt/Equity	0.89	1.61	1.7	2.52	2.16
	Debt/EBITDA	2.08	2.58	2.68	3.58	2.94
	Interest expenses /EBIT	0.31	0.37	0.30	0.41	0.31
Adjustments ⁴	Debt	-208	-5,566	-7,943	-11,199	-17,390
AGGREGATE TOTAL	Debt	123,966	136,405	167,438	266,198	294,811
	Debt/Equity	1.01	1.26	1.27	1.71	1.57
	Debt/EBITDA	2.8	2.9	2.9	3.86	3.91
	Interest expenses /EBIT	0.38	0.30	0.26	0.30	0.33

Source: CNMV.

1 Gross income.

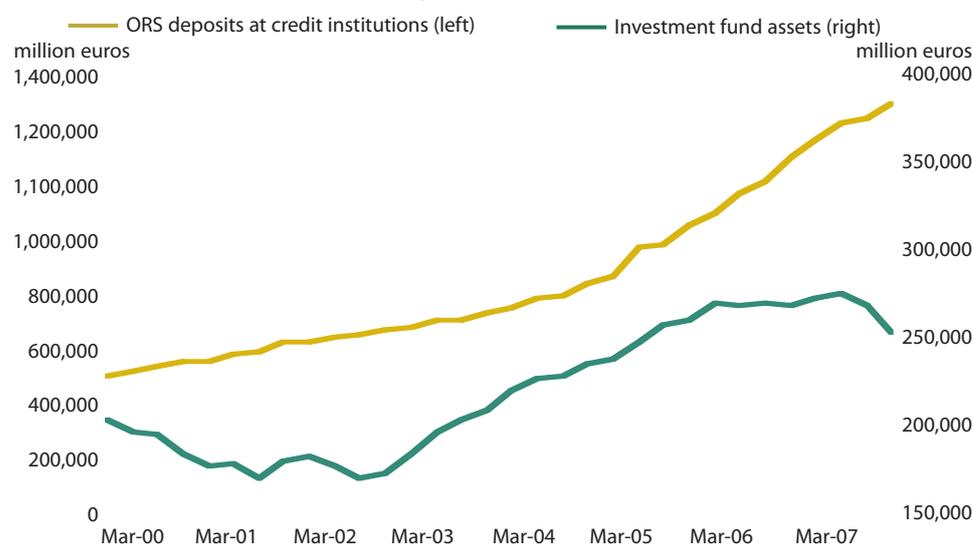
2 Earnings before interest and taxes

3 Including the Gecina debt carried by Metrovacesa under "liabilities directly associated with non current assets designated as available for sale and interrupted activities"

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

Investment fund assets vs. bank deposits

FIGURE 4



Source: CNMV and Banco de España.

ORS: Other resident sector.

The latest data, for the fourth quarter of 2007, confirm the flat evolution of investment fund assets due to the large volume of net redemptions. Fund earnings, though less than in past years, would not seem to warrant this scale of withdrawals,

which may have more to do with other factors like changes in the tax treatment of savings, rising interest rates (which favour bank deposits), the uncertainties engendered by the international mortgage and financial crises and, more recently, financial institutions competing for traditional liabilities to get round their funding difficulties on international markets (see section 4).

... to the detriment of investment funds, which last year suffered the largest outflows in a decade.

Investment fund subscriptions and redemptions (million euros)

TABLE 5

Category	Subscriptions				Redemptions			
	Q107	Q207	Q307	Q407	Q107	Q207	Q307	Q407
Fixed income ¹	31,679	27,498	30,581	26,566	32,087	28,502	28,983	32,606
Balanced fxd income ²	2,322	1,440	1,142	956	1,967	1,664	2,050	2,128
Balanced equity ³	909	753	635	452	1,023	894	999	1,107
Spanish equity	1,985	992	483	943	1,750	1,861	1,429	1,683
Intern. equity ⁴	5,519	4,925	3,215	2,971	4,987	4,011	5,242	5,834
Fxd-inc guaranteed	2,074	1,915	2,191	2,981	1,452	1,369	1,897	1,712
Equity guaranteed	1,800	1,858	1,316	3,096	2,785	2,238	2,142	4,437
Global funds	6,474	4,681	3,046	3,543	6,515	4,624	5,906	6,942
Hedge funds	47	29	32	243	0	0	0	2
Funds of hedge funds	9	614	233	215	0	2	11	53
TOTAL	52,817	44,705	42,875	41,967	52,567	45,165	48,659	56,504

Source: CNMV

1. Includes: Short-term, long-term and international fixed-income and money-market assets.

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

3. Includes: Balanced equity and balanced international equity.

4. Includes: Euro, international Europe, international Japan, international US, international emerging market and other international equity.

2.3 Outlook

Some aspects of this latest episode of financial turmoil bear similarities to earlier crises (the stock market crash of 1987, the Russian default and the collapse of Long Term Capital Management in 1998, the bursting of the “dot.com” bubble in 2000 or the terrorist attacks of 2001). As before, the result has been a widespread increase in the perception and price of risk that has pushed up volatility on international financial markets and prompted a flight to quality among the investor public.

This period of turbulences, which has some points in common with earlier crises...

The main difference this time round is possibly the dearth of liquidity affecting certain wholesale markets, which as well as limiting the funding channels available to banks speaks implicitly of a general crisis of confidence. Uncertainties will in all probability continue to predominate until the impact of the sub-prime crisis on corporate finances is fully out in the open, which will not be until companies release their income statements for the first half of 2008. The main risks for the baseline financial and economic scenario reside in: (i) the reporting of heavy losses on listed company balance sheets, (ii) the persistence of tight liquidity in financial markets causing severe constrictions in household and commercial lending, and (iii) as a result of the above, a sharper-than-expected correction in domestic demand.

... and others unique to itself, will only conclude when agents get back their lost confidence.

The Spanish economy confronts the same general risks as other economies. Greater exposure to the real estate cycle is perhaps its most vulnerable flank. But it also has compensating strengths like the soundness of its financial institutions and the fiscal policy leeway provided by a sustained general government budget surplus.

The Spanish economy is exposed to general and specific risks, but also has significant reserves of strength.

3 Spanish markets

3.1 Stock markets

The Spanish stock market followed up the strong gains of 2007 with a sharp run-down in the first months of 2008...

Spanish equity prices have been moving erratically since the onset of the international mortgage and financial crisis. Despite escalating market volatility, the main benchmark index (Ibex-35) closed 2007 with a sturdy gain of 7.3%, outperforming other comparable markets. However, the first three months of 2008 brought a price slide of over 10% and a renewed upswing in volatility, coinciding with a spate of negative newsflow on world economic activity. The Spanish index fell rather less steeply than other European exchanges (see table 2).

... which hurt some companies worse than others.

This performance was by no means common to all listed firms by sector or size. On the first score, the most heavily penalised were those linked to real estate (that is, construction and, especially, real estate services) and credit institutions, because of their exposure to financial turbulence. Meantime, telecommunications firms appear to have taken on a safe-haven status. By size, the worst performers were the small and medium caps, whose bear run of 2007 was prolonged through the opening months of 2008, taking year-on-year losses to around 30% in both cases. Even the large cap firms making up the Ibex-35 performed unevenly. Weighting played an important role here, with as much as 85% of the index's 2007 price variation tracing to just two companies.

Falling prices have taken the Ibex-35 price-earnings ratio (P/E) to recent lows...

The decline of the Ibex-35 since November 2007 has lowered the price-earnings ratio (P/E¹⁶) to just under 12, substantially below the average of recent years (16 since 2000). This multiple aligns Spanish market prices more closely with those of European than North American companies, in a break with the pattern observable since 2005.

Performance of Spanish market indices (%)

TABLE 6

	2004	2005	2006	2007	I 08 (to 31 March)	
					%/Dec	% y/y
Ibex-35	17.4	18.2	31.8	7.3	-13.3	-6.4
Madrid	18.7	20.6	34.5	5.6	-13.2	-8.6
Ibex Medium Cap	25.1	37.1	42.1	-10.4	-12.8	-26.9
Ibex Small Cap	22.4	42.5	54.4	-5.4	-11.5	-22.7
FTSE Latibex All-Share	31.0	83.9	23.8	57.8	-1.1	59.9
FTSE Latibex Top	28.1	77.9	18.2	33.7	0.2	35.4

Source: Thomson Datastream.

¹⁶P/E is the ratio between the price of a share (or index) and its earnings per share on a given date. Earnings per share can be expressed on a trailing or a forward basis. This report uses historical data from Thomson Datastream.

Performance by sector of the Spanish stock market (%)

TABLE 7

	2004	2005	2006	2007	I 08 (to 31 March)	
					%/Dec	% y/y
Steel	25.3	20.7	81.2	-17.5	-4.2	-12.0
Water	31.2	18.1	55.6	-0.8	2.8	11.2
Auto	0.6	21.8	171.1	0.0	-16.4	-25.7
Food and drink	1.3	10.4	14.6	10.8	-2.9	-0.7
Construction and construction materials	28.5	50.4	61.6	-12.0	-16.6	-28.4
Basic consumption	40.0	19.0	12.9	6.9	0.4	8.3
Discretionary consumption	33.7	24.8	21.2	-7.7	-17.0	-27.7
Electricity	19.6	32.9	46.1	16.9	-10.6	0.4
Financial companies	10.1	22.5	35.5	-10.5	-15.4	-25.3
Hotels	17.3	41.8	27.9	-25.0	-14.6	-44.2
Real estate	29.5	58.9	100.4	-42.6	-2.3	-42.8
Paper	30.2	13.7	36.6	-12.4	-15.4	-31.5
Chemicals	19.2	176.1	-20.4	-58.4	-3.5	-59.8
Tobacco	49.8	13.7	5.0	21.5	0.1	24.9
Telecommunications and media	16.7	-0.7	29.4	26.3	-13.2	8.5
Utilities	21.5	27.2	42.0	18.5	-8.9	3.9

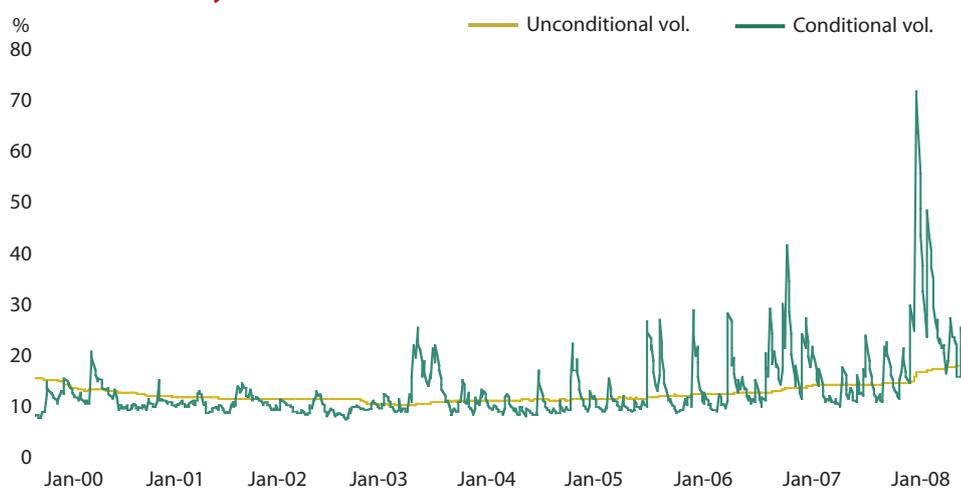
Source: Thomson Datastream. Monthly data.

Another trend was the significant widening of the earnings yield gap¹⁷ from its pre-crisis levels of last summer, with falling share prices post-crisis coinciding with a decline in long-term interest rates. This widening movement, though accompanied by some volatility, took the gap to a March level of 4.5% against a historical average since 1999 in the neighbourhood of 2%.

... and caused a widening of the earnings yield gap.

Historical volatility: Ibex-35

FIGURE 5



Source: Datastream and authors. Data to 31 March.

¹⁷The earnings yield gap reflects the return premium required to be invested in an asset carrying higher market risk than public debt. It assumes that the price of a share at any given moment is the present value of the future cashflows its ownership gives rise to. The cashflow discount factor will include the said premium. Its value can be expressed as: $\rho = \frac{1}{PER} - r$, in which P/E is the price earnings ratio and r the interest rate of long-term government bonds.

Asymmetry of Ibex-35 volatility

FIGURE 6



Source: Datastream and authors. Data to 31 March. The parameter represented uses an asymmetric GARCH model(*) to measure the sensitivity of conditional volatility to downside surprises.

(*) The specific equation is: $\ln(P_t / P_{t-1}) = \alpha + \varepsilon_t$
 with variance: $\sigma_t^2 = \omega + \theta \cdot \varepsilon_{t-1}^2 + \beta \cdot \sigma_{t-1}^2 + \eta \cdot \varepsilon_{t-1}^2 \cdot [1 \Leftrightarrow \varepsilon_{t-1} < 0] + u_t$

Arithmetical average of the correlation coefficients of Ibex-35 shares

FIGURE 7



Source: Datastream and authors. Data to 31 March.

Market uncertainty translates as greater volatility and an increased sensitivity to index falls...

...which stand as the principal risk factors, along with a rising correlation between asset returns.

Market uncertainty drove the index's historical volatility to beyond its 2002 highs in January, though with some degree of easing in the next two months (figure 5). The growth in the distribution asymmetry of daily Ibex-35 variations is significant here, since it means that price variability is becoming increasingly sensitive to downward movements in the index. This parameter has reduced slightly since its summer peak but continues at high levels (figure 6).

The growing correlation between different asset returns is a possible vulnerability factor for domestic financial markets. The returns of Spanish equity are now strongly correlated with those of other financial assets, notably European equity where the coefficient has been topping 80% for the last six months. The correlation among Ibex-35 shares has also been trending higher (to upwards of 45%). This

suggests there are common factors driving the performance of equity securities as a whole, possibly to do with economic globalisation and the greater liquidity of listed shares versus private fixed-income instruments at a time when investors are especially concerned about the depth of financial markets. In effect, an analysis of the pertinent measures (bid-ask spread, Kyle's lambda) shows that domestic equity markets remain strongly liquid.

Although the unsettled markets of the second half may have slowed the pace of equity issuance, full-year volumes were significantly up versus 2006 (almost five times higher) and 2005 (table 8). This increase is entirely a result of capital increases, since public share offerings were actually fewer than in 2006.

Equity issuance expands despite the year's unsettled climate, thanks to the large number of capital increases.

Equity issues and public offerings¹

TABLE 8

million euros	2004	2005	2006	2007	2007			2008	
					I 07	II 07	III 07	IV 07	I-08
CASH AMOUNTS²	21,735.6	2,960.5	5,021.7	23,757.9	803.9	11,218.1	4,337.2	7,398.7	9.5
Capital increases	18,748.0	2,803.4	2,562.9	21,689.5	696.1	9,896.5	4,273.8	6,823.1	0.0
Of which, rights offerings	1,101.9	0.0	644.9	8,502.7	0.0	334.2	3,485.2	4,683.3	0.0
Domestic tranche	537.9	0.0	303.0	4,821.4	0.0	334.2	2,449.6	2,037.6	0.0
International tranche	564.0	0.0	342.0	3,681.4	0.0	0.0	1,035.6	2,645.8	0.0
Public offerings	2,987.6	157.1	2,458.8	2,068.5	107.8	1,321.6	63.4	575.6	9.5
Domestic tranche	1,664.4	54.7	1,568.1	1,517.1	107.8	913.5	63.4	432.4	9.5
International tranche	1,323.2	102.5	890.7	551.4	0.0	408.1	0.0	143.3	0.0
NUMBER OF FILINGS³	42	27	30	35	7	10	6	12	1
Capital increases	37	25	21	26	6	8	5	7	0
Of which, rights offerings	4	0	8	8	0	2	2	4	0
Of which, bonus issues	15	6	0	0	0	0	0	0	0
Public offerings	7	2	14	12	1	3	1	7	1

Source: CNMV.

1 Issues filed with the CNMV. Initial and supplemental filings.

2 Excluding amounts recorded in respect of cancelled transactions.

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

Although the key factors for equity market performance remain generally supportive, with company earnings expected to stand up strongly, uncertainties are being stoked from two directions: (i) the fact no one is sure how the international mortgage and financial crisis will affect corporate balance sheets, and (ii) the risk for economic and employment growth in the economy as a whole, which right now is tilted to the downside. As we write, the combination of lower-than-projected corporate earnings for 2007 and US macroeconomic variables worse than the consensus view stands as the main risk scenario for world stock markets.

The main risks for equity markets lie with not knowing the true impact of the international mortgage crisis or the scale of economic slowdown.

Turnover in the Spanish stock market

TABLE 9

Million euros	2004	2005	2006	2007	Mar 07	Jun 07	Sep 07	Dec 07	Mar-08
All exchanges	642,109	854,145	1,154,294	1,667,219	418,540	441,725	372,131	434,823	383,254
Electronic market	636,527	847,664	1,146,390	1,658,019	415,857	439,664	370,417	432,081	380,935
Open outcry	5,194	5,899	5,318	1,155	574	209	98	274	44
Of which SICAVs ¹	4,541	4,864	3,980	362	258	57	32	15	3
MAB ²	-	-	1,814	6,985	1,771	1,605	1,369	2,240	1,966
Second Market	21	26	49	194	122	22	38	12	3
Latibex	366	557	723	868	217	226	209	216	306

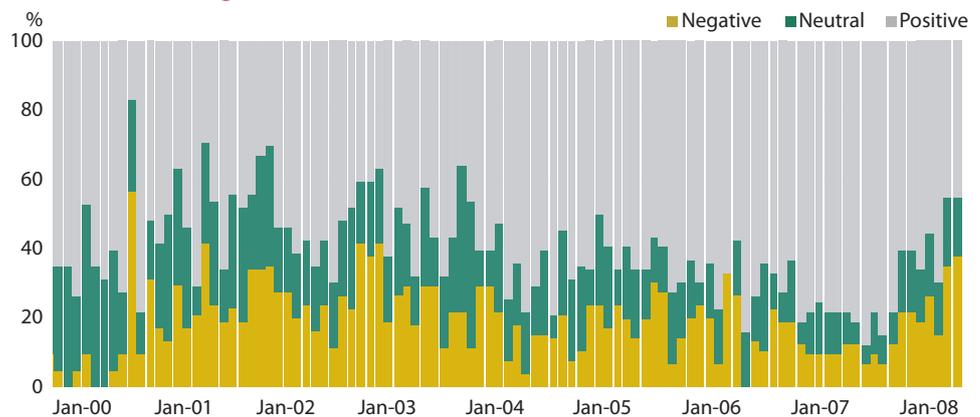
Source: CNMV.

¹ Open-end investment companies.

² Alternative stock market. Data since the start of trading on 29 May 2006.

Revisions of earnings forecasts. IBES

FIGURE 8



Source: Datastream and authors. Data to 31 March.

3.2 Fixed-income markets

Spanish fixed-income markets, like those elsewhere, are witnessing a flight to quality, as evidenced by a decline in long-term bond yields...

...and sharply rising issuer risk premiums (as gleaned from CDS).

Spanish government bond markets reacted to the crisis in much the same way as other international sovereign markets. Mounting investor uncertainty in the wake of the mortgage and financial turbulence prompted a flight to quality that sent long yields down to just over 4.0%, around 40 percentage points less than at the start of the crisis. This decline was accompanied by a widening yield spread versus the German benchmark; a trend shared with most of Europe's larger economies.

Corporate bond spreads also widened slightly with respect to governments and interbank deposits in tune with higher risk perceptions, though the fact is that the characteristics of private debt markets and the dearth of trading may also be distorting prices. For this reason, it was felt better to scrutinise aggregate data from the five-year CDS¹⁸ (credit default swaps) of the largest Spanish issuers.

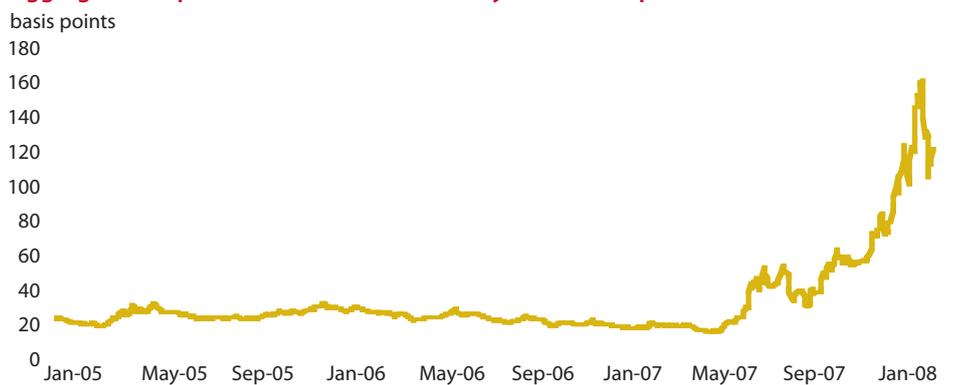
This analysis gives a much clearer picture of the rise in Spanish corporate risk premiums since the outbreak of the crisis. After a decline lasting several weeks, the aggregate premium resumed an upward course in October 2007 that shows not signs of petering out. As figure 9 shows, the five-year CSD aggregate stood upwards

¹⁸CDS are credit derivatives whose buyers acquire protection by transferring to the seller the credit risk associated to the underlying asset in return for an agreed regular fee. In the event of default, the seller pays the buyer the equivalent of the loss. CDS are quoted in basis points, and the fees payable by the buyer are calculated by multiplying the same by the notional amount of the contract.

of 100 basis points at the end of March; an over 90 point increase versus the pre-crisis level, which is slightly more than with other European references.

We can see from table 10 that tougher borrowing conditions caused companies to rein in debt issuance in the year's last quarter, pending the normalisation of the markets. The exceptions were commercial paper and asset-backed securities. Specifically, issues of commercial paper surged to €442,000 million from €334,000 million in 2006, and remained the most abundant in the closing quarter. Sales of asset-backed securities, meantime, recorded steady growth throughout the year up to and including the fourth quarter. Finally, 2007 issuance exceeded €141,600 million against the €91,600 million of 2006, with fourth-quarter volumes, moreover, actually tripling those of the previous quarter. The overall pattern of fixed-income issuance has remained much the same in 2008 albeit with sharply lower volumes compared to the first quarter of 2007. It should be stressed that a large portion of asset-backed securities are being acquired by the originating entities, in order to stock up on assets for eventual sale or for use as collateral against central bank funds. In fact, the disruption of international debt market trading – especially in instruments linked to the mortgage market – and the still unsettled state of interbank markets have led Spanish financial institutions to increase their recourse to Banco de España financing in the framework of Eurosystem monetary policy operations¹⁹.

Aggregate risk premium¹ based on the five-year CDS of Spanish issuers² FIGURE 9



Source: Thomson Datastream and authors. Data to 31 March.

1 Weighted for each issuer's capitalisation.

2 Data from July 2007 corresponding to eleven issuers (nine at the start of the sample).

¹⁹Spanish credit institutions' net borrowing from the ECB moved up from a monthly €20,000 million approximately between January and September (average of daily data) to over €44,000 million in December (January 2008, €39,644 million and February, €44,067 million). This represents an increase in Spanish banks' share of Eurosystem injected funds from around 4%-5% to over 9.0%, in line with our economy's relative weight in the euro area.

Gross fixed-income issues filed¹ with the CNMV

TABLE 10
2008

	2004	2005	2006	2007	2007				2008
					I-07	II-07	III-07	IV-07	I-08
NUMBER OF ISSUES	257	263	335	334	88	86	76	84	72
Mortgage bonds	17	21	37	32	8	10	9	5	9
Territorial bonds	2	3	6	8	2	1	4	1	7
Non convertible bonds and debentures	95	93	115	79	31	25	20	3	7
Convertible/exchangeable bonds and debentures	2	4	1	0	0	0	0	0	0
Asset-backed securities	48	54	82	101	17	25	19	40	18
Commercial paper facilities	62	80	83	106	28	23	20	35	27
Securitised	3	3	3	3	0	2	1	0	0
Other commercial paper	59	77	80	103	28	21	19	35	27
Other fixed-income issues	5	1	0	3	0	1	2	0	0
Preference shares	26	7	11	5	2	1	2	0	4
FACE VALUE million euros	329,962.3	414,253.9	523,131.4	648,757.0	173,448.3	156,957.4	163,782.9	154,568.4	117,385.3
Mortgage bonds	19,074.0	35,560.0	44,250.0	24,695.5	8,400.0	7,245.5	6,525.0	2,525.0	1,175.0
Territorial bonds	1,600.0	1,775.0	5,150.0	5,060.0	1,450.0	1,500.0	2,000.0	110.0	1,020.0
Non convertible bonds and debentures	38,123.6	41,907.1	46,687.5	27,416.0	9,982.0	9,427.0	7,750.0	257.0	604.1
Convertible/exchangeable bonds and debentures	67.4	162.8	68.1	0.0	0.0	0.0	0.0	0.0	0.0
Asset-backed securities	50,524.8	69,044.3	91,607.7	141,627.0	39,392.2	31,517.5	17,898.3	52,819.0	28,657.0
Domestic tranche	38,099.5	63,908.3	85,099.9	141,627.0	39,392.2	31,517.5	17,898.3	52,819.0	28,657.0
International tranche	12,425.3	5,136.0	6,507.8	0.0	0.0	0.0	0.0	0.0	0.0
Commercial paper ²	214,602.8	264,359.5	334,457.0	442,433.5	114,144.1	106,967.4	122,464.6	98,857.4	85,833.2
Securitised	3,723.6	2,767.5	1,992.7	464.8	156.0	138.8	85.0	85.0	133.0
Other commercial paper	210,879.2	261,592.0	332,464.3	441,968.7	113,988.1	106,828.6	122,379.6	98,772.4	85,700.2
Other fixed-income issues	428.1	89.3	0.0	7,300.0	0.0	225.0	7,075.0	0.0	0.0
Preference shares	5,541.5	1,356.0	911.0	225.0	80.0	75.0	70.0	0.0	96.0
Pro memoria:									
Subordinated issues	8,871.2	11,078.5	27,361.5	47,158.3	14,481.7	3,777.6	12,702.1	16,196.9	2,312.5
Covered issues	97,791.9	94,368.0	92,213.5	121,608.5	39,392.2	31,616.5	17,898.3	32,701.5	8,215.3

Source: CNMV.

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

² Figures for commercial paper issuance correspond to the amount placed.

Negative sentiment towards structured products has extended to the Spanish securitisation market, despite the high quality of issuer instruments.

Increased turnover in asset-backed securities in 2007 owes basically to their greater use in Banco de España monetary policy operations. Of remaining transactions, six securities alone account for over 50% of 2007 turnover, while fewer than a fifth of the securities admitted to trading generated any activity in the year (table 11). We can see then that growing distrust of structured products in the wake of the mortgage crisis has also made itself felt in the Spanish securitisation market in the form of a reduction in placements, desultory trading and a fall in the prices of the market's most liquid references. This scenario is basically about the diminishing worldwide popularity of structured products. Because the securitisation process in Spain generates high-quality assets supported on the low default rate of the underlying loans, the fact there is next to no transfer of credit risk, which will typically stay on the balance sheet of the originating bank, and the financial soundness of the banking sector (see text box on "Recent developments in securitisation" at the end of this section).

Asset-backed securities: number of securities needed to reach % of turnover (excluding operations with Banco de España)

TABLE 11

	No. of securities needed to reach % of turnover				% securities listed (excluding BdeE)	No. of securities outstanding
	25%	50%	75%	100%		
Jan 07	2	9	26	161	18.15%	887
Feb 07	1	4	12	175	19.62%	892
Mar 07	1	4	11	186	20.31%	916
Apr 07	1	2	9	146	15.82%	923
May 07	1	4	12	152	15.85%	959
Jun 07	1	2	8	168	17.32%	970
Jul 07	1	6	20	192	18.46%	1,040
Aug 07	1	6	27	177	16.48%	1,074
Sep 07	1	6	22	236	21.97%	1,074
Oct 07	2	5	18	171	15.60%	1,096
Nov 07	1	3	9	192	16.89%	1,137
Dec 07	4	11	28	218	18.84%	1,157
Jan-08	3	9	20	185	15.11%	1,224
Feb-08	2	6	21	209	16.98%	1,231
Mar-08	1	41	56	244	19.54%	1,249

Source: AIAF and authors.

The future performance of private fixed-income markets will hang on how far and fast confidence is restored in the financial situation of issuing companies, financial institutions most of all.

If all is well, the release of audited financial statements in the first half of 2008 should help reactivate interbank markets and allow the pricing system to resume its function as a discriminating mechanism for issue quality, ushering in a return to normality in corporate bond and other fixed-income issuance. Agents' risk aversion will not necessarily remit with the normalisation of market conditions. More likely is a repricing of financial instrument risk to beyond the levels of the pre-crisis period.

In any case, the mortgage crisis has spurred debate in national and international forums about the lessons to be learned. Among the most commented topics are ²⁰:

- **Rating agencies:** The role of these agencies in the international mortgage and financial crisis has been called into question in recent months. The controversy revolves basically around two points. The first is the possible existence of conflicts of interest in the conduct of their activity, localised in their role as advisers to issuing companies and the fact it is they – and not investors – who pay the valuation bills. The second is the methodology that agencies employ. In particular, criticisms have been levelled at their lack of transparency regarding the valuation criteria used (though this has improved somewhat in recent years), and at the relevance of their models – based on historical regularities – for a macro and financial landscape in constant flux. In any event, current ratings are unable to capture all the risks of the instruments under analysis. Agencies, we should remember, use an approach based on “expected loss” and may neglect improbable risk events that nonetheless have a high potential impact on asset returns (tail risk) and therefore a significant bearing on investment decisions. Finally, their ratings give no account of the instrument's liquidity; an all-important factor in the recent crisis.

The normalisation of debt market financing will come when confidence is restored in the issuing companies.

The international crisis has opened a number of debates, among them the role of the rating agencies, ...

²⁰These and another two topics were singled out as crisis lessons in reports by the Financial Stability Forum (Report of the Financial Stability Forum on Enhancing Market and Institutional Resilience) and the International Monetary Fund (Global Financial Stability Report), published in April 2008.

Hence the discussions underway about refining the legal framework for their activity along the lines followed in the United States. The first step promises to be a reform of the rating agency code of conduct drafted by IOSCO. This code can provide a platform for tightening up the sector's self-regulation mechanisms and generalising rules of conduct subject to supervisory oversight.

... problems of market transparency ...

- **Market transparency:** One of the roots of the credit market crisis was the difficulty knowing the real extent of financial institutions' exposure to certain kinds of risk. The culprits in this case were new credit transfer mechanisms, the extreme complexity of structured products and the scant information given out about the nature and performance of their underlying assets. Also, some markets – typically fixed income – lack effective disclosure pathways for important pre- and post-trade variables. All these shortcomings must be addressed by regulatory reforms that ensure investors a better quality of information.

... and the difficulties involved in valuing complex products.

- **Need for standardisation:** The problems brought to light in markets for complex products call for a reflection, at least, on the virtues of more standardised investment and financing instruments. The industry itself might wish to think about proposing categories of structured products that lend themselves to accurate valuation and could give rise to markets of adequate depth.

Recent developments in securitisation

The growth of the securitisation market in these last few years evidences how the practice of securitisation has become increasingly widespread among financial institutions. The need to draw in funds to cover their rapidly expanding mortgage business positioned banks and savings banks from the outset as the main sellers of securitised issues (between 94% and 97%). The year 2007 brought some important novelties in this market. Savings banks were again the biggest source of asset-backed securities (over €64,000 million), but with the bank segment coming up fast (+72%) to over €59,000 million at the annual close. This trend would be at least partly due to their eligibility as collateral in ECB financing operations. Note also the increased representation on the seller side of institutions like the Instituto de Crédito Oficial (ICO). Finally, non financial companies raised their share but are still a marginal presence only. Foreseeably this will change as market borrowing conditions normalise, given the value of such instruments to non financial firms as an alternative source of finance or a risk management tool.

In tandem with this increase in the number and nature of entities securitising on a regular basis, the range of assets being packaged has also grown with time. Although mortgage securitisation (via MBS²¹ or ABS²² backed by mortgage loans, mortgage bonds or developer loans) remains the dominant mode in the securitisation industry, in the last year its relative weight has dropped to 63% of operations compared to 69% in 2006. The low (though slightly rising) NPL ratios of home purchase loans confer a quality seal on these securitised assets. The advance in other financial instruments is primarily concentrated in the commercial and other loans categories.

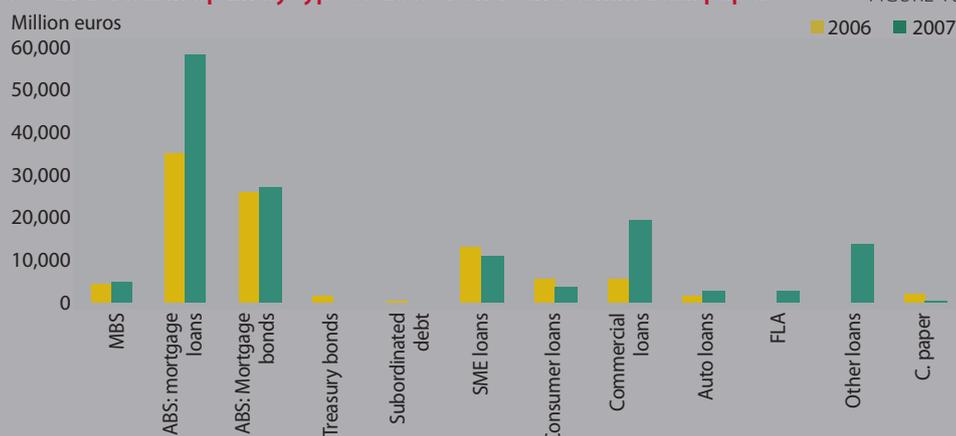
²¹Mortgage-backed securities.

²²Asset-backed securities.

As regards the investor public, there are various points to make. Firstly, that we are looking at a purely institutional market. The sophisticated financial structure of these products and the valuation difficulties they pose means they are mainly directed at qualified investors. Secondly, Spanish financial institutions have been so eager to acquire them for funding purposes that they now account for 66% of total subscriptions as against 30% during most of the last decade. It is this growth, along with the post-crisis lull in international markets, that explains the dwindling share of non resident investors, from 66% in 2006 to just 34% in 2007.

Securitisation in Spain by type of asset: bonds and commercial paper

FIGURE 10



Source: CNMV.

FLA: Financial lease arrangement.

Securitisation in Spain 2007: subscriber sector and issue ratings

TABLE 12

Million euros	AAA	GROUP A ¹	GROUP B ²	GROUP C ³	TOTAL	% total
Financial institutions	87,375	2,744	2,415	820	93,353	66
Banco de España						
Credit institutions	83,303	2,640	2,259	787	88,989	63
Spanish residents	81,654	2,610	2,224	787	87,274	62
Foreign residents	1,650	30	36	0	1,715	1
Other financial institutions	4,072	104	156	33	4,364	3
Investment firms	3,513	68	80	5	3,665	3
Financial ancillaries	559	36	76	28	700	0
Insurance undertakings	667	1	18	0	686	0
Public authorities	10	0	0	0	10	0
Non financial companies					0	0
Households					0	0
Non financial companies					0	0
Total Spanish market	88,052	2,745	2,433	820	94,049	66
Financial institutions	41,302	743	395	8	42,448	30
Rest	4,715	268	148	0	5,131	4
Total foreign market	46,017	1,011	542	8	47,578	34
Total subscribed	134,069	3,755	2,975	827	141,627	100

Source: CNMV.

1 Bonds rated in the interval [AA+,A-] as per Standard and Poor's.

2 Bonds rated in the interval [BBB+,B-] as per Standard and Poor's.

3 Bonds rated lower than B- as per Standard and Poor's.

Table 12 also shows how the subscription share falling to Spanish credit institutions increases as the rating gets lower to almost 100% in the riskiest grades (equity). This highlights a distinctive trait of the Spanish market: namely that domestic credit institutions carry practically all the credit risk of securitised assets.

In other words, the “originate to distribute” model that is currently being slated as an indirect cause of the mortgage market crisis in the United States has no relevance in the Spanish case. The fact the risk stays on bank sector balance sheets means outstanding Spanish issues are generally of high quality: Not only do the underlying assets conserve a low default rate, but they enjoy a *de facto* guarantee from the originating entities, which moreover stand out for their capital strength.

4 Market agents

4.1 Investment vehicles

Financial collective investment schemes²³

Investment fund assets fall off sharply with net redemptions reaching record levels...

The collective investment industry has been registering an outflow of funds since end 2006. Among the factors at work are the changed tax treatment of savings, which has eroded their relative advantage over deposits, and the losses of capital generated by rising interest rates. This trend was accentuated in the last four months of 2007 by the uncertainties accompanying the international mortgage and financial crisis. Finally, net redemptions in the year reached a decade-long high of over €20 billion²⁴. All fund categories²⁵ reported sizeable outflows, with the sole exceptions of guaranteed fixed-income funds and hedge funds and funds of hedge funds. Among the categories where redemptions bit deepest were global, short fixed-income and equity funds.

...as a result of tax changes and investor uncertainty.

Redemption volumes amply exceeded the returns earned on fund portfolios, resulting in an aggregate decline in assets under management to €255 billion at the 2007 close (5.7% less than one year before). Again, the fall was extensive to all categories except guaranteed fixed-income funds, which profited from the mounting uncertainty of the year’s closing quarter. In all, investment funds managed a bare 2.7% return in 2007 compared to the 6% approximately of 2006, with falling international equity markets as the principal culprit. Spanish equity funds, conversely, earned an annual 8%, the highest of the categories figuring in table 13, with returns holding up strongly in all but the third quarter.

Spanish collective investment schemes (CIS) stand out for their low risk profile (over two thirds of assets held in fixed-income and guaranteed schemes) and above par liquidity, though last year brought a small shift to riskier investment as manifest in the slightly higher weight of the equity portfolio (up from 22% in 2004 to around 25% in 2007²⁶) and fixed-income portfolio readjustment in favour of corporate vs. government bonds²⁷. In any case, the conservative bent of Spanish CIS has helped them come through the recent turbulence in relatively good shape.

²³Although this term 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.

²⁴Over 70% of net redemptions took place in the fourth quarter of 2007.

²⁵As per the grouping shown in table 13.

²⁶Accompanied by a decline in the fixed-income portfolio from 74% to 67% of assets, with the remainder up to 100% corresponding to warrants and options, the unlisted portfolio, cash and receivables/payables.

²⁷In the domestic portfolio, the weight of private fixed-income rose from 14% in 2004 to 24% in 2007, while public fixed-income dropped back from 23% to 16%.

Main investment fund variables¹

TABLE 13

Number	2007					
	2006	2007	I	II	III	IV
Total investment funds	2,822	2,926	2,872	2,919	2,920	2,926
Fixed income ²	606	600	609	606	604	600
Balanced fixed income ³	212	204	207	211	203	204
Balanced equity ⁴	222	207	215	216	216	207
Spanish equity	118	123	118	118	121	123
International equity ⁵	467	481	480	488	485	481
Guaranteed fixed-income	220	251	232	237	241	251
Guaranteed equity	559	590	577	586	589	590
Global funds	418	470	434	457	461	470
Assets (million euros)						
Total investment funds	270,406.3	255,040.9	273,412.8	276,600.4	269,907.1	255,040.9
Fixed income ²	116,511.9	113,234.1	116,963.0	116,344.7	118,489.4	113,234.1
Balanced fixed income ³	15,314.5	13,011.9	15,755.0	15,329.1	14,142.3	13,011.9
Balanced equity ⁴	10,149.2	8,848.0	10,090.7	10,289.1	9,753.4	8,848.0
Spanish equity	10,416.4	7,839.4	11,238.3	9,523.4	8,353.3	7,839.4
International equity ⁵	24,799.6	22,698.4	25,759.1	29,428.3	26,453.8	22,698.4
Guaranteed fixed-income	14,484.8	17,674.4	15,179.1	15,810.4	16,291.2	17,674.4
Guaranteed equity	44,796.6	42,042.1	43,998.9	44,140.0	43,365.6	42,042.1
Global funds	33,933.3	29,692.6	34,428.9	35,735.4	33,058.2	29,692.6
Shareholders						
Total investment funds	8,637,781	8,053,049	8,740,972	8,755,921	8,467,203	8,053,049
Fixed income ²	2,960,879	2,763,442	2,933,505	2,881,128	2,869,191	2,763,442
Balanced fixed income ³	524,827	493,786	551,786	539,799	511,811	493,786
Balanced equity ⁴	357,013	331,214	374,508	376,559	359,667	331,214
Spanish equity	317,386	288,210	341,396	363,017	343,208	288,210
International equity ⁵	1,258,426	1,089,868	1,274,138	1,263,619	1,184,871	1,089,868
Guaranteed fixed-income	497,540	549,108	518,940	541,442	540,637	549,108
Guaranteed equity	1,783,867	1,715,144	1,771,469	1,766,834	1,754,596	1,715,144
Global funds	937,843	822,277	975,230	1,023,523	903,222	822,277
Return⁶ (%)						
Total investment funds	5.59	2.73	1.11	1.65	-0.15	0.10
Fixed income ²	1.95	2.71	0.72	0.65	0.63	0.68
Balanced fixed income ³	4.18	1.93	0.94	0.96	-0.16	0.18
Balanced equity ⁴	10.34	2.69	1.71	2.57	-1.17	-0.40
Spanish equity	33.25	8.02	5.78	2.07	-2.42	2.53
International equity ⁵	14.98	2.13	2.12	6.38	-2.80	-3.28
Guaranteed fixed-income	0.83	2.78	0.59	0.29	1.03	0.84
Guaranteed equity	4.66	2.44	0.56	1.62	0.13	0.12
Global funds	4.01	1.47	0.99	1.57	-0.70	-0.38

Source: CNMV.

1 For data on subscriptions and redemptions, see table 5.

2 Includes: Short and long fixed-income, international fixed-income and money market funds.

3 Includes: Balanced fixed-income and balanced international fixed-income.

4 Includes: Balanced equity and balanced international equity.

5 Includes: Euro equity and international equity Europe, Japan, United States, emerging markets and others.

6 Annual return for 2006 and 2007 and non annualised quarterly return for each quarter of 2007.

To get a more precise handle on Spanish schemes' exposure to the international mortgage and financial crisis we must first scan for the presence of assets linked to the sub-prime mortgages whose slump in value started the trouble. Further, as one of the effects of the crisis has been a liquidity contraction in certain fixed-income and structured product markets, we must also consider funds' exposure to the assets harder to shift in current market conditions.

As advised by the CNMV in its press release of 23 August 2007, only 14 collective investment products (nine investment funds and five SICAVs) have any direct

Spanish CIS have next to no direct exposure to the products affected by the US mortgage crisis.

portfolio exposure to assets “contaminated” by the US mortgage crisis. The combined worth of these vehicles amounted at the time to 0.0162% of total CIS assets. Specifically, they were invested in three French schemes which temporarily suspended redemptions on the grounds that some of their bond holdings were backed by sub-prime paper. Of the Spanish funds affected, only one had to resort to partial redemptions, as envisaged in article 48.7 of the Collective Investment Scheme Regulation – the case of having over 5% of assets in a foreign CIS that has suspended subscriptions and redemptions. When investment was below this threshold, the CNMV instructed managers to issue a significant event notice²⁸, thus ensuring maximum transparency to current and prospective shareholders.

Analysis of CIS investments reveals that only 6% of portfolio assets could be classed as lacking in liquidity ...

A second type of analysis entails quantifying fund investments in less liquid products. Measuring the liquidity of a portfolio of financial instruments is no easy task in the absence of reliable indicators about how readily a given asset can be sold on the market. One possible indicator is the frequency with which a price communicator quotes bid and ask prices in its respect. Applying this indicator to the private fixed-income portfolio, which is where illiquid products will potentially be concentrated, reveals – with the reservations due to a less than perfect measurement tool – that the percentage of illiquid holdings is relatively modest.

As we can see from table 14, private fixed income (including instruments deriving from the securitisation of bank loans) represents 40% of the total Spanish CIS portfolio (December 2007). Of this percentage, just under half (15% of the portfolio) is commercial paper; that is, short-term securities that investors will typically hold to maturity. Subtracting commercial paper, only a quarter of private-fixed income holdings (6.3% of the portfolio) were not quoted on any occasion by the chosen price communicator.

... even those in the securitisation categories.

Asset-backed securities, at a little over 21% of private fixed income (8.6% of the portfolio), are just under half of the potentially illiquid assets (2.3% of the portfolio).

This low exposure to hard-to-sell instruments plus an abundance of highly liquid assets like deposits and repos (15% to 18% of the portfolio), suggests that Spanish CIS can cope reasonably comfortably with the present liquidity shortage in fixed-income markets.

²⁸In accordance with articles 19 of the Law on Collective Investment Schemes and 28.1 of the corresponding Regulation.

Private fixed-income holdings (Dec 07)

TABLE 14

a) Volume and composition of the fixed-income portfolio

Type of asset	Volume (million euros)			% private fixed-income		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Commercial paper	37,579.3	-	37,579.3	37.4	-	37.4
Mortgage bonds	2,466.7	-	2,466.7	2.5	-	2.5
Structured products	4,161.2	4,176.6	8,337.7	4.1	4.2	8.3
Securitisation	11,909.0	9,440.1	21,349.1	11.9	9.4	21.3
Other private fixed-income	4,228.8	26,467.0	30,695.8	4.2	26.4	30.6
TOTAL	60,344.9	40,083.7	100,428.6	60.1	39.9	100.0

b) Percentage of assets with and without market quotation

Type of asset (% portfolio)	Bloomberg price	No Bloomberg price
Mortgage bonds	1.0	-
Structured products	2.1	1.2
Securitisation	6.3	2.3
Other private fixed-income	9.5	2.8
TOTAL	18.9	6.3

Source: CNMV.

In any case, if the abnormal state of trading on certain markets lasts longer than expected, CIS managers will have to take regular depth soundings of the markets where their portfolio instruments are traded, as prescribed in article 40 of the current Regulation. They should also operate appropriate valuation criteria for instruments lacking a reliable market benchmark, for which internal models are employed. Specifically, such models should be able to correctly evaluate liquidity premiums in line with the market conditions of the moment. Finally, with financial institutions likely to be engrossed in strengthening their liquidity positions, managers within banking groups must make doubly sure that conflict of interest mechanisms are functioning properly.

Real estate collective investment schemes

Real estate funds were less affected by the slowdown in collective investment. Finally, assets under management rose almost 1% to over €9,121 million, contrasting with the decline suffered by financial CIS. This growth, however, pales in comparison to the 35% of 2006 and 50% of 2005. It also drew exclusively on portfolio gains, considering that the outflow of funds in the third and, especially, the fourth quarter far exceeded the inflows of the first six months, in a clear break with the pattern of the previous years. Aggregate returns (5.3%) were a little lower than in 2006 (6.0%), while the number of shareholders (funds and companies) dropped by 3.1% to just over 146,000.

Although the industry prospects are generally good, managers should be alert to the depth of investee markets and apply reliable valuation criteria to forestall any conflicts of interest.

Real estate CIS also registered sizeable outflows in 2007, but their large portfolio returns kept assets on an even keel.

Main real estate fund variables

TABLE 15

	2004	2005	2006	2007	2007			
					I	II	III	IV
FUNDS								
Number	7	7	9	9	9	9	10	9
Shareholders	86,369	118,857	150,304	145,510	152,902	153,630	151,916	145,510
Assets (million euros)	4,377.9	6,476.9	8,595.9	8,608.5	8,781.7	8,929.4	8,905	8,608.5
Return (%)	6.65	5.35	6.12	5.30	1.31	1.1	1.53	1.26
COMPANIES								
Number	2	6	8	9	8	8	9	9
Shareholders	121	256	749	843	754	769	661	843
Assets (million euros)	56.4	213.9	456.1	512.9	459.2	487.4	504.3	512.9

Source: CNMV.

Their risk has augmented with their degree of exposure to a faster contraction of the real estate market.

Despite being a small segment of the industry (just 3.1% of the total assets of all collective investment schemes marketed in Spain²⁹), their risk has recently augmented amid concerns about a sharper-than-envisaged downturn in Spanish real estate. This exposure, moreover, has increased in the past few quarters in line with the rising portfolio weight of their property investments³⁰.

Hedge funds

Hedge funds and funds of hedge funds have done relatively well in their first full year of life.

The hedge fund segment has fared reasonably well in its short life (barely a year), even at the height of financial market uncertainty. That said, it is still only a small parcel of the Spanish collective investment industry. At end December 2007, a total of 31 funds of hedge funds and 21 hedge funds were registered with the CNMV, with combined assets of over €1,446 million (0.5% of total CIS assets) and more than 5,000 shareholders (0.1% of the total). The philosophy of hedge funds is to seek a positive total return independent of the market environment. Their short history means it is too soon to judge the success of their strategies. In any event, their third quarter performance was the worst of the year as with all other investment fund categories.

Their outlook is not conditioned by the same factors as other collective investment schemes.

The start-up of these schemes was eagerly received, with subscriptions flooding in from the second quarter onwards, especially to funds of funds. The outlook for hedge funds is not conditioned by the same factors as the rest of the industry, given their freedom of investment strategy. For instance, while a traditional fund would incur losses in the event of a significant run-down in equity prices, a hedge fund taking the appropriate short positions could come out with gains. Even so, the final results of their strategies depend on such key factors as market liquidity, allowing them to take and unwind positions at relative speed, and the availability of finance³¹. And it is in this last factor that their main risk lies. In the event of further turbulence on the markets from which credit entities draw their funding, hedge funds could find themselves struggling to raise the finance needed to optimise their leveraged investment strategies, to the detriment of their income statements.

²⁹Excluding foreign schemes marketed in Spain, for which no Q4 2007 data were available at the closing date of this report.

³⁰In aggregate terms, property investments moved up from 72.5% of real estate fund assets in 2005 to 84.4% in 2007.

³¹Under Spanish legislation, these schemes can borrow up to five times their total assets.

Main hedge fund variables

TABLE 16

	2006		2007			
	IV	I	II	III	IV	
Funds of hedge funds						
Number	2	2	22	30	31	
Shareholders	2	26	1,456	3,142	3,880	
Assets (million euros)	0.6	9.5	600.2	829.2	1,000	
Return (%)	ns	-0.55	1.08	-2.14	0.67	
Hedge funds						
Number	5	6	9	17	21	
Shareholders	21	108	183	251	1,127	
Assets (million euros)	24.4	119.9	152.0	210.2	445.8	
Return ¹ (%)	ns	1.26	3.18	-2.20	-0.39	

Source: CNMV.

¹ Non annualised quarterly return.

ns: not significant.

4.2 Investment firms

Investment firms perform a number of functions in the securities market sphere (see the text box that follows on investment service provision in Spain). The most common have to do with channelling customers' orders or managing their investments. The list comprises securities broker-dealers, who are authorised to trade on their own account, brokers and portfolio management companies. A later sub-section discusses the role and performance of other non bank financial intermediaries, namely CIS management companies and venture capital entities.

Investment firms perform a series of functions in relation to securities markets, ...

Spanish investment firms are a fairly mixed group. Not only do they differ in size and scale of earnings, but also in the structure of the fees they charge. Broker-dealers, for instance, tend to specialise in the processing of orders, a function which brought in over 64% of their 2007 fees. Brokers too depend significantly on order processing (42% of total fees) but more of them specialise in other areas (24% in investment fund purchases and redemptions and 9% in portfolio management).

...and differ widely not only in size but also by earnings and business mix.

Broker-dealers, brokers and portfolio managers all grew their profits in 2007. Broker-dealers posted a large increase in income from both customer and proprietary trading. This strong performance, allied with modest growth in operating expenses, enabled them to advance in efficiency while conserving their high profitability ratios. Specifically, the aggregate gross income³² of the broker-dealer contingent³³ closed at over €1,021 million, 24% more than in 2006. The busy stock market year delivered a 24% rise in their largest fee item ("order processing and execution"), while the item next in importance "fund subscriptions and redemptions" was slightly down (-0.8%) on the year before, in tune with the slowing demand for collective investment products. Coming up fast in the year were "design and advising" fees, which closed just a little behind the third placed item "distribution and underwriting"; down 15% as a consequence of the subdued primary market activity of the year's second half.

All categories of investment firms grew their earnings in 2007, with broker-dealers to the fore thanks to busy own-account and customer activity...

³²Includes three items: net interest income and result on securities transactions (both own account activities) and net fee income (customer activity).

³³Excluding the figures of one broker-dealer which books part of its proprietary trading under "Other profit and loss", with a distorting effect on aggregates such as "result on securities transactions" and thereby "gross income" and "net operating income".

...while the broker group owed most of their profit growth to non recurrent activities.

Among the broker group, both main revenue items (fees) and operating costs registered a flat evolution in the year, so profits growth was largely due to non recurrent business. Aggregate gross income among this group rose by 1.9% to €247 million, while net fee income was up 5.5% overall, with the growth of “order processing and execution” (18%), and “fund subscriptions and redemptions” (10.4%) offsetting the decline under “portfolio management” (-6%) and a sharp increase in fees and commissions paid (17.6%).

Aggregate income statement

TABLE 17

Thousand euros	Broker-dealers		Brokers	
	2006	2007	2006	2007
I. NET INTEREST INCOME	92,820	124,946	12,548	14,008
II. RESULT ON SECURITIES TRANSACTIONS	54,611	115,584	2,277	610
III. NET FEE INCOME	675,708	780,958	227,278	232,122
Fee income (=1 to 9)	892,542	1,063,826	289,756	305,601
1. Order processing and execution	550,658	684,530	108,329	127,876
2. Distribution and underwriting	73,261	62,145	3,158	2,477
3. Securities custody and administration	21,069	25,112	1,490	1,680
4. Portfolio management	22,472	29,649	29,093	27,353
5. Design and advising	34,339	52,645	2,217	2,224
6. Search and placement	0	9	0	0
7. Margin trading	32	23	0	0
8. Fund subscriptions and redemptions	137,035	135,979	66,985	73,928
9. Others	53,676	73,734	78,484	70,063
Fee expense	216,834	282,868	62,478	73,479
IV. GROSS INCOME (=I+II+III)	823,139	1,021,488	242,103	246,740
10. Operating expenses	376,089	415,309	149,953	152,540
V. NET OPERATING INCOME (=IV-10)	447,050	606,179	92,150	94,200
11. Depreciation and other charges	16,798	87,182	9,011	12,558
12. Other profit and loss	131,153	171,655	7,550	31,413
VI. PROFIT BEFORE TAXES (=V-11+12)	561,405	690,652	90,689	113,055
VII. NET PROFIT	388,190	484,355	61,333	81,832

Source: CNMV.

Portfolio management companies obtained a combined gross income of over €16.6 million against €15.8 million in 2006 with net interest income and core portfolio management business as the main growth drivers. Also noteworthy was the increase in fees under “fund subscriptions and redemptions”.

...in both cases, return on assets and return on equity continued at highs.

The income growth of broker-dealers kept profitability ratios running at highs. Return on assets (ROA) closed near 6%, one point less than at end 2006, while return on equity (ROE) inched up from 43% to 44%. Among the brokers, these same ratios closed at 10.2% against 10% in 2006, and just under 45%, up from 36% the year before. The number of firms with ROE falling short of the annual gain of the Ibex-35 dropped from 66 in 2006 to 31 in 2007.

Figures 11 and 12 offer a breakdown of changes in ROE³⁴ for the broker-dealer and broker categories starting from the year 2000; with reference to leverage, asset productivity, efficiency, taxes and provisions and other charges. The main conclusions of this analysis are as follows:

- In the case of broker-dealers, the 2006 leap in ROE had a large extraordinary component (proceeds of the sale of stock exchange manager

³⁴See box.

BME), but was also driven by efficiency and productivity gains. In 2007, conversely, the indicator's more modest growth traced to firms' higher leverage and improvements in efficiency, while asset productivity contributed on the negative side.

- In the case of brokers, the 2006 increase drew on the positive performance of almost all ROE components. In contrast, 2007 growth (at a rate similar to in 2006) was almost exclusively due to provisions and extraordinary income, as stated, and changes in leverage. Asset productivity, finally, detracted from the return while efficiency made a near zero contribution.

The strength of sector earnings has brought a renewed decrease in the number of firms in losses, in line with the trend initiated in 2003. Specifically, just over 8% of operators reported losses in their end 2007 results. The percentages were highest among non exchange member brokers (13.6%) and portfolio management companies (9.1%), though the scale was by no means alarming; a bare 1.2% of aggregate earnings.

Also, the number of firms reporting losses and the scale of the same reduced once more in 2007.

ROE breakdown

Return on equity (ROE) is the end product of a series of management variables relating to productive efficiency, competitive strength, risk exposure and financial structure, among other factors. Hence an increase in ROE will mean different things depending on whether its cause is an improvement in competitiveness or greater risk exposure (via higher leverage). There follows an algebraic breakdown for ROE that allows us to isolate the effect of changes in each factor on its performance over time, and determine when improvements are due to mainly positive factors to do with efficiency and wealth creation.

$$ROE = \frac{\text{Netprofit}}{\text{Equity(tier1)}} = \frac{\text{Netprofit}}{\text{NOI}} * \frac{\text{NOI}}{\text{GI}} * \frac{\text{GI}}{\text{A}} * \frac{\text{A}}{\text{Equity}} * 100$$

Or put another way, $ROE = (1 - \frac{T}{PBT}) * \frac{PBT}{NOI} * \frac{NOI}{GI} * \frac{GI}{A} * \frac{A}{Equity} * 100$; in which:

T: Corporate income tax

PBT: Profit before taxes

NOI: Net operating income

GI: Gross income

A: Total assets

Tier 1: higher-quality equity

The annual change in ROE is expressed as the sum of changes (log differences) in each of the factors considered for the universe of broker-dealers and brokers. We will now look at how each of the five product terms can be interpreted:

1) Tax indicator (1-T/PBT). An increase in this indicator would point to a lower tax liability for the same result.

2) Provisions and extraordinary income indicator (PBT/NOI). Indicating a firm's financial strength in that a higher figure means provisioning for risks and contingencies and/or extraordinary losses are detracting less from the company's overall result. Note, though, that an increase could also be due to higher extraordinary income, so any resulting increase in ROE would not be sustained over time.

3) Efficiency indicator (NOI/GI). Also expressible as $(1 - \text{Efficiency ratio}(1))$ such that an increase in efficiency (higher 1-ER) would imply an increase in ROE driven by management improvements.

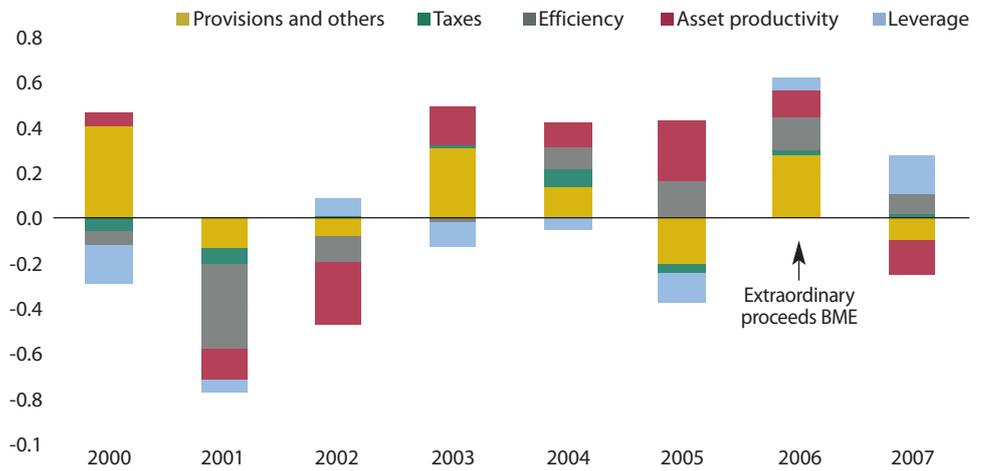
4) Asset productivity indicator (GI/A). ROE improvement drawing on this indicator could be read as a higher value-added extracted from each euro of assets.

5) Leverage/debt indicator (A/Equity). As stated, an increase in leverage will only add to ROE if ROA is higher than the cost of external borrowings. In any case, an excessive rise in leverage means a greater risk of insolvency or bankruptcy, meaning the company is financially fragile.

Similar proposals for the algebraic breakdown of ROE can be found in the *Informe de Estabilidad Financiera* published by Banco de España in May 2004 and the Bank of England's *Financial Stability Review* of December 2003.

Breakdown of year-on-year change in ROE: broker-dealers

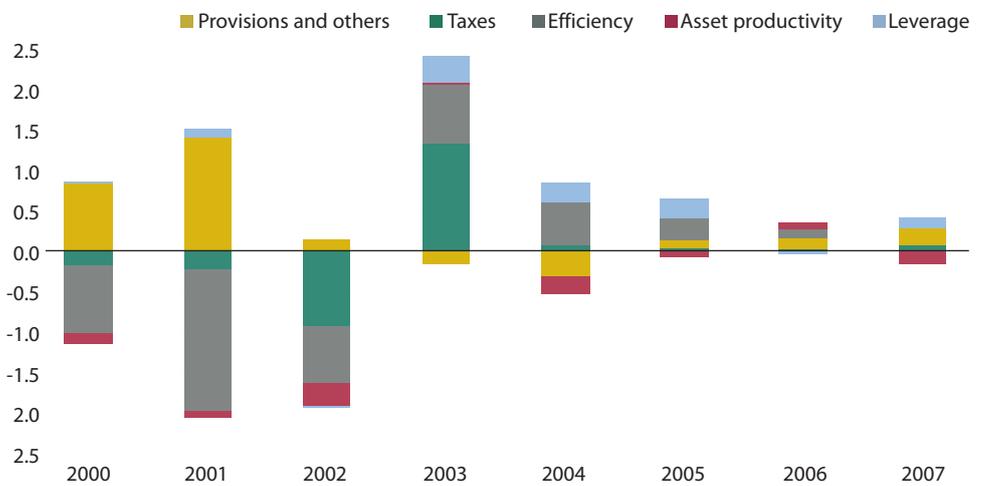
FIGURE 11



Source: CNMV and authors.

Breakdown of year-on-year change in ROE: brokers

FIGURE 12



Source: CNMV and authors.

Investment firms as a rule are comfortably compliant with capital adequacy requirements. Overall, their equity surplus in 2007 was on a par with the previous year's. In the case of broker-dealers this surplus stood at 4.2 times the minimum requirement (the same as in 2006), while the surplus for brokers was 2 times (2.1 times in 2006). Portfolio management companies, finally, presented 0.6 times the minimum requirement against 0.8 times in 2006. Among the firms with the tightest margin (less than 50% of required capital) two belonged to the broker-dealers contingent against nine brokers and three portfolio management companies.

Investment firms, broker-dealers in particular, are comfortably compliant with capital standards.

Investment firms distribution by pre-tax profits and equity 2007

FIGURE 13



Source: CNMV. 2007 results. Qualifying capital at 31/12/07.

Investment firms have felt no direct fallout from the mortgage crisis, as they do not carry related instruments in their trading books. Their main business continues to be the provision of investment services (i.e., distribution activity), and their main income stream, the fees earned from customer orders, has shown no signs of thinning out as a consequence of market turbulence. In fact some firms have benefited from the increase in trades that tends to accompany more nervous markets.

The international mortgage and financial crisis appears not to have done much harm to investment firm business.

At the same time, the growing quantity of business these firms have been doing is a test for the efficiency of their internal control mechanisms. Already one entity has been directly affected by customer defaults in OTC derivate trades.

Generally speaking, firms should be able to conserve their high standards of profitability and capital adequacy, even through a period of slower business. This will, however, put stronger demands on their risk management systems, with particular regard to the credit and liquidity risk emanating from customer transactions. Another short-term challenge for sector operators will be their adaptation to the new Securities Market Law, transposing the Directive on Markets in Financial Instruments³⁵ (MiFID). This legislative change implies both new organisational structures and a new way of handling the customer relationship³⁶ which may substantially alter their business mix. It will also introduce more competition within the European financial services market, as Spanish firms are

... but important challenges remain as regards risk control systems, the need to adapt to the requirements of the MiFID and growing competition in European investment services markets.

³⁵For more information, see section 5 of this report on securities market organisation, which devotes a special sub-section to MiFID implementation.

³⁶See text box on "Suitability and appropriateness testing" in section 5.

beginning to find out. The challenge they face is to coax out new improvements in efficiency and ensure they have the capacity on hand to offer Spanish clients a complete investment service anywhere in Europe.

Investment services provision in Spain: the role of credit institutions

The provision of investment services is governed by the Securities Market Law³⁷, which establishes what is meant by investment services and which entities are qualified to perform them. Its article 63 offers a list of such services, including the reception, forwarding and execution of customer orders, portfolio management, the distribution of financial instruments, the underwriting of securities issues and advising on investment matters³⁸. It also envisages a range of ancillary services, including securities custody and administration, that are subject to the same rules. The provision of investment services is reserved for investment firms (broker-dealers, brokers, portfolio management companies and financial advisors) and credit institutions. The latter may render all the services envisaged in the law assuming their legal regime, bylaws and individual licences authorise them to do so. Both credit institutions and investment firms can trade professionally, on customers' or their own account, and perform all the investment and ancillary services legally permitted. Brokers may only trade on customers' behalf, with or without representation, but may perform all other services except the lending to investors of securities or cash. Portfolio managers and financial advisors are the most circumscribed in their operations, with the former confined to the advising and managing of investment portfolios and the latter to the strict provision of investment advice. Investment firms are in all respects authorised and supervised by the CNMV, which also oversees the investment service operations of credit institutions, while their prudential supervision falls to Banco de España.

A structural analysis of the investment services industry (see figures below) reveals the dominant position of credit institutions. In the last five years, their share has ranged from 73% to 77% of total fee income, against the 17%-21% and 5%-6% respectively of broker-dealers and brokerage firms. They also take the lion's share of securities custody and administration business³⁹ (96% of income) and the sale of investment fund units (92% of income), thanks to the distribution muscle of their branch networks. In securities trading, the field is more open, with broker-dealers taking in 51% of sector income. Finally, portfolio management is the activity that is most widely diversified by sector agent.

³⁷ Title V.

³⁸ Recently enacted Law 47/2007 which, among other matters, implements the MiFID, extends the range of investment services to include investment advice and the management of multilateral trading facilities, and also introduces a new type of investment firm, the "financial advisor" authorised exclusively to render advisory services in investment matters.

³⁹ The differences are striking: a market value of €2,188 billion (30 June 2007) for the securities deposited at credit institutions against €92 billion worth at broker-dealers and brokers (as of 31 December).

Fee income from investment services (million euros)

FIGURE 14



Source: CNMV and Banco de España.

4.3 Collective investment scheme management companies

CIS managers did slightly worse in 2007 as the industry turned down...

... but with profitability ratios holding up strongly

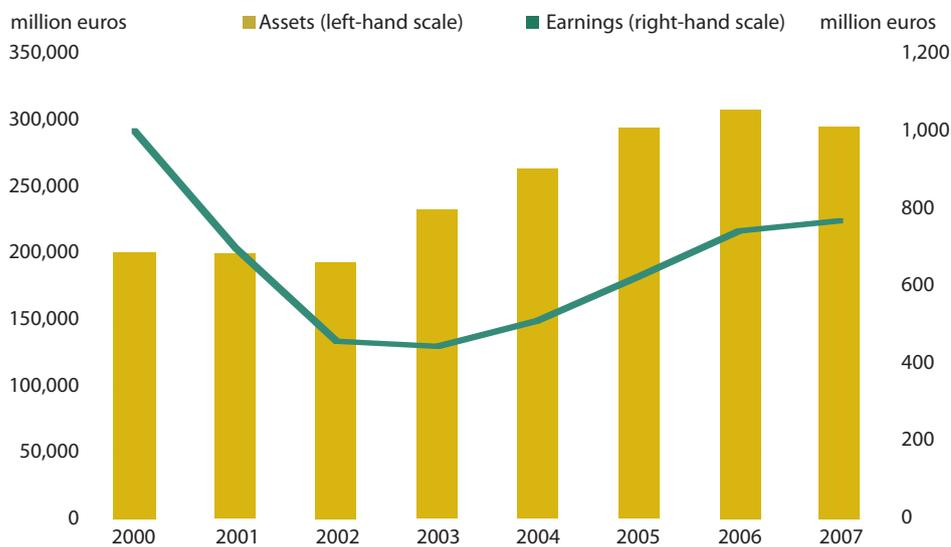
In the short term, competition between managers will remain fierce as demand stays mainly focused on bank deposits.

CIS managers too have fared reasonably well though with some slight earnings slippage versus the previous year. A total of 19 managers (out of 120 registered) reported losses, eight more than in 2006, though this was partly due to recent start-ups in the hedge fund and fund of hedge fund categories. In fact, eight of the 19 loss-making managers did not join the register until 2007 or late 2006. Of the other 11, five had declared losses persistently since 2005⁴⁰ at least, and six intermittently in preceding years or in the last two alone.

Return on equity (ROE) dropped to a mid-year 61% from the 69% of December 2006, though this is still high in historical terms. This aggregate decline can be explained by reference to: (i) the levelling-off of fund managers' profits growth, and (ii) an 18% increase in own funds.

The slower advance in profits reflects the general slowdown in the collective investment industry as a result of tax changes and the banks' new aggressiveness in capturing deposits. Managers are also experiencing fiercer competition both among themselves and with credit institutions, which have been cutting their prices in order to hang onto the greatest possible quantities of clients and assets. The business and earnings outlook for the next few months will continue to be coloured by the international financial crisis and its attendant uncertainties, with investors tending to shy away from investment fund products in favour of traditional bank deposits.

CIS management companies: assets under management and profit before taxes¹ FIGURE 15



Source: CNMV.

⁴⁰Including one manager in losses since 2001 and another since 2004.

CIS management companies: profit before taxes and ROE

TABLE 18

Million euros	Profit before taxes	ROE before taxes
2000	1,005.8	84
2001	701.7	63
2002	457.1	44
2003	445.3	44
2004	512.3	49
2005	622.8	53
2006	744.0	69
2007	790.6	61

Source: CNMV.

CIS management companies: assets under management, management fees and average fees

TABLE 19

Million euros	Assets managed	Fund manage-		Fee ratio (%) ¹
		ment fee income	Average fund management fee (%)	
2000	200,832	2,869	1.429	63.46
2001	199,427	2,465	1.236	65.78
2002	192,982	2,259	1.171	72.70
2003	232,915	2,304	0.989	73.78
2004	263,369	2,672	1.015	73.58
2005	294,372	2,976	1.011	72.17
2006	308,476	3,281	1.063	71.55
2007	295,907	3,206	1.084	70.22

Source: CNMV.

¹ Fee expense on fund distribution to fee income from fund management.**4.4 Other intermediaries: venture capital**

A total of 61 venture capital entities joined the CNMV register in 2007, breaking down 33 companies, 16 funds and 12 fund managers. These come on top of the sixty entities registering in 2006, of whom 27 were companies, 22 funds and 11 fund managers⁴¹.

CNMV registers evidence a new increase in venture capital entities operating in Spain.

Data from the industry association in Spain (ASCRI) show that venture capital entities invested €4,298 million in 2007, 44.4% more than in 2006 and beating the 2005 record of €4,198 million. Transaction numbers (776) were likewise 26.7% up on the 2006 figure. Divestments in the year summed €1,547 million, an increase of 18.8%, with transactions down by nine to 33⁴².

Investment and transaction numbers attained record levels in 2007...

Movements in the CNMV venture capital register 2007

TABLE 20

	Situation at 31/12/2006	Registrations	Removals	Situation at 31/12/2007
Entities	221	61	6	276
Venture capital funds	64	16	4	76
Venture capital companies	102	33	1	134
Venture capital fund managers	55	12	1	66

Source: CNMV.

⁴¹Part of this increase owes to the provisions of Law 25/2005 of 24 November regulating venture capital entities and their management companies. This law allows for a speedier registration process in the hands of the CNMV. Prior to its enactment, numerous entities engaging in venture capital activities (ECRs) were not entered in the corresponding register. The new law addresses this problem by establishing a more simplified form of ECR; a more flexible investment vehicle with less protectionist rules for qualified investors. Now, venture capital entities can invest in other ECRs or acquire listed companies to withdraw them from trading. The former option has encouraged the creation of venture capital funds specialising in other ECRs and targeted mainly on the retail public.

⁴²Two 2007 divestments went through as initial public offerings, involving Clínica Baviera and Fluidra.

... though the financial crisis has tended to drive down the size of investments.

Although the sector recorded a strong full-year performance, the last quarter brought signs of change, particularly a fall in investment (€910 million against an average of €1,096 million in the first three quarters) and a jump in transaction numbers (225 against an average 135 in the first three quarters). In all, credit market tensions in the year's closing months signalled a drier period for investment.

What were slated to be the year's headline operations involving European venture capital entities – their entries to Iberia and Altadis – eventually fell through. These cancellations reflect the decline observed in leveraged buyout transactions (LBO), which tend to be the largest sized (55% of the total invested in the year).

Within the general sector trend towards more modest investment levels, Spanish entities should fare rather better than their counterparts elsewhere in Europe. The reasons are three: (i) the LBOs most affected by bank credit rationing will tend to be the biggest sized transactions that are less predominant in the Spanish market, (ii) venture capital entities enjoy a favourable tax treatment in Spain, making it easier for them to recruit investor funds⁴³ and (iii) the success of Spanish venture capitalists in raising new funds for investment; an estimated €3,049 million in 2007⁴⁴. Also likely is a reduction in the size of industry divestments and less frequent recourse to initial public offerings, in what threatens to be a more adverse economic-financial climate. Indeed, some entities had to call off plans for stock market launches in the second half of 2007⁴⁵.

Spanish entities could continue to outperform their European peers, despite a shrinkage in investment volumes.

5 Changes in securities market organisation

For investment firms, the current international juncture has coincided with a period of transformation ...

The current international setting as mapped out in the preceding sections coincides with a period of industry transformation, as Spanish firms readjust their structure and operations in line with the financial integration process⁴⁶. Two challenges stand out on the immediate horizon. Firstly, the entry to force of the MiFID in November 2007 means investment service providers must adapt their organisational forms and rules of conduct. And second, Spanish post-trade infrastructures may shortly be caught up in a new wave of changes of a legal and operational nature.

5.1 MiFID implementation

... deriving from the entry to force of the MiFID.

The publication of Law 47/2007 of 19 December amending Securities Markets Law 24/1988 marks an important step forward in transposing MiFID provisions into Spanish legislation. Although the new law will require subsequent regulatory developments that flesh out the provisions firms must adhere to, its

⁴³Article 35 of Law 25/2005 establishes a 99% tax exemption on capital gains from the transfer of ECR stakes.
⁴⁴We might mention here the closure of the vehicles launched by Mågnum (€850 million), N+1 (500 million), Artá Capital (500 million, with 50% contributed by Corporación Financiera Alba and Mercapital), Nazca (150 million), Realza Capital (120 million), N+1 Capital Empresarial (120 million) and Miura (60 millions).

⁴⁵For instance, the owners of Eolia and High Tech.

⁴⁶As contemplated in certain measures emanating from the EC's Financial Services Action Plan, and also in market initiatives like the Code of Conduct signed by post-trade providers in November 2006.

text presents important novelties with a bearing on the way investment firms conduct their business.

Pre-MiFID legislation already imposed certain organisational requirements on firms operating in Spain that have since been written into the European Directive⁴⁶. Among the new obligations it brings in are the need to operate a business continuity plan and, in general, have plans in place to cover operational risk, including legal/compliance risk. A possible sticking point here is that these continuity plans depend for their success on a very small number of companies equipped to offer back up services.

A core MiFID requirement is that firms class their clients according to a standard scheme, and run appropriateness and suitability tests on the services they are offered (see text box on “MiFID appropriateness and suitability testing”). And they must also have a defined “best execution” policy in respect of customer orders, requiring a series of process changes in the firms that supply this kind of service. This policy, moreover, cannot be the same for retail as for professional clients, with the result that some investment firms may opt to specialise in one or other segment.

The new Directive may usher in structural changes further ahead in a context of greater European competition.

Finally, the triggering event for even more radical changes in market organisation would be the decision by a Spanish or international investment service provider to set up and manage an MTF⁴⁷ specialising in shares listed on the Spanish exchanges. Under the terms of the MiFID, firms rendering investment services can also become systematic internalisers⁴⁸ (SI) and offer securities trading services. There is a chance that some operator may opt to do so, especially if it already has a sizeable portfolio of institutional clients. In any event, the transparency requirements the MiFID imposes for MTFs and SIs mean that such an initiative may have to wait some time.

The CNMV has sought to smooth the transition by means of an intense publicity and informative effort. Described below are just two of the numerous initiatives set in train to help firms make a trouble-free transition to the new regulatory environment:

The CNMV worked throughout 2007 to assist investment service providers in adapting to the MiFID.

- A document was sent out to all financial institutions in July 2006 to canvass them about their adaptation plans. CNMV teams also held meetings with the most representative of their number to assess the state of progress, the main obstacles they were encountering and the solutions each had found. It was clear from these contacts that both financial entities and their associations were working all out to ensure MiFID conditions were implemented.
- A dedicated discussion forum was launched in 2006 with the involvement of CNMV and Banco de España and the main associations representing financial institution interests. The work of the Financial Intermediaries Expert Group brought to light the key issues and success drivers in the MiFID adaptation process, which were then circulated to the interested public in Q&A format.

⁴⁷Investment firms and credit institutions.

⁴⁸For instance, the organisational requirements for the control of investment firm activities were laid down in CNMV Circular 1/98 of 10 June on internal systems for the control, monitoring and ongoing evaluation of risks. Spanish legislation also lays down rules of conduct for investment service providers in Royal Decree 629/1993 of 3 March and its implementing provisions.

⁴⁹Multilateral trading facility.

The CNMV has given investment firms ample time to adapt themselves to the MiFID framework and has simplified the necessary authorisation procedures; in short, sparing no effort so firms can make the adjustment with a minimum of fuss.

MiFID suitability and appropriateness testing

One of the main changes introduced by the MiFID and its implementing regulations is the requirement that obligated subjects run a suitability test in determined circumstances. This is a safeguard measure to ensure the investment services provided to clients are right for their particular needs.

The suitability test is regulated in article 19.4 of Directive 2004/39/EC and implemented in articles 35 and 37 of Directive 2006/72/EC. Although gathering and processing the information needed for this test will call for a major adaptation effort, it is one of the provisions that will generate the most value-added for investment service users. The services for which the test is compulsory for investment providers⁵⁰ are advising on investment matters and discretionary portfolio management. The following input must be procured from the customer:

1. Knowledge concerning the type of product or service proposed.
2. Experience in the investment field relevant to the specific type of product or service (kinds of products he/she is familiar with, the nature and size of transactions, frequency, period, educational background, profession).
3. Financial situation (source and level of income, assets, regular financial obligations).
4. Investment goals (time horizon, risk profile, purpose of the investment).

Informational requirements regarding the customer's knowledge and experience in the corresponding investment field will depend on the type of client, the nature and level of the service, and the product or operation being proposed (proportionality principle). Suitability test contents will also vary in the case of professional clients.

Only when a product's suitability can be established, i.e., when: (i) it meets the customers' investment goals, (ii) he or she can confront the degree of risk consistent with these goals, and (iii) he or she has sufficient knowledge and experience to understand the risk involved in the transaction or the management of his/her portfolio, can the investment firm issue the pertinent recommendation or render the proposed portfolio management service. If the firm cannot gather the necessary information it must refrain from providing the investment advice or portfolio management service. In the latter case, moreover, is not enough just to establish suitability at the start of the arrangement, it must also be re-checked each time the manager makes a recommendation, suggestion or request to a customer for the issue or modification of a mandate defining the scope of its discretionary management.

⁵⁰Investment firms, as defined by Directive 2004/39/EC and credit institutions authorised pursuant to Directive 2000/12/EC when they provide investment services or activities, according to article 1.2 of Directive 2004/39/EC.

The Directive also stipulates that investment firms must keep a record of all information gathered for suitability testing. The work done by CESR on level 3 measures makes reference to this requirement.

The appropriateness test is another MiFID requirement⁵¹. The idea in this case is to ascertain the customer's knowledge and experience with regard to the product or service being proposed or sought. The investment service provider can omit this test in the following circumstances: (i) the non complexity of the financial instruments in question, (ii) the service is to be rendered at the client's request, (iii) the client has been told that the investment firm is not obliged to assess the appropriateness of the proposed instrument or service, so knows he/she is not protected under the corresponding rules of conduct and (iv) the service provider is compliant with its obligations in regard to conflicts of interest. The orientative content of the test is similar to that of points 1 and 2 of the suitability test, as discussed above. The principle of proportionality is likewise upheld and the firm must keep a record of the information gathered. The provider is also relieved of the need to run appropriateness tests for professional clients, when it can be assumed that this categorisation implies sufficient knowledge and experience to understand the risks of the products, services or transactions in question. In certain cases, a provider can also allege that a customer's previous investments in similar instruments imply that he or she is sufficiently knowledgeable and experienced.

If an investment firm concludes that a transaction/product/service is not right for a given customer, it may still go ahead providing it first conveys this opinion to the interested party. The same holds when it has been unable to gather enough input information; in which case it should warn the client that it cannot be sure whether the product or service meets his or her interests.

In closing, a few brief words on the relationship between the suitability and appropriateness tests. As stated, the first is reserved for products or services that entail an element of recommendation, i.e., investment advice or portfolio management. If a firm is going to provide some other investment service involving products or services on which a suitability test has already been run, it can dispense with the appropriateness text. In all other cases, this test will be necessary.

5.2 Developments in the post-trade sphere

The Spanish clearing, settlement and registration system (the System) must take immediate steps to adapt its procedures to the MiFID rules transposed through Law 47/2007 of 19 December, and the commitments entered into as a signatory to the voluntary Code of Conduct (CoC⁵²). In particular, it must be prepared to grant System access to non resident investment firms, with or without a physical establishment in Spain, that wish to directly settle trades on Spanish securities closed outside of Spanish regulated markets, and attend access or interoperability requests from other European clearing and settlement systems or central counterparties.

The Spanish trading and settlement system will have to line up with new European initiatives.

⁵¹Set out in articles 19.5 and 19.6 of Directive 2004/39/EC.

⁵²The Code of Conduct was published on 7 November 2006 to enhance the transparency of post-trade service pricing, enlarge interoperability between markets, securities depositories and central counterparties and introduce the separate accounting and administration of operator services. It arose from an initiative of internal market commissioner Charles McCreevy and was adopted voluntarily by a majority of the industry.

All this will mean far-reaching changes in operational procedures, including the establishment of direct communication channels with investment firms⁵³ so they can clear and settle their non market operations, and a review of current procedures for the matching, validation, clearing and settlement of such transactions and their registration, including daily update of the file records of issuers of registered securities, and checks on issue balance controls, securities matching and, where applicable, procedures for the provision of pooled and supplementary collateral.

These changes will take their place alongside improvement measures already approved by the System directors, including a new liquidity provision facility (final lender) and the solution of problems to do with the recognition of purchase settlements.

Developments to address these challenges should prioritise the closest possible alignment with the settlement practices and standards in widest use among European Union member countries, so the System can keep pace with the gathering process of market integration, and strengthen its capacity to attract international business, and conserve existing clients, in an increasingly competitive landscape.

In the medium term, the System should be alert to all the possibilities offered by the new Target-2 Securities platform, which will allow central securities depositories and their participants to settle transactions in central bank money throughout the euro area. This will mean exploring possible technical improvements in the present system, analysing where change is needed in legal and procedural rules, and setting a realistic timetable for completion. Among the current specifications that may not fit well with the future single market are the overly rigid system of trade registration, transaction finality at the point of trade rather than settlement (more common internationally) and the absence of a central counterparty to cover cash transactions in equity and fixed-income markets.

6 Conclusions

The performance of Spanish securities markets since summer 2007 has been conditioned by the disruption ensuing from the sub-prime mortgage crisis in the United States. The effects of this crisis have been to cloud the global macroeconomic outlook, reduce the liquidity of interbank and private fixed-income markets, and prompt a sizeable re-pricing of risk in world markets.

The pattern in Spain has been similar to elsewhere; namely, a notable correction in share prices – though less abrupt than in other markets – the enlargement of risk premiums and a liquidity shortfall in fixed-income markets, including bank asset securitisation markets. In particular, the crisis has engendered a negative investor

⁵³The MiFID gives legal sanction to the non exchange trading of listed securities. In stock markets, for instance, it will no longer be necessary to channel all trades through an exchange. However, the System is not equipped to handle trades without the mediation of an exchange; the only venue which can affix registration and transaction codes, respectively, to securities purchases and sales for their subsequent settlement and registration.

sentiment towards bank sector paper, which has fallen on all issues regardless of their objective quality.

The Spanish securities and financial industries are in reasonably good shape to confront this unsettled period, thanks to the overall vigour of the economy – despite some degree of slowdown – and the soundness of main financial intermediaries. But both prices and activity will ultimately depend on how the key uncertainty factors pan out. These are, firstly, the extent of slowdown in the Spanish and international economy and, secondly, the speed at which financial market conditions normalise. Of special importance here is how soon price formation mechanisms can be restored to order in securitisation markets and private fixed-income markets in general.

Most of the agents participating in Spanish markets should come through the crisis without too large a dent in their income statements, and far less in their capital adequacy. However, collective investment products like investment funds could face significant near-term challenges; in particular growing competition from bank deposits due to credit institutions' greater difficulties in raising finance on the markets. At the same time, CIS management companies will have to make doubly sure that the mechanisms to prevent conflicts of interest between them and the bank groups many of them belong to are operating effectively. Finally, although the collective investment sector as a whole is amply positioned in readily transferable assets, the situation of the markets counsels constant surveillance of the liquidity of trading venues.

Liquidity problems in certain markets may counsel the use of internal valuation models for positions in the corresponding instruments. They also place difficulties in the way of their practical application. Listed companies, intermediaries and investment vehicles should accordingly redouble their efforts at transparency and information quality, in line with international accounting standards, to ensure there is no discrepancy between their published financial statements and the underlying financial reality.

Although the business of investment service providers is only moderately sensitive to the current market situation, firms will have to tighten up their risk control systems and take immediate steps to meet the operational requirements of the new Securities Market Law implementing the MiFID directive. Further ahead, they could find their competitive quality put to the test in the framework of the emerging pan-European competition that the Directive will help to consolidate.

This changed regulatory environment will also extend to the infrastructures of national regulated markets, which may end up competing with alternative trading platforms such as MTFs and systematic internalisers. At the same time, new legal and operational developments in the post-trade sphere represent an important impetus towards integration, of which national systems must strive to be part. This will mean reviewing the technical peculiarities of the Spanish settlement system, and debating on the wisdom of its near-term adaptation to the model prevailing in most advanced countries.

II Reports and Analyses

Subprime crisis and fixed-income markets

Francisco de Oña Navarro and Gonzalo Gómez Retuerto (*)

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The views expressed in this article are personal and do not necessarily reflect those of the organization to which the authors belong.

1 Introduction

The subprime crisis has affected not only all the financial markets but also economic activity worldwide, which has been hit by the knock-on effect of the global fall in the index – moreover hard to measure – of “confidence of economic agents”.

Although this crisis affects the economy as a whole, the subject of this article is confined to its effects on the fixed-income market¹. These markets contain an increasing number of instruments and are vital to the funding of the economy.

In this paper we shall make a non-exhaustive analysis of the origin and development of the subprime crisis, its impact on the financial markets, the widening of credit spreads, its effects on the primary market and the difficulties encountered in asset valuation. One of our main conclusions is that a lack of transparency is the element which has most contributed to the crisis of confidence and the imbalances that have occurred in the finance markets.

The coincidence in time with a global process of reform of market regulations by regulators and supervisors which, in the European case, is apparent chiefly in the MiFID directive, could enable changes to be made in the operation of these markets so as to compensate for the lack of information detected. Hence this article’s proposals refer very directly to the need to increase transparency as a means of restoring normality and efficiency in the fixed-income markets.

In its second section this paper will discuss the origins and development of the crisis, in its third section the crisis’s consequences will be analyzed, and finally its fourth section will offer some conclusions.

2 Origins and development of the subprime crisis

The subprime mortgage crisis marks the end of the greatest expansive cycle experienced by the US economy in the last few decades.

After the huge economic and emotional impact of the attacks of 11 September 2001 in New York, the US economic authorities took measures aimed at boosting domestic growth with a policy of low interest rates intended to keep up a high influx of cheap money into the economy. Today the US is undergoing an acute mortgage crisis arising from the difficulties encountered by American financial

¹ The term “fixed-income markets” should be taken to include the “finance markets” or “capital markets” on which products of various kinds are issued and traded (excluding shares and equity derivatives).

institutions in collecting the high-risk mortgages granted to families and companies in the country which, as a result of the economic downturn experienced in late 2006 and in the course of 2007, have been unable to pay off their debts.

The crisis has led directly to the closure and bankruptcy of various institutions linked to the American property sector and has spread throughout the international financial system, in which central banks and monetary authorities have been obliged to inject millions of euros, or dollars, in the form of loans to financial institutions.

The crisis is also affecting issuers of securities, who have seen the conditions of access to the finance markets become tougher, which may give rise to a financial crisis of potentially wider consequences.

2.1 Origins of the subprime phenomenon

The granting of subprime loans is a typical credit practice in the US financial sector, characterized by a level of borrower insolvency risk higher than the average for other credits granted by financial institutions in that country. This higher credit risk is offset by higher interest rates and commissions. Though the term “subprime” may refer to any type of loan granted by financial institutions, loans originating from mortgages account for most of this category.

The procedure for granting loans in the United States is based on a system for the scoring of applicants, so that where the score obtained by the individual or company is between 700 and 850 points, the borrower is rated as Grade A, with low credit risk, and may have access to preferential terms with low interest and other benefits. Applicants below this level are known as Alt-As, with a score between 620 and 700 points but without the necessary documentation to be included in the top group. Borrowers with credit difficulties, a limited credit history or insufficient collateral guarantees form the so-called subprime segment – grades B, C or D – with scores generally of less than 620 points.

Mortgage originations in the US

TABLE 1

Billions of dollars Year	Subprime originations	Total originations	Subprime as a percent of total
1994	35.0	773.1	4.5
1995	65.0	635.8	10.2
1996	96.5	785.3	12.3
1997	125.0	859.1	14.5
1998	150.0	1,430.0	10.5
1999	160.0	1,275.0	12.5
2000	138.0	1,048.0	13.2
2001	173.0	2,100.0	8.2
2002	241.0	2,780.0	8.7
2003	335.0	3,945.0	8.5
2004	540.0	2,920.0	18.5
2005	625.0	3,120.0	20.0
2006	600.0	2,980.0	20.1
Average growth (%)	25.0	17.6	--

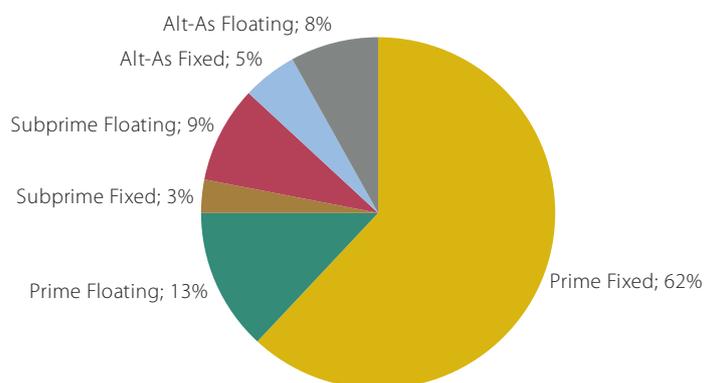
Source: Mortgage Statistical Annual.

The subprime mortgage segment was developed in the US from the mid-90s in order to meet the needs for home-buying finance of a part of the American population with high

insolvency risk ratings. In order to be able to buy a home or get a loan with their home as collateral, this group needed either to devote a large part of their total income to paying off their debts, with debt-to-income ratios in excess of 75%, or to take out a mortgage for a large amount relative to the appraisal value of the home being bought, with loan-to-value percentages in excess of 90%.

Distribution of mortgage debt in the US

FIGURE 1



Source: Mortgage Bankers Association.

Moreover, during the credit boom a large number of subprime loans began to be granted at variable interest rates – known as adjustable rate mortgages or ARMs. This segment of the subprime market, of debtors with high credit risk, became very popular inasmuch as it allowed the intermediary to grant more favourable terms to the borrower in the first few years of the mortgage, with relatively low interest rates that subsequently became adjustable. This format, known as 2/28, has interest rates which are low in the first two years but which then become variable as from the third year and for the rest of the loan's life.

This credit pattern, as time would show, opened up a high degree of interest rate risk for many debtors, who became unable to pay the rising cost of instalments as a result of the upward trend in the key interest rates.

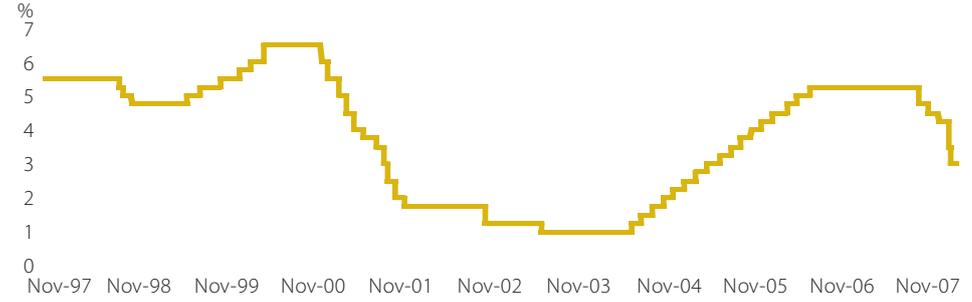
2.2 Causes and outbreak of the crisis

With the turn of the century the economic outlook changed considerably. As a result of the implosion of high-tech companies in 2000, known as the dot.com phenomenon, and also and in particular due to the impact of the terrorist attacks on the World Trade Center in September 2001, the central banks of the world's main economies sought to stimulate growth by means of a large reduction in interest rates in their areas of economic influence.

As an example of this expansive policy, from 2000 to 2004 the Federal Reserve (Fed) reduced its key interest rates from 6.5% to 1%, the lowest rate set by the Fed in decades. This measure succeeded in boosting the economy and stimulating high growth rates. Between 2002 and 2007 GDP growth in the US moved in a range of 2% to 3.5%.

US: Official interest rates

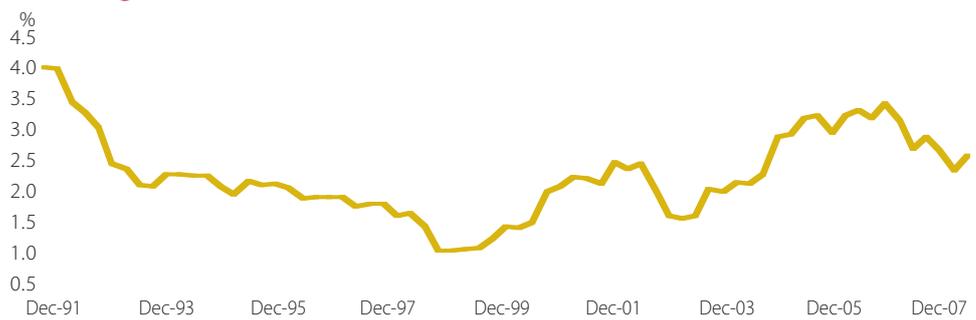
FIGURE 2



Source: Federal Reserve.

US: GDP growth

FIGURE 3



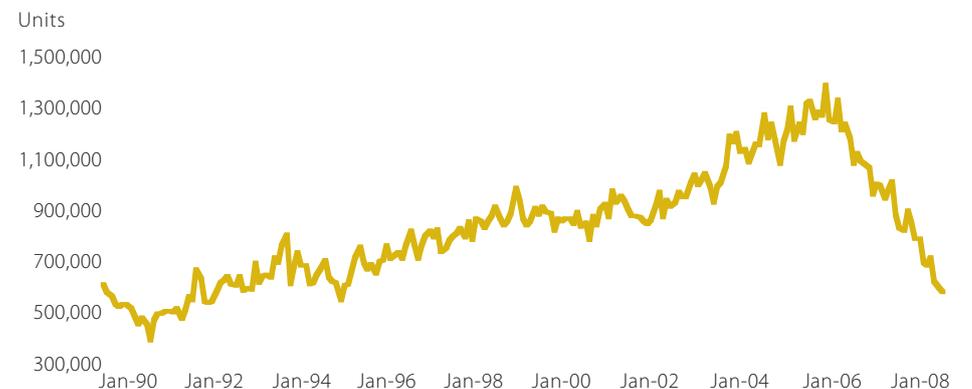
Source: Reuters.

A major component in the economic recovery was the strong activity in the US property sector. Low benchmark interest rates, surplus liquidity in the US banking system, the appearance of new participants and a rising number of intermediaries engaged in the sector, the creation of financial products allowing credit risk to be diversified and spread, etc. led directly to a fall in the cost of home-buying finance and a rise in demand. The stock of mortgage debt in financial sector portfolios grew at yearly cumulative rates of more than 10% in the period 2001-2006.

Similarly, the abundance of mortgage credit and the high demand for home ownership fuelled rapid growth in construction, house sales soared, and growth in property prices reached yearly rates of more than 10%.

US: New house sales

FIGURE 4



Source: Reuters.

Various studies have shown after the event that the problems in the subprime mortgage market have been largely the result of a relaxation of the conditions for the granting of mortgages. For example, the mortgages known as “low doc”, characterized by requiring little or no checking of income and assets, increased from 23% of total subprime mortgages in 2000 to 40% in 2006.

Moreover, as the chances of home ownership became slimmer for less affluent people, the rise in house prices led to the granting of ever more low-quality mortgages. Subprime mortgages rose from 8.5% of total mortgages granted in 2003 to 20.1% of the total in 2006.

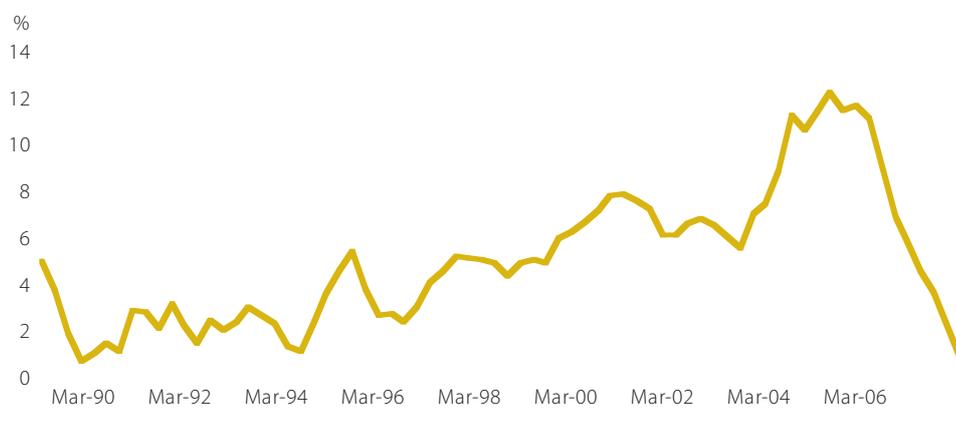
This state of affairs continued until the economic downturn. The Fed’s efforts to halt the rise of inflation in the US economy, due partly to the low cost of money and a surplus of liquidity, led to a change in monetary policy involving a series of rises in the benchmark Fed Funds rate, up to a peak of 5.25% in the summer of 2006.

In these new conditions many borrowers, and especially those with higher credit risk, began to have trouble paying back their mortgages, and the delinquency rate climbed above 14% in the subprime sector.

Early in 2007 the situation became critical and a series of mass defaults began in the subprime segment. These defaults caused a sharp drop in the value of mortgage credits in banks’ assets. As a protective measure some financial institutions active in the sector closed their high-risk subprime divisions and restricted their credit offering, thereby exacerbating the crisis.

US: Quarterly growth in house prices

FIGURE 5



Source: Mortgage Bankers Association.

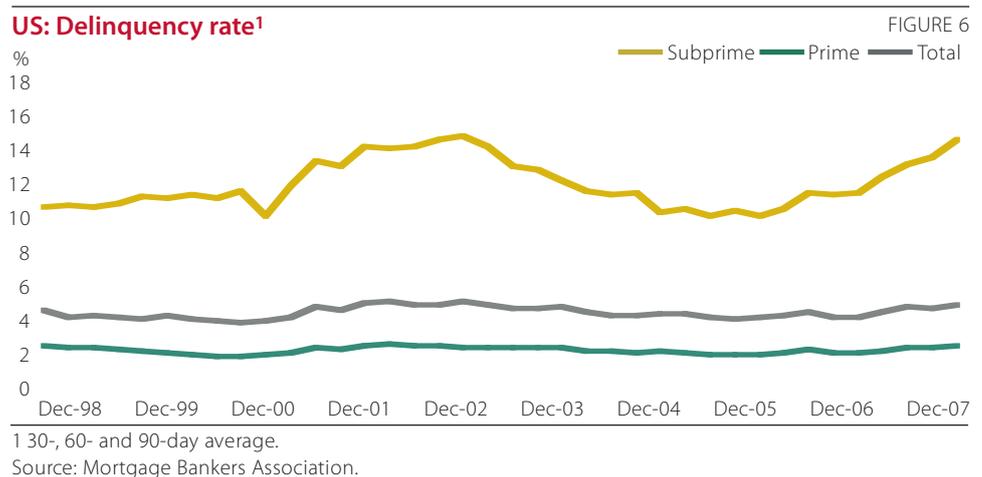
2.3 Transmission of the crisis to the financial sector as a whole

The subprime crisis is of financial origin, since, as we have seen, it sprang from an inappropriate appraisal of risk by certain financial agents and intermediaries in the process of granting mortgage loans to borrowers with high levels of credit risk. But, despite this financial origin, some of the questions posed in connection with the events of recent months are, for example, why did the crisis spread so quickly from the agents involved in its genesis to the financial sector as a whole, even beyond its initial

geographic scope so as to become a crisis with major international ramifications?; how has the problem arising from subprime mortgages managed to call into question some of the basic principles on which financial theory has traditionally been founded?; how is credit risk analyzed, and how are assets at risk valued? etc.

Some time before the final outbreak of the mortgage crisis, in the summer of 2007, some financial analysts and certain specialist media had been giving periodic warnings and publishing articles on the state of the subprime market. These analyses laid particular emphasis on the situation resulting from the high level of competitiveness attained by the US mortgage market, in which aggressive marketing by many lenders and intermediaries meant that credit was granted easily to applicants whose ability to pay it back was doubtful.

However, despite this state of affairs, at that time it was expected that, if the system were to collapse, this would cause a crisis in the property sector, by extension from the mortgage sector, but that its effects would be confined to the participants in this segment of the economy, not significantly affecting growth in the US economy as a whole and certainly not globally.



The perception of there being a crisis became more acute towards the end of the first quarter of 2007 (see timeline in table 2) as the problems of institutions directly linked in one way or another to the US mortgage sector became known. But there was no full awareness of the real scope of the subprime crisis and its spread to other international markets until the summer of 2007, when new players, in principle distant in geographic and business terms from the US mortgage sector, saw their results adversely affected by the presence on their balance sheets of holdings linked to subprime mortgages, and the domestic crisis in the US spread to financial institutions in other countries.

But how did these financial instruments get into the hands of other institutions not linked to the US mortgage sector? The contagion occurred through the improper use of the tools provided for structuring and spreading the risk associated with default in such portfolios of loans, already doubtful at source, with the issue of securities backed by subprime mortgages and, in addition, the multiplier effect of the involvement of structured investment vehicles (SIVs), and their cousins SIV-lites, which acted as redistributors of these risks towards new types of investor.

Moreover, as well as harming investors, these vehicles returned part of the insolvency risk to the loan granters through the liquidity lines that the SIVs had signed with the promoting financial institutions and which could be used by them in order to return cash to investors taking up the instruments issued by these vehicles in stress situations.

By structuring their subprime mortgage portfolios and transforming them into securities, US financial institutions removed the risk associated with such loans from their balance sheets and transferred it to vehicles which in turn issued bonds to be placed on the international financial markets.

With this asset transformation, investors in any part of the world had access and exposure to instruments backed by American subprime mortgages, which, moreover, because of the particular conditions of this market, had an ever poorer credit rating. The mortgage originators, for their part, were able to redistribute the risk in their mortgage portfolios to third parties, freeing their balance sheets and, in addition, obtaining liquidity with which to grant new loans to new applicants.

Thus the process was self-feeding, generating exponential growth in the sector. However, as we have said, the problems resided at source in the loan-granting system and the scant supervision at the point where mortgages were originated.

US: ABCP volume issued

FIGURE 7



Source: Bloomberg.

Moreover, from 2002 SIVs began to emerge seeking to arbitrage the yield gap offered by the positive slope in the curve of market interest rates. The SIVs had high leverage and invested in long-term financial instruments, with higher yields, financing their acquisitions with the issue of short-term securities with lower finance costs.

To attract funds they used asset-backed commercial paper (ABCP), and on many occasions bought assets linked to the American mortgage market. Similarly, the SIV-lites were a more risky version of these vehicles, as they repeatedly bought assets with collateral linked to subprime portfolios.

The first structure to declare itself in difficulties was *Rhineland Funding*, an ABCP vehicle promoted and run by *IKB-Deutsche Industriebank AG*. The fund had a renewable liquidity line with IKB and also with a number of other financial institutions. It was precisely this liquidity formula that transferred the problem directly to the supplier banks since, in mid-July, as a result of the deterioration of the US subprime market,

investors refused to refund the balance maturities of the fund's circulating ABCP and *Rhineland Funding* had to resort to its contracts signed with IKB and other banks.

From this moment rumours began to circulate on the market about IKB's solvency. Finally, concerned at the risk of the crisis of confidence spreading to IKB itself, *Kreditanstalt für Wiederaufbau*. *KfW Bankengruppe*, IKB's main shareholder, intervened to bail out the bank and assumed the obligations arising from the more than €12 billion committed in the credit line taken out by IKB. It also announced its intention to cover any losses that this structured-vehicle operation might cause.

At the same time in the US there were further casualties among the financial institutions hit by the subprime epidemic, which had spread to a large part of the country's financial industry.

Some milestones in the crisis

TABLE 2

8 March 2007	New Century Financial , the second-largest originator of American subprime mortgages, announces that it is ceasing to provide loans due its liquidity problems in financing itself.
13 March 2007	The stock of New Century Financial is delisted from the New York stock exchange.
2 April 2007	New Century Financial files for bankruptcy.
14 June 2007	Bearn Stearns : collapse of two hedge funds owned by Bearn Stearns investing in subprime mortgages.
Week of 16 July 2007	S&P lowers the rating of several CDO and RMBS operations due to their subprime exposure.
11 July 2007	Moody's puts under review some 200 CDOs with a view to downgrading them for including mortgage-backed tranches. In the next few days the main agencies announce further reviews and rating downgrades.
31 July 2007	KfW: the crisis spreads to Europe , as the bank announces that it will assume all the obligations resulting from IKB's exposure in <i>Rhineland Funding</i> .
6 August 2007	American Home Mortgage , the tenth-largest US mortgage lender, files for bankruptcy.
9 August 2007	BNP Paribas freezes the liquidity of three of its funds linked to the subprime sector, worth USD 2.2 billion, because it is impossible to value some of their assets appropriately.
10 August 2007	Countrywide announces that the situation of the credit markets will have a direct impact on its results. It is forced to use its credit lines signed with various financial institutions.
2nd week of August	The crisis moves to the stock markets, which show considerable losses.
14 August 2007	Sentinel Management Group asks the SEC to halt redemptions in several of its funds.
11 to 19 August 2007	Concerted action by the Fed , BCE , BCJ and the Bank of Canada to inject liquidity into the market.
21 August 2007	HBOS announces that it is to draw on the credit lines of its Grampian ABCP programme. At this time Grampian was the largest ABCP programme in the world with an active balance of more than USD 36 billion.
24 August 2007	Industrial & Commercial Bank of China , China Construction Bank and Bank of China : declare that they have assets linked to the subprime market. The crisis breaks out in Asia.
13 September 2007	Notthern Rock : the British mortgage bank experiences a mass withdrawal of deposits. The Bank of England announces a USD 45 billion bailout.
From the above date on	Write-offs and negative earnings become widespread in the results posted by the main US banks - Citigroup , Morgan Stanley , Merrill Lynch , etc. - and some European banks - Sachsen LB , UBS , Barclays PLC - are affected by the crisis.

Source: compiled by authors.

3 Consequences of the crisis on the financial markets

2007 was a highly complex year for the financial markets, with two clearly distinct halves. In the first part of the year the market followed the trend of the previous few years: stable financial asset yields, at levels similar to those of previous years, bullish stock markets and credit spreads at lowest-ever levels. But the end of the first quarter saw the start of the subprime crisis, finally setting off a full-blown credit crisis causing a sharp widening of spreads and reflecting a total lack of investor confidence in mortgage-related products, and especially in structured credit and, by extension, any assets containing credit risk.

Previously we remarked on the origin of the crisis and how it was transmitted from the subprime “sphere” to the international financial markets. We will now analyze some of the crisis’s main repercussions from what we have experienced so far in 2008, and with which we shall have to live for some time.

3.1 Lack of transparency. Crisis of confidence and crisis of liquidity

One of the most notable results of this crisis is the ability that it has shown to call into question the basis on which the financial markets have been developed in recent years.

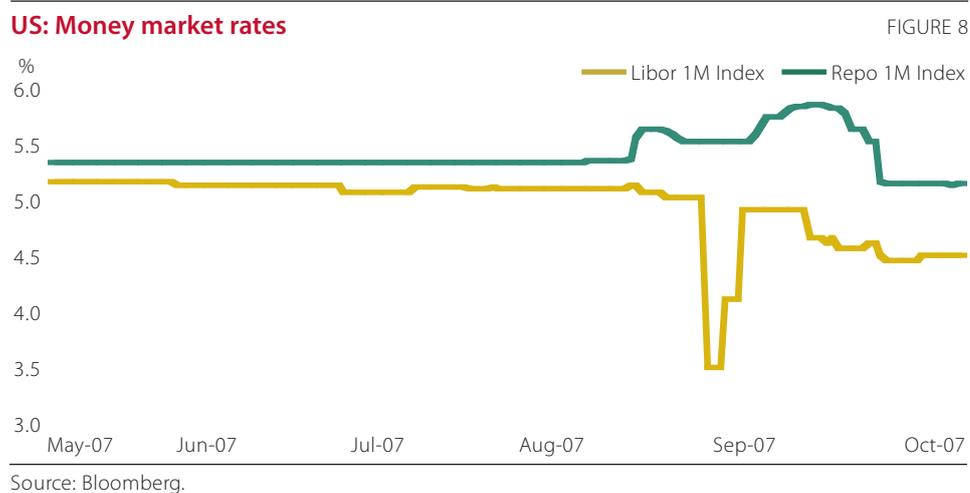
Many of the products issued using American subprime mortgage portfolios had a very high credit rating, often AAA, the highest level assigned by the international rating agencies that assess issuers’ insolvency risk and that of the financial instruments that they issue, and which is equal to the rating assigned to the public issuers in the main developed countries in the world, such as the US, German and Spanish treasuries, etc.

Institutional investors, which have traditionally established their investment policies on the basis of securities’ ratings, were soon attracted by these financial instruments which, a priori, enjoyed high solvency and allowed them to diversify their portfolios, given the very features of lower liquidity and comparative risk, and offered a yield pick-up that made them especially interesting in economic terms in an environment of rock-bottom interest rates. Did the risk level assigned to these products back then make sense? Experience has shown that it did not, and the expansion of the portfolios containing them led to a sharp drop in their price.

Moreover, most of the products issued with subprime backing were not quoted on the markets and therefore had no transparent benchmark prices for valuation. In the absence of real prices, investors used complex mark-to-model methods in order to obtain valuations and estimate their theoretical sale price. The inputs to these valuation models included factors such as mortgage delinquency ratios. As soon as there were sharp rises in delinquencies, the models were subject to stress that made their output unreliable, prompting investors to sell their positions.

Moreover, as mentioned above, these subprime mortgage packages were bought chiefly by institutional investors. First by hedge funds, or alternative investment funds, and in a second phase by other traditional investment funds, pension schemes, funds of funds, etc., which bought holdings in those hedge funds or in the

first funds that took out positions in these products, redistributing and fragmenting the subprime risk in the portfolios of countless institutional investors who were thereby contaminated. This situation made it even harder to ascertain the actual extent of the crisis's economic impact, and who was really affected.



The uncertainty regarding the real value of these assets, and the economic damage that could be done to their holders, up to the point of it being impossible to determine clearly which institutions were affected by the subprime question, triggered a worldwide crisis of confidence in the financial sector. Accordingly financial institutions decided, provisionally until they could get a clear view of the situation, to close down their loan lines and not to offer money to the interbank market, or at any rate to offer it with very short terms, causing interest rates to be tightened and liquidity to be choked off.

From then on uncertainty and volatility took hold of the international financial markets in what has come to be called the liquidity crisis, which, by extension, is affecting financial institutions not involved in the subprime phenomenon and whose consequences may grow to the point of causing much greater and more harmful effects in the sphere of financial economics and also in the real economy.

3.2 Widening of credit spreads

One direct result of the subprime crisis, shaping the new credit scenario, is the severe correction that financial assets containing credit risk have undergone in the past months in their risk premiums, and which has affected debt instruments and issuers of all kinds, regardless of their credit rating. Credit spreads have shot up in a process of repricing by investors prompted by an increasingly conservative attitude when assuming credit-related risk.

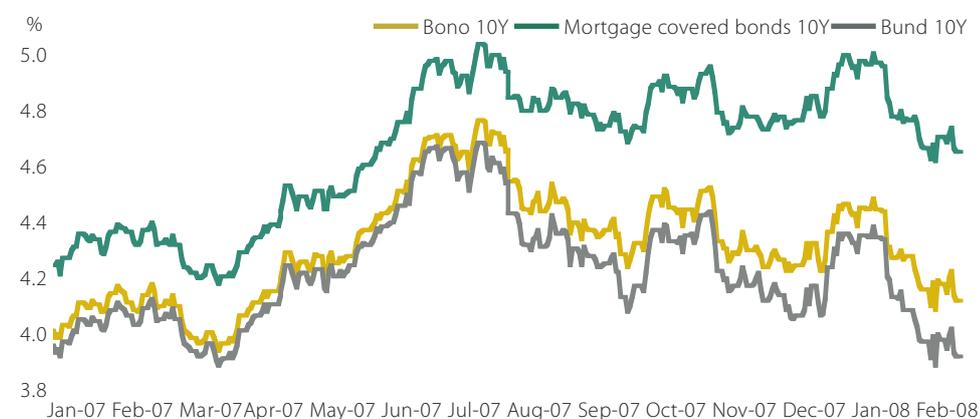
This situation has been very clearly demonstrated by the “flight to quality” in recent months. Investors have taken refuge and shielded themselves from the crisis by taking positions in the short-term public debt securities issued by the treasuries of the main developed countries, traditionally regarded as free of risk. This move

has caused a migration of short portfolios to treasury bills or other financial assets issued by the public sector. The move has also been reinforced by the non-renewal of many previous balances in asset-backed commercial paper (ABCP).

In short, as a first consequence of the crisis, analysis of credit risk associated with securities has become more complex and investors are going to be much fussier when analyzing an issuer's rating, the sector to which it belongs, the term of its securities or the covenants and degree of subordination that they contain. Greater attention is going to be paid to issuers' financial and business profile and to the features of their activities distinguishing them from others. In practice this will mean an end to the uniformity of credit spreads that has characterized the market in recent years, in which we had got used to using generic curves basically defined according to the rating and liquidity of securities.

Yields on 10-year AAA-rated issues

FIGURE 9



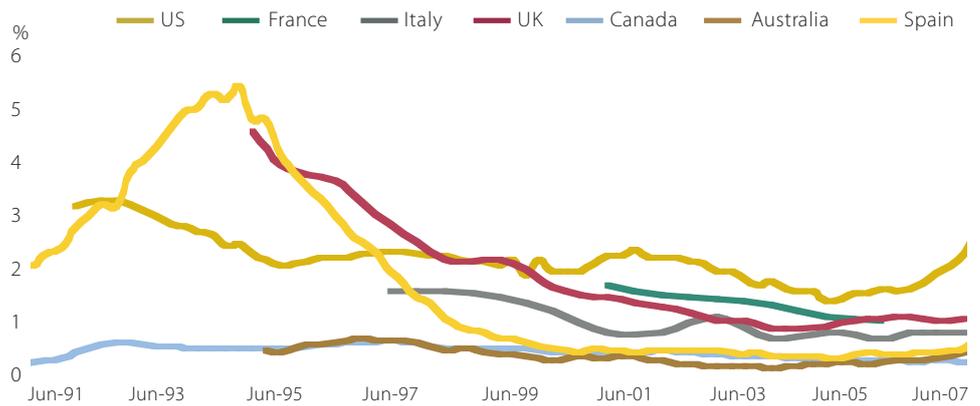
Source: Bloomberg.

In February 2008, after the correction undergone by the international financial markets, Spanish Treasury bonds saw their spreads in relation to their German counterparts rise above 20 basis points, while mortgage covered bonds doubled their spreads to the extent of 60 points being payable in excess of the German benchmark.

At times of economic downturn and slowdown it is normal for demand to shrink and for the spreads between the various government bonds to increase. In the case of securities with mortgage collateral issued in Spain, no great deterioration in the mortgage portfolios held by financial institutions has been seen. The widening of spreads is chiefly explained by the uncertainty among investors as to factors such as the rising trend in interest rates and the impact that future rises will have on family debt. The extent to which this situation will affect the mortgage market and whether the rising delinquency rate, normal in such cases, will significantly impact the earnings of financial institutions are questions which, along with the strong growth experienced by the Spanish property sector in recent years, are viewed by investors with caution.

Mortgage uncertainty rates in OECD countries

FIGURE 10



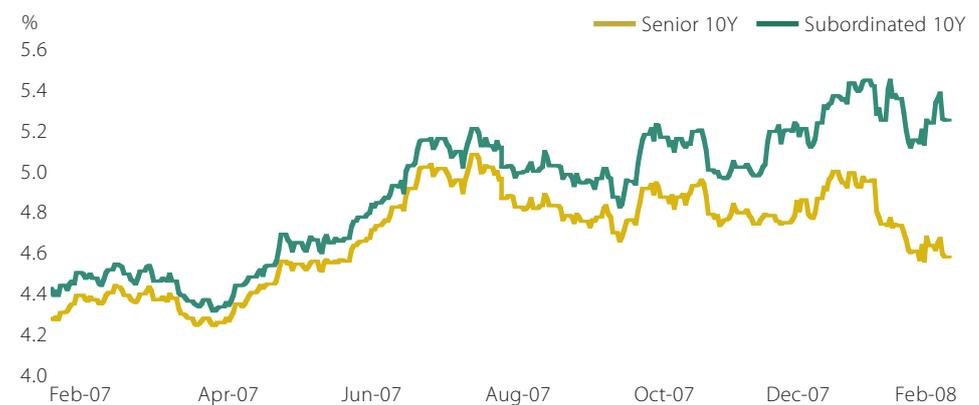
Source: OECE & AHE (Spanish Mortgage Association).

In this connection many attempts have been made to establish parallels between the situation experienced in the US in recent months and possible developments in the Spanish market. The economic slowdown is undeniably harming some of the ratios regarded as vital in securities with mortgage collateral. But it is worth recalling that, in the Spanish case, these figures, such as the delinquency ratios, are very distant from those of the American mortgage market, as regards not only subprime mortgages, which triggered the problem, but even the prime sector, which in the US is highly solvent and secure.

In addition, as has often been pointed out by the economic authorities and supervisors, the Spanish financial industry is one of the financial sectors in the world with the greatest volume of provisions. This circumstance, together with the lack of exposure to assets backed by US junk mortgages, the way in which business is done and the checks made in Spain in the origination of mortgages and their supervision by the Bank of Spain, is the best guarantee of the Spanish mortgage sector.

Yield on financial issuers' 10-year issues

FIGURE 11



Source: Bloomberg.

Spreads in the financial industry have also widened considerably since the subprime mortgage crisis. A clear example of this is the trend in the spreads between AA bonds issued by financial institutions in senior and subordinated

format, which have shot up in recent months. Senior 10-year AA bonds issued by a financial institution in January 2007 had a yield of just over 4.25%. In January this year such bonds were quoted at just over 4.70%. The same term in subordinated format went from 4.37% to 5.25%. Thus the financing costs through credit margins between senior and subordinated debt that financial institutions have to bear have risen from 12 basis points in early 2007 to 55 basis points in 2008. As a result it is going to be much more expensive for credit institutions to attract resources with which to bolster their financial stability.

Corporate spreads in basis points over Swap. February 2008

TABLE 3

Sector	Asset	Rating	5Y	10Y
Financial	Certificates	AAA	31	43
	Senior Debt	AA	92	110
	Lower Tier II	A+	195	225
	Upper Tier II	A-	278	318
	Tier I	A-	323	383
Corporate	Senior Debt	AA	79	101
Securitization	RMBS LTV ≤ 80%	AAA	148	
	RMBS LTV > 80%	AAA	182	

Source: compiled by author.

3.3 Effects on the primary market

The interbank liquidity crisis quickly spread to all terms on the yield curve. Thus since the outbreak of the subprime crisis we have seen a sharp drop in the volumes issued by the capital markets, especially by the financial institutions which used regularly to draw funding from those markets, and, though in absolute data the issuance figures for 2007 were higher than for 2006, such new issues dried up in the second half of the year.

This lower volume of issues has become clearly apparent in the securitization bond market on which, according to the European Securitisation Forum, the volumes issued in the third and fourth quarters of 2007 reached a figure of just 181 billion euros, representing a 39% fall relative to the nearly 300 billion euros recorded in the same period of 2006. This drop was especially notable in CDOs and RMBS (see tables 4 and 5).

Securitization issuance in Europe

TABLE 4

Euro billion	Q1	Q2	Q3	Q4	Total
2000	14.1	16.4	21.4	26.3	78.2
2001	20.5	43.2	22.7	66.2	152.6
2002	24.3	42.6	35.7	55.1	157.7
2003	43.3	51.9	39.7	82.4	217.3
2004	55.8	59.0	53.2	75.5	243.5
2005	47.8	94.4	41.5	143.3	327.0
2006	69.0	114.3	112.8	184.9	481.0
2007	150.7	164.3	107.8	73.9	496.7

Source: European Securitisation Forum.

Securitization issuance in Europe by collateral type

TABLE 5

Euro billion	2006:Q1	2006:Q2	2006:Q3	2006:Q4	2006 TOTAL
RMBS	37.6	49.3	58.0	99.7	244.6
CMBS	7.5	9.9	21.8	20.7	59.9
Car loans	0.8	1.0	3.2	6.8	11.8
CDOs	14.3	31.8	20.5	43.5	110.1
Credit cards	1.6	1.0	0.2	0.6	3.4
Leasing	0.4	1.0	0.3	4.2	5.9
Loans	1.2	5.4	3.0	6.1	15.7
Receipts	0.6	1.5	3.6	0.4	6.1
Other	5.1	13.4	2.2	2.9	23.5
Total	69.0	114.3	112.8	184.9	481.0
	2007:Q1	2007:Q2	2007:Q3	2007:Q4	2007 TOTAL
RMBS	81.8	77.8	52.6	47.5	259.6
CMBS	11.9	25.0	6.0	4.7	47.6
Car loans	2.2	6.0	2.7	4.0	14.9
CDOs	47.9	40.4	34.4	9.0	131.7
Credit cards	0.1	0.4	0.2		0.7
Leasing	1.7	2.5		0.3	4.5
Loans	5.1	8.2	7.2	6.7	27.2
Receipts		2.9	2.5	1.7	7.2
Other		1.1	2.2		3.3
Total	150.7	164.3	107.8	73.9	496.7

Source: European Securitisation Forum.

However, it is interesting to note that, by contrast with what has happened in Europe, companies in the US adapted to the new circumstances from the start, and though spreads in that country have increased three- or fourfold, companies have continued to issue paper and investors have continued to invest, showing that the American market has a liquidity and depth that give it a maturity much greater than that shown by the European market.

The capital markets have in the last few years been one of the main sources of funding for credit institutions. Procuring funding through issues of securities is currently a complex task involving, on one hand, a greater effort by the issuer as regards promotion, transparency and the convincing of investors, and on the other, the assumption of greater financial costs in so far as, as remarked on above, the spreads currently required by investors are higher than before the crisis.

4 Conclusions

As we have seen, the effects of the so-called subprime crisis have been felt not only in all the financial markets but also in economic activity worldwide, driven by the fall in global terms of the index – moreover hard to measure – of “confidence of economic agents”.

Basically, the origin of the crisis lies in the risky practices for providing finance – mainly property-backed – of financial agents in the US, which was subsequently distributed by very particular securitization processes, through the main international agents, to clients demanding high yield but little risk analysis.

The direct effects of the crisis might have been absorbed by the international financial system, but its transmission to the financial market as a whole through a “crisis of confidence” maintains uncertainty as to its likely duration and depth.

Our reflection focuses on the lessons which, with a view to a better operation of the fixed-income markets, may be drawn from the experiences of the last few months and, consequently, the improvements that need to be made in the current market model.

In this connection we have made a non-exhaustive analysis of the origin and development of the subprime crisis, its impact on the financial markets, the widening of credit spreads, its effects on the primary market and the difficulties encountered in asset valuation.

From all this we infer that a lack of transparency has been the key problem apparent in the fixed-income markets, contributing to the spread of the crisis of confidence and giving rise to most of the causes of the liquidity and funding crisis. This need to give the fixed-income markets more transparency is the underlying point in the proposals set out below.

This situation in the fixed-income market coincides in time with the enactment of legislation around the world on market operation by regulators and supervisors, prompted ultimately by the recognition of the financial markets as key factors in economic globalization and therefore of the need for them to operate efficiently and transparently.

In the European Union the legal arrangements applicable to markets have an overall approach, touching every sphere affected by regulation. Perhaps the most important piece of legislation is the European Directive on Markets in Financial Instruments (MiFID), in so far as it deals in a general way with almost all aspects of such markets’ operations.

As regards the matter in hand, the Directive establishes market transparency as a general principle. However, though it does so clearly and decisively as regards the equity market, probably because it is considered that this is where most retail investment takes place, it is indecisive as to the extension of this transparency to fixed-income markets, contrary to many of the basic principles upheld by the Directive itself. It is precisely equity markets which, by virtue of their way of working, currently show the highest levels of transparency, except perhaps in big corporate transactions normally linked to transactions in derivative products.

The financing markets on which fixed-income securities are issued are the principal and most innovative financial markets in the world, constantly generating ever more complex financial structures. The current model is fully decentralized, internalized and, for trading purposes, carried out outside the regulated markets (OTC)². These features naturally deprive it of a large degree of transparency, unless obligations are imposed on market operators. The example of TRACE in the US is, with its limitations, one to follow here. In this respect there is a surprising lack of determination on the part of the European economic authorities and supervisors when applying basic pre- and post-trade criteria to fixed-income securities, which may in turn ensure that the requirement of better execution is met.

² In the Spanish case there is a different situation, given the existence of a regulated market such as *AIAF Mercado de Renta Fija*.

If anything has been shown by this crisis, as regards market transparency, it is precisely that the assets with most pure risk, namely shares, have maintained transparency in their prices, and consequently in their liquidity, whereas the debt markets have remained in a degree of darkness in which what goes on is discernible only with the torches used by specialists.

The peculiarities of the fixed-income markets require a model different to that established for equity, but this does not mean that transparency criteria cannot be fully applicable to them.

Transparency, which is precisely what has proven to be most lacking as the crisis has unfolded, is of value in itself, regardless of its positive effects on liquidity and market development. In this respect MiFID contains sufficient elements to undertake a reform of these markets and to include transparency as a requisite in improving the way they operate.

A suitable treatment of the MiFID requirements for pre- and post-trade transparency, better transaction execution and reporting and a differentiation between investors basically involving, in market terms, wholesale and retail investors, should form the basis of changes liable to include greater levels of transparency in the operation of the fixed-income markets.

In essence we propose two measures:

- Transparency in transactions as a criterion extensible to all product types
- A change in market model for transactions aimed at retail investors

Regarding the first point, we should say that the current situation is peculiar in that, under MiFID, it is obligatory for all transactions made by credit institutions and investment companies (ICs) to be reported to the market supervisor, whereas the requirement of post-trade transparency is not applicable unless expressly so decided by a Member State. In short, all transactions are known to the supervisor but the data involved are not made public.

Moreover, given the nature of these markets, it is necessary for the information gathered to undergo a prior analysis in order for the data to be presented in an intelligible way and for transparency to be meaningful, beyond an exhaustive list of prices and volumes.

On this basis, the use by the Member States of their prerogatives in relation to post-trade transparency, along with imaginative formulas for cooperation between market agents, would solve the problem of transaction price and volume information and the publicity thereof, with no particular need for additional efforts and expenditure by credit institutions and ICs.

Moreover, the introduction of a system similar to TRACE, which anticipates the reporting of transactions, would provide information closer in time and therefore of more value in terms of transparency.

With these measures, the information on the prices and volumes of most fixed-income products would undergo a radical change, and this would in turn allow the portfolio investments of the various institutions to be valued appropriately, all without changing the operating formulas used on the fixed-income markets.

For products aimed at retail investors, however, it seems advisable to apply additional measures. The features that products must have in order to be regarded as aimed at retail or wholesale investors are specified in the regulations on issue prospectuses. But the need for greater protection of retail investors makes it advisable for issues aimed at such clients to enjoy more pre-trade transparency, regardless of the product's internal structure.

In this respect the regulated markets should provide flexible trading systems which, together with the existence of the figure of security creator or caretaker that is currently required for certain issues, would modify the current model, bringing it in line with that existing on the equity markets.

To sum up, and regardless of the other effects analyzed in this article, there can be no doubt that a lack of transparency has been the most notable factor in the progression of the crisis in the fixed-income markets. The process of adapting to the MiFID directive may allow modifications to be made in the financial markets so as to remedy this information shortage. The measures proposed here are founded on the basic principles of MiFID and, in our view, constitute the challenge to be met by the fixed-income market in the coming months.

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Current situation and projects underway affecting securities clearing, settlement and depository systems in Europe

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1 Introduction

The securities markets have not been unaffected by the phenomenon of globalization in the financial industry. The response in Europe has sought to address the industry's fragmentation and to reduce the large current number of trade and post-trade infrastructures. The introduction of the euro, the resulting regulation provided in the Financial Services Plan and other industry initiatives have given rise to successive concentration processes in market infrastructure around various large national and, in some cases, multinational groups, mitigating the fragmentation of the last decade, though in a pan-European framework the integration has been limited.

In a new attempt to promote integration certain initiatives have emerged recently in European institutions with the aim of fostering greater competition between market infrastructures with measures such as free access and choice of infrastructure for intermediaries, or the removal of historical monopoly privileges in the provision of some services. All these measures are aimed at reducing monopolistic practices and encouraging transparency.

The purpose of this article, based on a joint report issued by the CNMV and the Bank of Spain in December 2007 on post-trade systems in Europe, is to outline the content and implications of the recent Community initiatives in this field. Accordingly this article is structured in five sections, starting with this brief introduction, followed by a second section on the current configuration of the European securities markets. The third section will remark upon the European initiatives currently underway (the Code of Conduct and the Target 2 Securities project) and the changes to which they may give rise in European post-trade infrastructures in general. The fourth section will deal specifically with the current post-trade situation in Spain, briefly describing its particular features and the possible impact of the current European initiatives. The article will end with a fifth section setting out some brief conclusions on some of the measures that could be taken to help improve the context in which these services are provided in Europe and to improve efficacy of the Spanish clearing and settlement system in a framework that would be more open and probably more competitive than the current one.

2 General configuration of the European securities markets

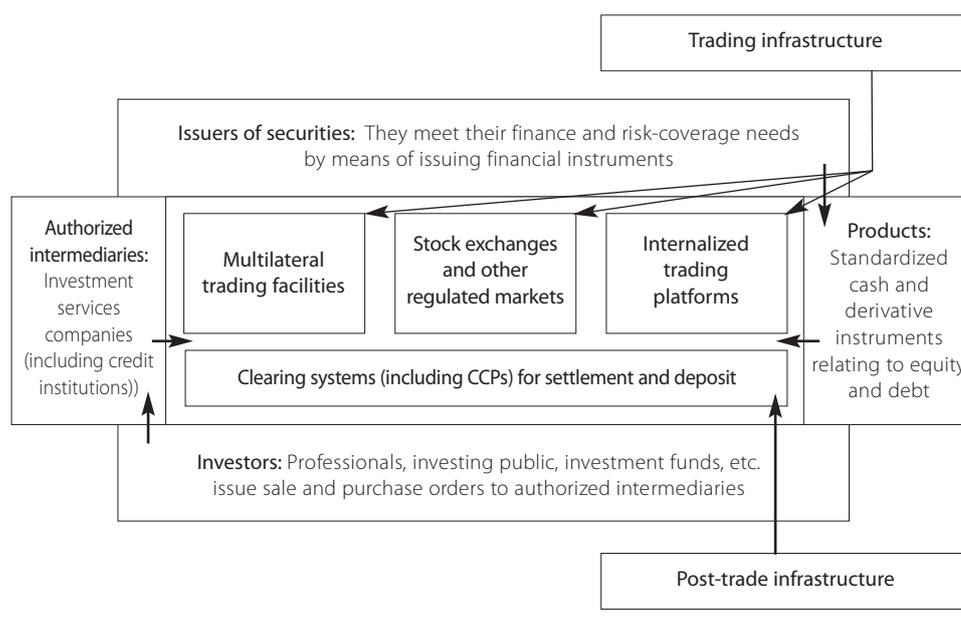
The securities markets are configured in two overall families of infrastructure, according to the various stages making up the process, from the search for a counterparty and the matching of supply and demand to a transaction's completion

with the transfer of the securities' ownership and the receipt of payment. Such infrastructure may be grouped into two categories: trade and post-trade.

Trading infrastructures are physical or electronic forums containing the supply and demand in financial instruments (hereinafter "securities") and in which the terms of trading are agreed: amount, price, buyer and seller. The official or regulated markets for shares (stock exchanges), debt or futures and options are the traditional trading infrastructures but there are also other legally recognized forums such as platforms for the "internalization of transactions" and multilateral trading facilities.

Participants in securities markets

FIGURE 1



Transactions are matched in trading infrastructures, but trades are completed and concluded in post-trade infrastructures. These manage the processes of delivering securities to buyers and payment to sellers, and provide proof of who owns the securities.

Post-trade processes are carried out consecutively in three core activities: (i) clearing, (ii) settlement and (iii) custody/deposit of securities. These three activities may be performed by a single organization or by different organizations specialized in each one.

2.1 The main European securities infrastructures

Historically post-trade securities infrastructure has been closely linked, and even joined, to trade infrastructure, by which post-trade activities were treated as ancillary to trading. The advent of new technologies forced market infrastructures to specialize so as not to show a loss, leading in turn to the splitting of cash securities trade and post-trade activities into distinct infrastructures.

The concentration of markets in Europe in response to financial globalization has, with a few exceptions, been chiefly in the national sphere, bringing about only a limited integration of market infrastructure at pan-European level, following two distinct consolidation models, one vertical and the other horizontal.

In the vertical model, trade and post-trade infrastructures are integrated in a single group under the same holding company. The Spanish group BME, together with the *Deutsche Börse* and *Borsa Italia* market groups, are vertically integrated. In the horizontal model, the integration is between organizations that perform the same type of activity, either trade or post-trade. Groups such as the *London Stock Exchange* (LSE), *NYSE-Euronext*, *OMX* in Nordic countries or *SWX* in Switzerland are examples of horizontal groups formed around trade infrastructures, whereas groups such as *LCH.Clearnet*, *Euroclear* and *NCSD*, are examples of horizontal groups formed around post-trade infrastructures.

Vertically integrated groups generally complete trades made in their trade infrastructures solely in the post-trade infrastructures that they control. This exclusive relationship, or partnership, between trade and post-trade infrastructures is also to be found in horizontal groups. Thus the *Euronext* group (currently *NYSE Euronext*) has been using the *LCH.Clearnet* group almost exclusively as a clearing house and the *Euroclear* group for settlement and custody/deposit. These same organizations were until recently the clearing and settlement standards for the *London Stock Exchange* group, which for equities continues to use a subsidiary of *Euroclear* (the former *Crest.Co*) as a central depository, and the two largest exchanges in the *OMX* group (Stockholm and Helsinki) have for their part traditionally used the organization *NCSD*¹ as their central securities depository.

The size of the main market groups may be seen in the four comparative tables and figure attached in the Annex at the end of this article. Of the three leading groups – *NYSE-Euronext*, *London Stock Exchange* and *Deutsche Börse* – two are horizontal and one is vertical, and the others are relatively far behind. The Spanish group BME is third or fourth, depending on the parameter considered, practically on a par with *Borsa Italiana*, a group acquired in September 2007 by the *London Stock Exchange* group in a takeover.

All these groups have profits and return on assets and equity in two digits, for to date each one has had its own slice of the market with few openings for competition.

2.2 The framework regulation to which the securities markets are subject

The field of securities markets has been tightly regulated and subject to specific national legislation in all jurisdictions. But the national regulations of the 80s and early 90s, either home-produced or inspired by the US ones, have now been replaced by the principles of Directives and Regulations emerging largely from the Financial Services Action Plan launched in 1999.

¹ Both *NCSD* and *LCH.Clearnet* and *Euroclear* were, in December 2006, independent entities or groups whose assets were not controlled by any of the market groups to which they provided post-trade services.

European legislation on the securities markets addresses various aspects of the investment services industry and imposes various obligations on firms providing services to other participants in such markets. However, the currently applicable Directives contain few references to the organization of the activities of market infrastructures. Directive 2004/39/EC on markets in financial instruments (MiFID) partially addresses some aspects of market infrastructure. But MiFID seeks only to increase competition in the provision of services between infrastructures, without regulating their type or way of working.

Thus in the trading sphere, MiFID makes it obligatory to allow intermediaries remote access to regulated markets and removes the monopoly that those markets, and in particular stock exchanges, had over share trading. In the post-trade sphere, MiFID declares that intermediaries are free to choose their clearing system.

Apart from the partial treatment given by MiFID, the only post-trade questions covered by Community regulations are to be found in Directive 98/26/EC on Settlement Finality in Payment and Securities Settlement Systems and Directive 2002/47/EC on Financial Collateral Arrangements. The European regulations provided in these two Directives focus chiefly on demands for legal certainty and the protection of participants in clearing and settlement systems, excluding securities depository questions.

European regulations have not yet addressed key issues for the efficiency and security of clearing and settlement and depository systems such as price transparency, requirements for participation in and access to post-trade infrastructures, organizational requirements, the risks to be assumed, capitalization requirements or the supervision to be undertaken by the competent authorities.

The few harmonizing initiatives on basic aspects of the risks in clearing and settlement and on the legal framework for these processes have all been of a non-binding, consultative nature. Among these we should mention those of the CESR-ESCB² group, which embarked on a certain harmonization process by defining standards in some of these fields, before being shelved due to lack of agreement.

In a more global sphere, we should also mention the international legal initiatives in the field of rights attributable to securities held in custody by financial intermediaries, such as the Hague Securities Convention – not yet ratified by EU countries, and it seems they are not going to sign up to it – and the Unidroit Convention on Intermediated Securities, which is in its final stages and might be adopted this year (2008).

² In October 2001 CESR and ESCB set up a joint working group to develop “Standards for securities clearing and settlement systems in the European Union”. The document put out for public consultation in September 2004, drawn up on the basis of recommendations defined by CPSS-IOSCO in 2001, contains 19 standards covering, among other things, the legal framework, settlement mechanisms, securities lending, governance, user protection and links between settlement systems. The opposition of a CESR member to the standard’s conclusions, which might have given rise to a Directive, has for the moment prevented the project’s completion.

3 Current initiatives affecting the activity of European post-trade infrastructures

In order to mitigate some of the effects of the lack of European regulations and, chiefly, to continue promoting greater integration in European markets and their infrastructure, two non-legislative measures of notable scope have emerged: the voluntary Code of Conduct promoted by the European Commission (and in particular by Commissioner McCreevy) and the European Central Bank's *TARGET2-Securities* (T2S) project. These initiatives might come to affect the configuration of infrastructures in the European market more even than the MiFID Directive.

3.1 The Code of Conduct promoted by the European Commission

This Code, published in November 2006³, consists of a set of voluntary measures and covers chiefly post-trade activities in cash equities, though it may later be extended to cover other financial assets. The Code concerns two types of organization: (1) those providing clearing services such as central counterparties (CCPs) and some central securities depositories (CSDs); (2) those providing securities settlement and custody services, such as CSDs; and (3) stock exchanges and other markets providing trading services.

The measures provided in the Code are grouped into four phases with specific implementation deadlines: (1) by 31 December 2006, price transparency; (2) by 30 June 2007, conditions for free access and interoperability between infrastructures; (3) by 1 January 2008, unbundling of services and accounting separation; and (4) monitoring of compliance with the Code (with no specified deadline), both by the organizations themselves, with the help of external auditors, and by the EU.

The Code of Conduct has been adopted by almost all post-trade markets and infrastructures geographically located in Europe. Thus it has been signed up to by most of the markets belonging to the Federation of European Securities Exchanges (FESE), the houses belonging to the European Association of Central Counterparty Clearing Houses (EACH), and the CSDs belonging to the European Central Securities Depositories Association (ECSDA).

3.2 Impact of the Code of Conduct

The Code is a self-regulatory measure that needs less time for implementation than a Directive. The Code prompts the industry to voluntarily adopt certain measures allowing the barriers⁴ to competition between post-trade infrastructures to be removed.

One of the problems to be addressed by this Code is that there is still not a suitably level playing field between European infrastructures in post-trade activity, for national legislation allows them to provide non-uniform services

³ European Code of Conduct for Clearing and Settlement, 7 November 2006.

⁴ These barriers were highlighted in the 2001 and 2003 reports on settlement mechanisms in the EU drawn up by a group of experts chaired by professor Giovannini.

and to assume unequal risks. Moreover, the costs of developing connections between systems could, because of the current asymmetry, be uneven, and so infrastructures could delay their development until they have ascertained whether they may, either themselves or with others, reasonably recover them. Finally, the Code does not cover issues linked to the deposit and holding of domestic equities in other CSDs or the implications of the various legal systems for the recognition and custody of securities.

In any case, the various measures provided for in the Code, such as interoperability, transparency and service unbundling, are highly positive, as they will help enhance competition and lead to price reductions in activities which, in the case of post-trading, operate as a natural monopoly on national markets and which, partly for this reason, are fragmented across Europe.

The Code will require greater cooperation between the authorities supervising infrastructures and the activity of securities markets, as it will presumably encourage cross-border trading.

3.3 The Eurosystem initiative: the T2S project

The preparations for the launch of the new *Target 2* payment system by the Eurosystem revealed a need to achieve greater harmonization in the settlement of securities in Europe. It was in this context that the T2S project emerged in July 2006.

This technical platform would be devoted, under a single system, to the national and cross-border settlement of securities in Central Bank money. It would be owned and managed by the Eurosystem, and the membership of the CSDs would involve the transfer to T2S of all settlement (all transactions against payment and free of payment) for all cash securities of any kind.

The T2S platform's settlement activity would have a wide scope and various transaction matching services would be offered. It would follow an optimized model of securities and cash settlement by gross amounts (DvP¹⁵ model) from the international payment bank, although there would be optimization mechanisms and algorithms to facilitate the settlement of securities (queue and chain transaction management, technical netting, etc.) and of cash (automatic provision of intraday credit or self-collateralization).

T2S's clients would be the CSDs that join voluntarily, along with their participants, although these would be linked through the member CSD, which would be the entity in direct contact with the platform. However, the plan is for the participants, with the agreement and authorization of the corresponding CSD, to be able to communicate directly with T2S.

The securities accounts and balances of the member CSDs will have to be supplied to T2S so as to form the platform's securities databases. The platform will charge to and pay into these accounts and automatically update their

¹⁵ DvP stands for delivery versus payment, and the number 1 identifies a gross settlement model, in which purchases and sales are settled one by one with no offsetting of securities or cash payable, i.e. on a gross basis.

balances. These will be available for the CSDs and their participants in real time, as the CSDs belonging to T2S will continue to be legally responsible for the opening, maintenance and closure of securities accounts, and for the deposit and custody of their balances.

The ultimate legal status of the T2S platform, for which the final implementation date is reckoned at 2014, has yet to be determined, and its legal basis will be of significance, for joining it might infringe the national legislation governing the various countries' CSDs, giving them exclusive securities settlement and depositary functions in the domestic sphere.

The T2S project has been promoted by the central banks in the eurozone and, to date, has been widely supported by the European authorities and financial institutions. The CSDs' position is for the moment one of caution, given the possible impact of the transfer of settlement management to the T2S platform, for this activity is normally one of their chief sources of profit.

3.4 Impact of T2S on post-trade infrastructures

The T2S project harmonizes the settlement of all securities denominated in euro and settled in Central Bank money, and it will be a major boost to the integration of eurozone markets in financial services. It is also designed to maximize synergies with other projects, such as Target 2 or the future Eurosystem collateral framework, which will allow the management of collateral in the euro zone to be streamlined, and promote greater harmonization.

T2S is designed to generate sufficient economies of scale and of scope in order to enable annual settlement costs to be reduced so that a single price may be offered for all securities trading, whether national or cross-border. But given that T2S makes all settlement a cross-border process, as it treats domestic and foreign trading in the same way, the national CSDs operating locally with settlement costs considerably lower than the EU average will feel this cost reduction to a lesser extent.

T2S is a project that is intended to be neutral and to treat everyone equally, regardless of their size, and offers a response to the complex links between infrastructures promoted by the Code of Conduct and to the uncertainty as to whether the costs of developing these links will be recovered. By centralizing settlement in euro in the EU in a single infrastructure, T2S makes it unnecessary to undertake investments for interconnecting the various settlement platforms.

The T2S project also helps increase competition by enabling financial intermediaries to concentrate their securities holdings in the CSDs of their choice, thereby enhancing intermediaries' freedom of choice.

National CSDs may offer access to all eurozone securities through connections with the other central depositories, for T2S allows transactions to be settled against payment between the participants in the various CSDs and in Central Bank money, as in domestic transactions. National CSDs could act as single points of access for

their clients to all securities in Europe, provided that they offer the corresponding custody and administration services. This is an opportunity that may be taken by national CSDs which, like the Spanish Iberclear, operate in a jurisdiction in which there is a lot of investment in securities abroad.

In the other direction, the big international depositaries, whose outlets and subsidiaries are usually clearing members in the domestic sphere of the national CSDs, could centralize the custody of all their securities in Europe in another jurisdiction. This could be the case of the outlets and subsidiaries of the big global depositaries that are highly active in the local settlement business, as in Spain and other European countries.

The national CSDs joining the T2S platform would lose their settlement function, but the impact of this in money terms is not expected to be necessarily equivalent to their possible loss of settlement revenue, as the CSDs may charge their participants a portion of the cost billed by T2S and cut costs by assigning resources previously engaged in settlement to other activities.

As regards the supervisors of conduct in securities markets and of prudential solvency, in order to prevent the risk of losing information in real time for the end-to-end monitoring of transactions, the T2S project should ensure that the necessary mechanisms are provided for the control and monitoring of the settlement process.

4 Situation and development of post-trade activity in Spain

4.1 Regulation and peculiarities of post-trade cash-securities activity in Spain

Post-trade activities for fixed-income securities in Spain may be regarded as in line with the rest of Europe, in so far as the various fixed-income trading models in Europe are similar. In the case of fixed-income securities, the centralized trading models in Europe are the product of specific historical developments in each country and therefore are not uniform, as is the case of the associated post-trade models. The main differences between the Spanish legal system for the clearing, settlement and deposit of fixed-income securities and that of the main EU countries are as follows:

1. The Spanish stock-market regulations provide that finality in stock-exchange transactions occurs with the trade, and accordingly, as a result of this legal arrangement, transactions cannot, once concluded, be cancelled even if the securities to be delivered by the seller do not appear at the time set for settlement or the buyer has no money with which to pay for them. The rights associated with the securities being bought (D day) are recognized at the time of the trade for legal purposes, without waiting for the settlement to be made (D day + 3). This model presupposes that all stock market trading in any one session will

necessarily be settled and, moreover, given that delivery is guaranteed as a governing principle, the provision of a central counterparty has historically been seen as an unnecessary burden on fixed-income securities, which is why the Spanish settlement system has no such risk mitigation system for these securities.

In most jurisdictions, transactions may be cancelled if they cannot be settled, and trading finality is achieved only on settlement.

2. The settlement of stock-exchange securities is multilateral – in keeping with trading, which is also multilateral, and in order to be a member of the Spanish stock exchange one must also be a clearing member of Iberclear, as the model considers that any trading member must be able to be liable for the multilateral risk introduced into the system and to settle what has been traded. Members must therefore be participants in clearing and provide certain guarantees individually. If these guarantees are insufficient, given that the system operates multilaterally, not bilaterally, the other participants in each session are temporarily obliged to make up the shortfall⁶. Hence the individual guarantees to be deposited by clearing participants, taken as a whole, become general joint, several and multilateral guarantees to cover pecuniary risk arising from settlement defaults. This is the alternative adopted by the Spanish system in the absence of a CCP.

Other settlement systems also operate multilaterally but in one way or another allow transactions to be matched and settled bilaterally. This possibility does not exist in the Spanish system, in which making trade settlements bilateral is not allowed and would be highly difficult.

3. The regulations make payments and debits in security accounts conditional on the sending or cancellation of numbers called *referencias de registro* (deposit references, DR) and requires Iberclear and its participants to keep a DR file covering the balances in each security. It is the Spanish stock exchanges⁷ which, in each session and for each purchase transaction, assign DRs. In order for purchases to be settled, all that is required is for the buyer to have delivered the corresponding cash, enabling DRs covering the relevant securities to be assigned. For sales to be settled, specific, individualized DRs must be provided (not any DR may be used). The existence of DRs, and the way they are used, is a product of the impossibility of cancelling transactions in the Spanish equity settlement system, and this in turn is an effect of trade finality.

The DR system is unique and characteristic of equity depositary functions in Spain. The most widespread model in Europe is settlement administration by a system of balances.

⁶ In practice, if the guarantees need to be executed, they will become effective on a date after the settlement day, D+3.

⁷ This is a difference in respect of what happens with fixed-income securities, where the process of identifying transactions to be settled is carried out by the CADE system with its participants (the managing entities in CADE for transactions with their clients).

It is worth adding two more differences, namely, on one hand, the wide scope of Spanish post-trade regulations as compared to other national regulations, and on the other, as in other European systems, the fact that the Spanish system does not recognize fiduciary ownership, though more than 50% of the turnover on the Spanish stock exchange comes from non-resident investment, of which the title-holders are often financial intermediaries based in an Anglo-Saxon country, acting more or less implicitly as fiduciary holders. This phenomenon has grown in recent years due to the lack of worldwide harmonization, and the supervision and certification of the final ownership of accounts managed centrally by the national continental European CSDs have rather suffered as a result.

4.2 Impact of European initiatives on Spanish post-trade activity

The securities industry in Spain must face up to the changes taking place in Europe. In particular, in the field of clearing and settlement, the three initiatives – MiFID, the Code of Conduct and the T2S project – pose considerable challenges to post-trade infrastructures. The effects of these initiatives were described in general terms in our third section. Now we will describe the differential effects that will occur in the case of Spanish infrastructures, due to the peculiarities of their regulations and organization.

The unbundling of equity trading on stock exchanges, as well as possibly taking business away from the stock markets, together with the free choice of settlement systems, could make it difficult to indefinitely maintain certain features of the current Spanish depositary model, especially the obligatory keeping and use of DRs by intermediaries wishing to settle Spanish equity.

The DR system is so different from the general system of account-keeping by balances (the most widespread one) that it requires a considerable prior learning process and computer routines adapted ad hoc so as to be able to meet Iberclear's specifications without making errors, which are moreover penalized with fines, making this learning and adaptation process even more onerous. The maintenance of DRs for any new intermediary wishing to settle transactions in Iberclear is a disincentive to access or participation in the Spanish platform by new European intermediaries.

Moreover, given the barriers represented by the current requirements concerning the settlement system and depositary administration for Spanish equity by means of DRs, in the medium and long term we could see a relocation of non-resident equity trading so as to elude these barriers and be settled more easily outside the Spanish system.

As to the possible adaptation of non-listed public and private fixed-income activity to T2S, no substantial changes are likely to be required in the systems currently used by Iberclear. Adjusting Iberclear's settlement model for equity to T2S may be more problematic. Especially if certain differential characteristics of the Spanish model are maintained:

- Spanish equity settlement is on a gross basis for securities and on a net basis for cash (DvP2 model), whereas in T2S both securities and cash will be settled on a gross basis (DvP1), optimized so as to resemble net settlement (DvP2 and DvP3 models). The T2S platform could offer CSDs the possibility, which they would pay for, of multilateral settlement by net amounts on markets that do not use a central counterparty (such as the Spanish retail equity segment), but this would not avert the need to modify some of the current stock exchange settlement procedures.
- Adjusting stock exchange settlement to T2S may be highly complex given the differential and interlinked characteristics of the Spanish model: finality in trading, not on settlement, and certification of sales with specific prior DRs. Between them these features prevent the cancellation of transactions once concluded. The T2S platform will work with a single system and a specific settlement method to which the CSDs joining it will have to adapt, and at this initial stage no functionalities allowing for national peculiarities are anticipated. In this context it may be difficult to make the Spanish model (which does not provide for the cancellation of transactions once concluded) compatible with another one such as T2S, in which transactions are final if they are settled, and otherwise are cancelled. To prevent malfunctions Iberclear would have to ensure that everything sent to T2S were settled without fail.

5 Conclusions

Spanish securities infrastructures and in particular post-trade ones must participate fully in the European initiatives designed to encourage competition and greater integration. At the same time, the Community authorities should undertake more ambitious projects. These should seek greater Europe-wide regulatory harmonization in securities settlement practices and also in the regulation and organization of the activities of infrastructures providing these services and of the risks that they may assume.

This harmonization should affect securities depositary and custody activity, the role of financial intermediaries in the custody of securities, the functions of the central depositary and the conditions for certifying the ownership of securities.

The most plausible solution to the fragmentation of securities settlement practices in Europe is currently the T2S project, designed to unify processes and integrate systems. Those in charge of the project should for their part ensure that there is no diminishment of the current capacities and powers for supervision of the processes involved in T2S and of the participating entities.

In the domestic sphere, the Spanish post-trade system for cash securities should be developed so that all its processes are made more equivalent to the most widely accepted European practices. This may require greater independence

from the trading platforms to which it provides services, including those to which it has historically been linked, moving towards a more universal service provider model allowing it to compete more openly in Europe and to interact with a greater number of European intermediaries participating in settlement processes. To this end it would be necessary to:

- Study the possibility of updating the system for equity, replacing the DR monitoring system with another more flexible system for the numerical supervision of transactions, more in line with the general practice in Europe. This might involve a review of the point at which transactions concluded on the markets become final, so as to adapt the system to the most widespread pattern in which finality is reached only with the exchange of securities and cash.
- Evaluate the feasibility of establishing a CCP for equity in Spain so as to simplify pre-settlement procedures and to be able to process transactions from other Spanish and foreign securities markets.

6 Annex

Basic financial magnitudes. 2006¹

TABLE A.1

Millions of euros; IFRS principles			Deutsche	Borsa				
	LSE	Euronext	Börse	Italiana	OMX	SWX	BME	
Financial magnitudes								
Net profit	163	374	666	63	101	102	131	
Total assets	393	2,676	65,025	21,313	1,386	450	4,385	
Non-current assets	195	1,401	1,908	361	587	52	149	
Current assets	198	1,276	63,118	20,952	798	398	4,236	
Equity (I)	(515)	1,718	2,283	319	510	380	428	
Non-current debts (II)	423	429	646	158	179	8	11	
Current debts	485	529	62,095	20,837	696	73	3,946	
Working capital	(287)	746	1,022	116	102	325	290	
Staff								
Average workforce	446	n/a	2,739	456	1,324	430	721	
Workforce at year end	444	2,324	2,966	472	1,402	424	724	

Source: Market reports and prepared by author.

¹ Data for the year ended Dec 2006, except LSE, ended Mar 2007.

Revenue from services to third parties, 2006¹ (excluding internal turnover)

TABLE A.2

Millions of euros; IFRS principles	LSE	Euronext	Deutsche Börse	Borsa Italiana	OMX	SWX	BME
Revenue from sales	514	1,102	1,854	274	367	264	285
Cash market	334	367	229	108		123	162
Clearing and settlement	n/a	15	786 ²	99	176	n/a	62
Derivatives	14	392	598	20		114	24
Reporting	156	112	148	47	62	24	26
Consulting and technology	n/a	185	94	n/a	129	n/a	11
Corporate services	11	33	0	0	n/a	4	0

Source: Market reports and prepared by author.

¹ Data for the year ended Dec 2006, except LSE, ended Mar 2007.

² This figure of 786 does not include banking revenue, which DB itself excludes from its sales and services revenue.

Earnings before interest and tax. 2006¹

TABLE A.3

Millions of euros; IFRS principles	LSE	Euronext	Deutsche Börse	Borsa Italiana	OMX	SWX	BME
EBIT	256	409	1,028	107	142	120	185
Cash market	208	192	174	60		33	117
Clearing and settlement	n/a	10	536	54	104	n/a	48
Derivatives	7	170	479	5		76	13
Reporting	77	73	95	15	28	20	19
Consulting and technology	n/a	30	(148)	n/a	10	n/a	3
Corporate services	(36)	(66)	(107)	(27)	n/a	(9)	(16)
EBIT over third party revenue	50%	37%	96%	39%	39%	46%	65%

Source: Market reports and prepared by author.

¹ Data for the year ended Dec 2006, except LSE, ended Mar 2007.

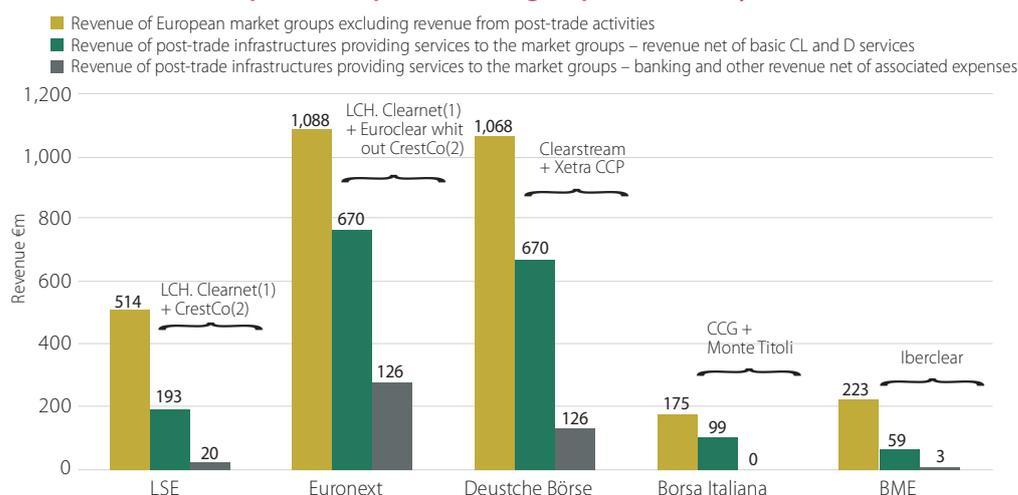
Detail of the turnover and financial magnitudes of post-trade infrastructures TABLE A.4

Amounts in millions of euros (2006) – Revenue and expenditure and financial magnitudes	Euroclear(a)	LCH.Clearnet(a)	Clearstream + Xetra-CCP	CCG + MT	Borsa Italiana Iberclear	BME(a)
Revenue from clearing, settlement and custody/depository services	814	386	786	99	62	
Revenue from clearing activity			86	35	n/a	
Revenue from settlement activity			150	24	30	
Revenue from depository activity + issuer and custody services	802	364	434	40	29	
Other revenue associated with clearing, settlement and depository services	12	22	116	0	3	
Revenue from banking interest net of financial expenses	271	58	10	n/a	n/a	
Total operating revenue	1,085	444	796	99	62	
Operating expenses: staff and external personnel	-621	-204	-361	-42	-13	
Amortization and depreciation	-46	-62	-52	-3	-4	
EBIT (operating earnings before interest and tax)	418	178	383	54	45	
EBIT over operating revenue	39%	40%	48%	55%	73%	
Total gross assets associated with these infrastructures	14,057	274,113	8,101	21,150	980	
Non-current assets associated with these infrastructures	2,540	561	1,151	240	62	
Working capital associated with these infrastructures	1,729	2,169	712	118	118	
Non-current debt associated with these infrastructures	1,382	2,005	-	28	-	
Net assets associated with these infrastructures	2,887	725	1,863	330	180	
EBIT over net associated assets	14%	25%	21%	16%	25%	

(a) For an appropriate comparison of revenue from basic clearing, settlement and depository activities the following should be noted: (1) the revenue of Euroclear and Iberclear is chiefly from settlement and custody and hardly at all from clearing, though the latter is clearly present in the three other infrastructures. (2) Regarding the latter three it is worth noting that in the case of LCH.Clearnet, revenue from clearing services on the commodities and energy markets are included (€68m), whereas these markets are barely served by the other infrastructures.

Source: Compiled by author on the basis of annual reports and sundry financial information published by these markets.

Comparative revenue from trade and post-trade activity in cash securities in the top five European market groups – financial year 2006 FIGURE A.1



(1) LCH.Clearnet's revenue corresponds solely to its clearing activity in cash equity (€154m) and fixed income and repos (€24m), with a total of €178m from clearing. The distribution of this revenue and of basic services and other non-basic services to LSE and Euronext was calculated by taking the proportion of the number of transactions cleared in Euronext and LSE over the total cleared in shares.

(2) The distribution of revenue to LSE and Euronext was calculated on the basis of information appearing in Euroclear's annual accounts for 2006.

Source: Data from reports and websites of the entities concerned.

III Studies

Initial and continued listing conditions in regulated equity markets

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1 Introduction

The admission of securities to listing on regulated markets is subject to various requirements that overall aim to reduce informational asymmetry and as far as possible guarantee an ordered and efficient trading system. Before admission itself, information is usually required about the operating history and financial situation of the issuing companies. Some suitability conditions also tend to be set to guarantee that the securities are fully tradable and that minimum liquidity levels can be ensured. Once the securities are actually admitted to listing their issuers have to comply with transparency requirements and rules governing market abuse. There are also often other requirements to guarantee that a minimum trading liquidity is maintained. It is the job of the supervisory authorities and the market managers themselves to ensure that these obligations are complied with and to guarantee an ordered trading process. Among the instruments used when intervening are temporarily suspending listing of securities, and even discontinuing their listing.

Spanish legislation has over recent years incorporated Community directives regulating initial and continued listing conditions. This article focuses on equity securities. It describes the basic approach taken by Community legislation and compares Spanish legislation with that of other European countries. It also looks at the rules in American markets. A point that is highlighted is the division of powers between the public regulator and the markets, both in terms of setting the requirements for initial and continued listing and the decision-making capacity to temporarily suspend or discontinue listing. This question is of particular relevance today, for a number of reasons. The process of market demutualisation that has taken place over recent years could lead to potential conflicts of interest that cannot be ignored; but it could also condition the capacity of the markets to adapt speedily to the conditions of what is an increasingly competitive environment.

The article is set out as follows: Section 2 reviews regulations in the European Union; section 3 in Spain; and section 4 in other European countries, specifically the United Kingdom, France, Germany and Italy; section 5 describes some characteristics of American regulations; and section 6 offers some conclusions.

2 Community regulations

The Community regulations relating to initial and continued listing conditions are at present mainly to be found in five texts: the Consolidated Admissions and Reporting Directive (CARD), the Prospectus Directive, the Transparency Directive, the Market Abuse Directive and the Markets in Financial Instruments Directive (MiFID)¹.

CARD is the oldest of these Directives. Initially its scope covered both the conditions for admission, including those related to the obligation to produce a prospectus, and those for remaining listed, consisting above all in obligations on the part of the issuers to inform the market. However, after the approval of the Prospectus and Transparency Directives, its scope was substantially reduced. Today it mainly affects the minimum suitability requirements for securities and companies with regard to the process of admission and the competences of the Member States regarding admission, and temporary suspension and discontinuance of listing.

The requirements set out by CARD for admission are designed to ensure the following: (i) compliance with the law in the country in which the company has been set up; (ii) that the investors have sufficient information on the operating history and current financial situation of the company; (iii) that the securities are tradable and (iv) that there are minimum liquidity conditions given the size of the company and, above the distribution of shares among the public. The Directive does not demand any additional conditions to ensure liquidity after admission to listing, such as trading frequencies or minimum volumes.

To ensure that there is sufficient information about the operating history of the company requesting admission to listing, annual accounts have to be published or submitted for the past three years in accordance with the requirements of the applicable national legislation. However, the competent authorities may waive this requirement if they consider it desirable in the interests of the company or the investors, and if they are convinced that they have sufficient information to form a reasoned judgement about the securities.

With regard to the requirement relating to market capitalisation, CARD demands a minimum foreseeable market capitalisation of 1 million euros or, if this cannot be assessed, the same minimum amount in capital and reserves, including profit or loss, as determined by the accounts for the previous year. Nevertheless, Member States may permit admission to listing even when this condition is not fulfilled, provided that they consider that there is an adequate market for the shares admitted. Stricter minimum conditions may also be established, but only if other open, recognised, regulated markets operate regularly in the Member State concerned and the requirements for them are equal or less than those in the Directive. In addition, the minimum is not applicable if shares of the same class have already been admitted to listing.

With regard to the distribution of shares, there must be a sufficient number of shares distributed to the public of one or more Member States, not later than the time of admission. For these purposes, sufficient distribution is deemed to be when

¹ European Parliament and Council Directives 2001/34/EC, 2003/71/EC, 2004/104/EC, 2003/6/EC and 2004/39/EC respectively.

at least 25% of the subscribed capital represented by the class of shares concerned is in the hands of the public. A lower percentage may also be admitted if it is thought that the market can operate properly given the number of shares and their distribution among the public. When the shares are already listed in non-member countries, they may be admitted to listing if their distribution among the public in these countries is considered adequate.

CARD allows Member States to establish more rigorous or additional conditions for admission of securities to trading within the limitations provided by the Directive itself. This may be, for example, with regard to the criteria for distribution, or by introducing quantitative criteria for continued listing. In any event, no discrimination is permitted, so that the stricter and supplementary conditions must be applied to all issuers or categories of issuers, and they must have been published before the admission of the securities whose application is being considered. The principle of non-discrimination is also required when Member States exercise the power to establish exemptions in cases provided for by the Directive itself.

In accordance with CARD, the decisions relating to admission to listing correspond to the competent authority of the Member State in which the stock exchange to which admission is being sought is situated or operates. This authority also has competence with respect to temporary suspension and discontinuance. In these two cases, the regulator's decision is broadly based on its appreciation of any possible negative effects on the proper operation of the market, the protection of investors (suspension) or on the existence of special circumstances that do not permit the normal continuity of trading with the security (discontinuance).

The bulk of the information requirements for issuers are regulated by the Prospectus and Transparency Directives. The Prospectus Directive deals with the prospectus, which is the main piece of information that has to be submitted before admission; and the Transparency Directive with the regular information requirements when the security is already listed. The Market Abuse Directive is another relevant directive related to information. It establishes the obligation to communicate any significant event and sets out requirements that companies must comply with while they are listed to prevent the misuse of inside information and price manipulation.

The last of the five main relevant Directives affecting admission and continued listing is the MiFID. It is fairly recent, as its transposition to national law took place in 2007. MiFID is an extremely wide-ranging Directive referring to admission and continued listing in the more general context of rules applicable to what are called regulated markets. This context is defined by the Directive itself. The Directive requires the managers of these markets to implement clear and transparent rules on this matter and urges Member States to check that they have efficient mechanisms to ensure compliance with the requirements for admission and continued listing under Community law.

MiFID does not introduce additional quantitative or information requirements related to the issuer or securities other than those already included in the four

Directives mentioned above. In particular, Regulation 1287/2006², which develops some points of this Directive, assumes that compliance with the conditions included in CARD is sufficient to ensure that securities are fully tradable and that they may be traded in a fair, ordered and efficient way in a regulated market.

In line with CARD, but perhaps even more clearly, MiFID requires that the administrative authorities designated by the Member States should have the competence to intervene on the question of suspension or discontinuance of listing. Without prejudice to these competences, it also recognises that the markets may suspend or exclude financial instruments from trading if they do not comply with the rules of the regulated market, unless such a decision could cause serious harm to the interests of the investors or the ordered operation of the market.

The decisions relating to temporary suspension or exclusion from listing should be made public immediately. They should also always take into account the fact that the affected instrument may be traded on other regulated markets or European multilateral trading systems, with the competent authorities in the other Member States being informed in this case. The other Member States should in turn demand the suspension or discontinuance of the financial instrument concerned in the regulated markets or multilateral systems under their jurisdiction. However, they have a certain room for manoeuvre if they consider that such a decision could be seriously detrimental to investors or to the ordered operation of the market. The responsibility for informing the competent authorities in other Member States always lies with the authority that has jurisdiction over the market concerned, including when the decision has already been adopted by the manager of this market. The Directive urges Member States to require that the market managers publish their decisions on these questions and communicate them to the competent authority.

3 Spanish regulations

The Securities Market Law³ (LMV) includes in its current amendment all the Directives related to admission to listing, the conditions for remaining listed and the measures for suspension and discontinuance. This text is complemented by the implementing regulations passed up to now, basically the Royal Decrees 1310/2005 and 1362/2007⁴. The former establishes detailed regulations relating to the process of admission, laying down suitability conditions for securities and companies and regulating the prospectus. The second deals with the transparency requirements for issuers with listed securities.

Broadly, Spanish law on these matters is in line with the minimum requirements set out in the Directives. In particular, it barely considers the possibility of

² Regulation (EC) No. 1287/2006 of the European Commission.

³ Law 24/1998 of 28 July.

⁴ Royal Decrees 1310/2005 of 4 November, and 1362/2007 of 19 October.

imposing more restrictive conditions, as included in CARD. The markets themselves may impose additional conditions through their own rules, which they were given six months to pass under Royal Decree 1310/2005. Nevertheless, these rules have still not been drawn up. As a result, according to a temporary provision of this Royal Decree, Chapter V of the Stock Market Regulation of 1967⁵ still holds in those cases where it does not contradict the provisions of the new law.

In accordance with the Stock Market Law, admission of securities to trading in official secondary markets requires prior verification by the CNMV of compliance with the requirements of the law. In the specific case of securities that are tradable in securities markets, including shares, there will be a single verification valid for all of them. Admission to listing also demands agreement by the governing body of the market chosen by the issuer. Such agreement may be applied for once the securities are issued or when the corresponding entries are made in the books. It should be pointed out that apart from the CNMV, in Spain some autonomous regions may act as competent authorities for admission, suspension or discontinuance, as long as in the case of equity, the shares are exclusively traded on a market with its registered office in the region in question.

The article dealing with the admission requirements and procedure refers to developing the provisions and suggests that they should adopt a flexible approach, pointing to the possibility of making the requirements different depending on the securities and markets concerned. In accordance with MiFID, the regions have to establish clear and transparent rules with relation to admission to trading and they should have efficient mechanisms for checking compliance with the requirements for continued listing.

Article 32 bis of the Law includes a completely new provision for Spanish markets: it allows admission to listing without permission by the issuer of securities that are already listed on another official secondary market or a regulated market in another Member State. When there is no such permission, the information obligation does not lie with the issuer, but with the market, whose governing body should have available the means needed to obtain and distribute such information.

As indicated above, the detailed rules relating to admission and continued listing are set out in Royal Decree 1319/2005. This legal text mostly reproduces - at times literally - the criteria and requirements of CARD and the Prospectus Directive, hardly introducing any additional criteria to the minimum determined by the Directives. It is worth highlighting that the law distinguishes between the primary stock market and the secondary market in relation to the minimum capitalisation and distribution of shares among the public; but it does not do so with respect to the contents of the prospectus and the information requirements for securities already listed.

Spanish law adopts a more restrictive criterion than Community law in terms of the minimum amount of shares to be admitted, specifying a foreseeable market value of 6 million euros. However, this limit is not applied to secondary stock

⁵ Decree 1506/1967 of 30 June, passing into law the Commercial Markets Regulation.

markets. It is important to point out that Spanish law does not refer to the alternative method included in Community law. This alternative is based on calculating the capital plus reserves and including, if appropriate, the results of the previous year, when the foreseeable market value cannot be estimated. Nevertheless, in the case of a public share issue, the law stipulates that the price actually paid is taken into account.

Royal Decree 1310/2005 does also not go beyond the minimum formulated by the Directive with regard to the conditions for distributing shares. Thus it demands that this distribution should be sufficient prior to admission, and understands that in any case this requirement is met if a percentage equal or greater than 25% of the shares whose admission is requested is in the hands of the public in one or more Member States of the European Union or in non-member countries if such shares are listed in markets based in such countries. This requirement is not effective for admission to secondary stock markets, although the issuer may in this case designate an investment services firm or a credit institution that is a member of the market to help provide liquidity to the security while it is listed.

With regard to information on the issuer, Article 11 of the Royal Decree requires the issuer to certify its operating history and register its annual accounts and prospectus with the CNMV. They must then be approved by this supervisory body. The operating history is certified by presenting annual audited accounts, whether individual or consolidated as appropriate, covering as a minimum the previous three years. The CNMV may accept a period of less than three years for companies applying for admission to the New Market⁶, or as indicated in the Directive, when it considers that this is in the interests of the issuer or the investors, as long as it considers that the investors have sufficient information available to form an informed assessment. With regard to the prospectus, the requirements of the Royal Decree are in line with what is established by the Prospectus Directive, with only small differences.

Given the temporary nature of Chapter V of the Regulation on Commercial Markets, it is also worth bearing in mind some specific requirements contained in this text referring both to conditions prior to admission and the conditions for remaining listed. With regard to the conditions for admission, it is worth highlighting the minimum share capital requirement of 1,202,025 million euros, not including the direct or indirect holdings of shareholders who own 25% or more. Regarding share distribution, there must be a minimum of 100 shareholders with an individual holding of less than 25% of the share capital. In terms of operating history, the company must have obtained a profit in the previous two years, or in three non-consecutive years over a period of five years, sufficient to pay a dividend of at least 6% of the paid-up share capital after provision for taxes and legal reserves. However, it is specified that the CNMV may make exceptions to the latter condition in some cases, in particular when admission is sought to the New Market. There are also minimum trading frequency and volume requirements. The minimum frequency percentage should be not less than 25% of the total number of stock market sessions, and the

⁶ Special segment of the stock market for technologically innovative companies or those with a high growth potential.

minimum volume the nominal value admitted to listing for the same class of shares. Both these frequency and volume requirements and those referring to the minimum number of shareholders and the profit history of the company may be considered additional to those included in Community regulations.

On the question of discontinuing trading, the Stock Market Law recognises the capacity of the CNMV in this respect and grants it a broad discretionary margin. It explains that the decision to discontinue may be adopted when special circumstances occur that may disrupt normal trading in securities or when the measure is advisable in order to protect investors. The Stock Market Law also allows for an official secondary market to adopt the measure of suspension when a security no longer complies with the rules included in the market regulations. In this case, the decision should be communicated to the CNMV and made public. The CNMV should comply with the disclosure requirement to other Member States included in the MiFID. The managers of multilateral trading systems and internalisers should suspend trading in a security as soon as its suspension is made public.

The Stock Market Law envisages three possibilities of excluding from trading: action at its own initiative by the CNMV, action at its own initiative by the market itself and discontinuance at the request of the issuer. The first possibility is dependent on the CNMV noting non-compliance with the requirements for distribution, frequency or volume demanded for securities or with the transparency requirements for issuers. Discontinuance at the market's own initiative should be based on non-compliance with the market regulations and be dependent on the measure not representing any serious detriment to investors or to the ordered operation of the market. In any case, when the market adopts a decision of this type it should communicate it to the CNMV and make it public. Those agents who request the discontinuance of their shares from the market are obliged to promote a public takeover bid for all the shares affected by the discontinuance. The price and other requirements of the bid are regulated by the takeover regulations⁷. The CNMV may waive the requirement for the issuer to launch a takeover bid if it ensures the protection of the legitimate interests of the shareholders through another equivalent procedure.

4 Other European Union countries

Following the approval of the core Directives of the Financial Services Action Plan (basically the Prospectus, Transparency and Market Abuse Directives) there is a clear contrast in the EU between the United Kingdom and the main continental countries in terms of the regulation of the conditions for admission and continued listing. In the U.K., public regulation is detailed and the public supervisory agency plays a very active role, whereas in continental Europe the regulations tend to adapt to the Community minimum. As a result, the decision on whether or not to

⁷ Royal Decree 1066/2007 of 27 July.

introduce more demanding conditions is in fact in the hands of the markets. The difference not only seems motivated by different traditions, but also by different competitive strategies. Thus the United Kingdom tends to stress the quality of the public regulation as an intangible asset giving it an edge over other markets, while continental Europe opts for a greater flexibility to ensure that the regulated markets adapt to the competitive environment.

British regulations distinguish between “admission to trading” in a particular market and compliance with the requirements of the competent administrative authority, the United Kingdom Listing Authority (UKLA), for “admission to listing”. The securities complying with the latter requirements are included in what is known as the Official Listing, as long as they also obtain admission to a British market. Since 2000 the Financial Services Authority (FSA) acts as the UKLA, replacing the London Stock Exchange. The Official Listing is divided into two different listings with regard to shares: the Primary Listing, which is obligatory for British companies, although it is also open to foreign companies; and the Secondary Listing, only open to foreign companies. Whereas the Secondary Listing only requires compliance with the minimum requirements of the Directives, the Primary Listing demands additional “super-equivalent” requirements, so this is often presented as the primary brand of the Official Listing. The companies applying for admission in the Official Listing are required to have a registered entity as sponsor in the FSA to act as a contact with respect to compliance with the regulations.

The Official Listing requires a minimum initial capital of 700,000 pounds sterling, both for the Primary Listing and the Secondary. The share distribution in the hands of the public is in accordance with the Community minimum as set out in CARD, although when calculating this figure it does not include those in the hands of certain shareholders (mainly directors, directors' or employees' pension funds or schemes and significant shareholdings of more than 5%). Some of the super-equivalent requirements are quantitative or affect the company's activities, and the rest refer mainly to corporate governance. Among the former are the requirements that before admission (i) the company has been in profit for the past three years; (ii) 75% of the activities of the company have generated profits during this period, including the main activity or business; (iii) the main activity or business is an independent activity and is controlled by the company; and (iv) there is proof of sufficient working capital to cover company needs for at least the 12 months following publication of the prospectus⁸. The existence of sufficient distribution of shares, control by the company of most of its assets and the independence of the main business are conditions that must continue to be complied with while the company is listed.

The system of two listings has given rise to some criticisms in the United Kingdom because of its complexity. It has been pointed out that it could lead to confusion among investors, as they also have to differentiate between different types of trading infrastructure (regulated markets, multilateral trading systems and internalisers). These criticisms, together with considerations regarding the competitiveness of British markets, have led to the FSA setting up a consultation process on whether to reform the current system⁹. Among other questions, the

⁸ Under certain conditions financial institutions are not required to comply with this condition.

⁹ Financial Services Authority (2008): “A Review of the Structure of the Listing Regime”. Discussion Paper 08/1.

market participants have been asked whether the FSA should continue to set “super-equivalent” rules or whether it should leave this in the hands of the markets themselves, as happens in most European markets. At the same time, if the current dual listing system is to be continued, it asks whether it is a good idea to allow companies admission to the Secondary Listing for companies constituted in the U.K.

In terms of competences over suspension and discontinuance, the FSA reserves the right to act on its own initiative when faced by circumstances provided for in a general way in CARD. Unlike the Spanish legislation, the FSA regulations offer some examples, though not exhaustive, of situations in which this kind of decision may be taken. The markets are obliged to suspend or cancel trading definitively after a decision has been taken to this effect by the FSA. In addition, they may do so on their own initiative in order to improve market operation (suspension) or in the case of non-compliance with its rules (discontinuance).

The main continental European countries have opted to transfer Community legislation to their own regulations with very few changes. This approach means that national regulators mainly deal with checking information rules (the prospectus, regular public information, significant events, etc.), while the determination of special requirements for securities and companies to adapt to the commercial strategy of the markets is left in the hands of the markets themselves, always respecting the minimum Community standards. On the question of suspension and discontinuance, the continental model also tends to give the markets a greater role in these decisions.

The four countries where the NYSE Euronext has equity markets (France, Holland, Belgium and Portugal) have all in general terms taken on the model described in the above paragraph. French legislation is particularly clear in this respect, assigning the powers to decide on admission, temporary suspensions and discontinuance to the managers of the regulated markets¹⁰. The French regulator *Autorité des Marchés Financiers* (AMF) is granted the right to object to the decisions taken on admission or discontinuance and to be informed of the decisions on suspension. With regard to suspensions, the legislation states that the AMF may act on its own initiative in exceptional cases.

Within the scope of NYSE Euronext, the relevant national legislations do not include additional requirements to the minimum set out in the Directives, either with regard to admission or continued listing. There are no particularly restrictive requirements compared with Community minimums in the matter of market rules either. One aspect, however, is particularly different from the Spanish regulations: a lower limit is established for the number of shares in the hands of the public, which may not be less than 5% of the total, or represent a value of less than 5 million euros, calculated on the basis of the price of the public offering. If a lower percentage is detected while the security is listed this may give rise to immediate exclusion.

¹⁰Article L421-4 of the Monetary and Financial Code.

The German regulations follow a similar pattern. They simply include the Community minimums, so that the markets have a wide margin for establishing their own requirements. So far, the Frankfurt Stock Exchange has not introduced particularly restrictive or novel conditions. As requirements for continued listing, there are aspects related to communication between the market and companies, information on dividend payments and other corporate actions, as well as transparency requirements. The latter are not substantially different from those in the Transparency Directive, but they are varied according to the different trading segments. With regard to suspensions and exclusions, the German Market Law recognises the competence of regulated markets both in interventions at their own initiative and in interventions at the request of the issuer.

In the case of the Italian stock exchange, there are two requirements for admission in its own rules that are notable because of how they differ from Spanish regulations. The first is the demand for foreseeable market capitalisation of at least 40 million euros, an amount which is far higher than that in any other country mentioned so far. The second is the adoption of a more restrictive criterion with regard to the calculation of shares in the hands of the public, as it excludes holdings of more than 2%, although there may be exceptions depending on the nature of the investor. The Italian stock exchange has not so far incorporated any particularly notable requirements for continued listing. Rather, it focuses on conditions related to operation and on taking advantage of the room for manoeuvre given by the Transparency Directive to adapt the requirements of this type to the different market segments. In the matter of suspension discontinuance, the Italian stock market may act on its own initiative. A point worth highlighting is that the market rules give examples of situations in which a decision for suspension or discontinuance may be taken, as is the case in the British rules. Finally, it is also interesting to point out that the decisions for suspending or discontinuing securities issued by the market itself, which is a listed company, must be adopted exclusively by the public regulator (Consob).

5 The United States

Companies that want to be listed on American stock exchanges should comply with conditions for initial and continued listing, which are both quantitative and qualitative. Federal regulations impose qualitative conditions referring fundamentally to obligations with respect to information and registration. The markets lay down quantitative conditions, but may also impose supplementary requirements in addition to those in the federal regulations relating to transparency or corporate governance. The rules for admission and continued listing on the two main markets, the New York Stock Exchange and Nasdaq, are considerably more detailed and complex than European ones. Given that the outlines of each market are similar, this section will focus on the New York Stock Exchange (NYSE) as an example.

The NYSE demands prior quantitative requirements referring both to the financial situation of the company and the foreseeable liquidity of its shares. In some cases it offers alternatives depending on the origins of the company or the ways in which its admission to the stock exchange occurs. In all cases there is a clear distinction between national and foreign companies. Once the companies are admitted to listing, they also have to comply, on a continuous basis, with various quantitative requirements according to the options they have chosen at the time of admission.

Basically, the companies have two alternatives with regard to the initial requirements referring to the financial situation. The first consists of providing evidence of aggregate pre-tax profits for the previous three years (10 million dollars for national companies and 100 million for foreign companies), or minimum pre-tax profits for each of the two previous years (2 million dollars for national companies, which must also give proof of profits for each of the previous three years, and 25 million for foreign companies). The alternative is to submit themselves to a valuation of a combination of market value and earnings, or market value and cash flow. This test requires compliance with minimums for these variables. The initial liquidity requirement is based on compliance with minimum levels of the total number of shares (1.1 million for national companies and 2.5 million for foreign companies), the number of holders of minimum trading units¹¹ (2,200 for national companies and 5,000 for foreign companies) and a minimum foreseeable market value (100 million dollars for both national and foreign companies, except in the case of initial public offerings of national companies, where the minimum is 60 million).

In terms of the quantitative requirements for continued listing, the market establishes price, distribution and capital thresholds below which proceedings for temporary suspension or exclusion from listing may be initiated. In terms of price, the threshold is set at a closing price of 1 dollar for a consecutive period of 30 days. The distribution criterion has three alternative limits: a) fewer than 400 shareholders; b) fewer than 1,200 shareholders and an average monthly volume of less than 100,000 shares over the previous 12 months; and c) fewer than 600,000 shares in the hands of the public. Finally, the capital thresholds are determined according to the option chosen at admission with regard to the proof of the company's financial situation. Thus for example, if the initial requirement was based on proof of previous earnings, neither market capitalisation nor financial assets and liabilities may be less than 75 million dollars, as an average of the last 30 sessions, nor may the average capitalisation during this period be less than 25 million dollars.

In American markets, the public regulator has the power to intervene through decisions to suspend or exclude from trading, but only in special cases, usually related to recurrent non-compliance with obligations for issuers to inform or in cases of fraud. Thus it is the markets themselves that usually adopt these decisions.

¹¹ Usually 100 shares.

6 Conclusions

On the question of admission and continued listing, Spanish regulations are in line with the minimums established in the relevant Community Directives, with very few differences. This means that it is always the stock exchanges which decide on whether or not to introduce more restrictive or additional conditions through their own rules. Such rules have not yet been adopted, so that Chapter V of the Stock Market Regulation is still temporarily in force in those respects where it does not contradict the provisions of Royal Decree 1310/2005. The continued applicability of this text means that attention must be paid to it, because it includes prior requirements that are clearly different from those established in the Royal Decree, particularly on the question of distribution of shares and the company's operating history. In addition, unlike the Royal Decree, it includes quantitative requirements for continued listing relating to trading frequency and volume.

Generally, the Spanish regulations have adopted a similar approach to those of the main European Union countries, except for the United Kingdom. To sum up, public regulations reflect the minimums established by the relevant Directives, and as a result they give the markets a notable room for manoeuvre to establish additional or more restrictive additional rules if they so wish. The British approach is different. Public regulation in the U.K. is more detailed and establishes more restrictive criteria than those included in the Directives, at least in certain segments of the listing, because it is considered that these criteria constitute a competitive factor giving it the edge over other markets.

Socially responsible investment and corporate social responsibility in the financial markets: their application to management institutions in Spain

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1 Introduction

Socially responsible investment (SRI) is a very broad concept whose origins date back to the 1960s in the United States. It refers to a variety of investment practices that take into account not only financial aspects, but also social and environmental criteria.

Both in Spain and internationally, SRI is mainly practiced through collective investment schemes, mutual funds and pension funds. The management institutions of collective investment schemes (CIS) play a fundamental role in allowing and promoting the transmission of social demands on the part of investors who when given the choice value companies that issue securities which take into account ethical, social and environmental aspects, apart from purely financial ones.

Conventional analysts and fund managers increasingly take into account analysis of sustainability and the socially responsible preferences of investors. In addition, today there is greater social pressure for responsible behaviour by companies, mainly as a result of high-profile scandals affecting large corporations linked to lack of transparency and ethics. SRI aims to participate in restoring confidence in the system and the transparency of markets and to offer managers a tool for controlling risks and making better investment choices.

This article analyses SRI and corporate social responsibility (CSR) in the Spanish financial market from the perspective of the management entities. Ethical, social and environmental criteria are increasingly being incorporated into the valuation of management and economic risk. In addition, as some authors have maintained (Cox et al., 2004; Sethi, 2005; Moshe, 2006), the international development of the institutional market puts many investment decisions into the hands of the managers of these products. Thus these agents constitute a group of great importance when it comes to determining how and how much CSR is going to influence their investment decisions, and as a result by the stock market value of the companies.

The article approaches this question from a twin perspective. First, through a descriptive analysis, studying the degree of commitment and implementation of CSR and SRI in Spanish management institutions. Second, from an empirical perspective (based on a logistic regression model), aiming to identify the aspects that may influence or determine whether an institution decides to manage or market socially responsible investment funds (SRI funds), and those variables that may determine whether an institution decides to implement an explicit CSR policy.

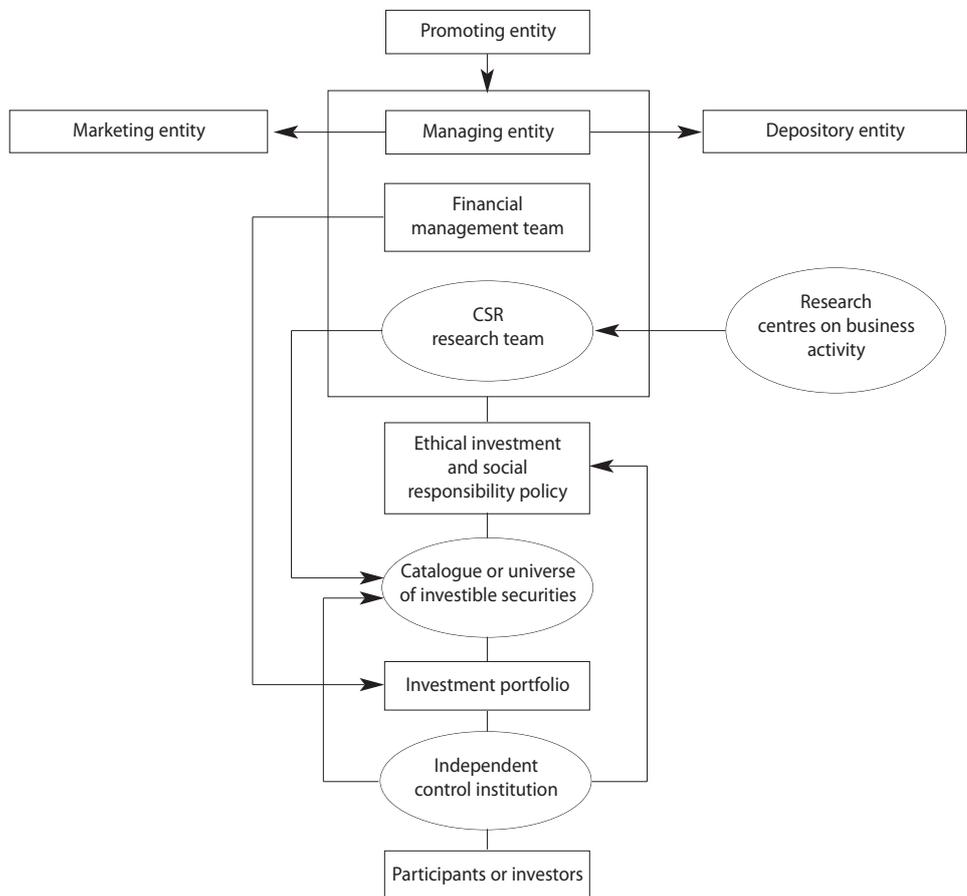
2 Outline of socially responsible investment in collective investment schemes

The United Kingdom Social Investment Forum (UKSIF) defines SRI as “investment allowing investors to combine financial objectives with their social values, linked to the spheres of social justice, economic development, peace and the environment.” The idea is thus use CSR criteria to act within the financial framework. This principle of CSR may be applied to a number of collective investment instruments, among them mutual funds and pension funds.

The elements making up a SRI fund are the same as those in a normal mutual fund, but with added mechanisms allowing a pre-selection of the catalogue of investible securities based on CSR criteria defined in the SRI policy of each fund (figure 1).

Elements making up a SRI fund

FIGURE 1



Source: Lozano and Albareda (2001).

The basis of any SRI fund is its policy of ethical or socially responsible investment (ethical strategy), combining the ethical, social and environmental criteria that define the SRI fund. The catalogue or universe of potential equity investments¹ is

¹ The methodology for choosing the companies is based on negative criteria that exclude certain investments combined with positive criteria. Its aim is to select those with the best behaviour in CSR terms.

then drawn up on the basis of this policy. This includes the universe of companies that may form part of the fund. A financial and sustainability analysis is then carried out by an ethical research team, and the companies that will form part of the fund are selected. The ethical research team may be independent of the management institution or part of it. In addition, SRI funds have an independent control institution (ethical commission) formed by persons of recognised prestige in the environmental and social aspects of the company's activity. This institution guarantees and verifies that the management of SRI funds is carried out according to the established criteria.

In short, SRI implies adding a fourth criterion to those of liquidity, profitability and risk - the three traditionally present when taking investment decisions. This fourth criterion involves analysing the social and environmental impact of the companies in which investors place their money. It is based on the idea that companies should play a role in society beyond obtaining profits and that they should contribute to sustainable development.

3 Socially responsible investment in international financial markets

In recent decades there has been a gradual move in international financial markets towards more responsible investment approaches, above all in collective investment schemes. As results of the growth and consolidation of the new social values of CSR the need to take into account the social and environmental consequences of the models of corporate economic growth has been placed on the international financial agenda.

The United States is the country where SRI is most developed and has most instruments available. According to data from the Social Investment Forum SIF (2006), at the end of 2005 nearly one out of every ten dollars of investment by CIS in the United States used some kind of screening criteria for the portfolio related to SRI. In addition, this is the product with the biggest growth in the 1995-2005 period in terms of volume of capital invested: from 12 billion dollars in 1995 to 179 billion dollars in 2005.

Despite being some way behind the United States in terms of the level of assets, the European SRI market is becoming increasingly mature. At the end of June 2005 the market represented 24,127 million euros in Europe, while a year before, the total managed capital was 19,034 million euros², an increase of 27%. In Europe the United Kingdom leads the way in SRI, with 19% of SRI funds and 33.15% of invested assets, corresponding to 7,999 million euros.

² Avanzi Research/SiRi Company, 2005.

3.1 Socially responsible investment in the Spanish financial market

In Spain, SRI emerged at the end of the 1990s. Although since then a number of different initiatives have arisen to manage and implement CSR and SRI strategies such as codes of conduct, good governance or ethical management systems, the situation has not yet become consolidated if we compare it to other European countries. Currently SRI is marginal in the Spanish financial market in terms of the percentage volume of capital in funds managed using these criteria. At the end of 2005, it represented only 0.49% of total assets invested in investment funds in Spain.

A number of factors may explain this situation, from lower share investment by small investors and the lack of demand by institutional investors (which has been crucial in other countries) to the lack of strong institutional support by financial groups that market funds, and including what is possibly insufficient promotion by the government.

There is also a lack of information about socially responsible behaviour by companies and the criteria by which SRI funds are constituted. The confusion relating to the profitability and risk of these funds has also blocked their development. In Spain a large number of investors are not aware that these funds are no different in terms of profitability or risk from other funds, as the investment decisions are taken with the obvious intention of offering an attractive return to shareholders. The difference lies in the selection of the investment portfolio according to criteria not only of economic profitability, but also of social and environmental values.

In this context, the role of management institutions is key in acting as a catalyst to the interest of investors and giving a much-needed boost to SRI in Spain.

4 Selection of the sample and database

The information required for the research is based on a survey sent to the entities managing CIS that make investment decisions based on an ethical, environmental or socially responsible strategy, as well as to the rest of the range of management entities. The aim has been to discover and quantify the different evaluations of CSR and SRI by both sets of investment portfolio managers, as well as their declared sensitivity to these concepts. The field work was carried out between May and September of 2004.

The sample studied included 47 management entities, representing 40.51% of the total population³. These 47 management entities represent 100% of the entities managing or marketing SRI in Spain (20 in all), and 25% of the entities that do not manage SRI funds (27 funds). The percentage of management entities in Spain either managing or marketing SRI funds in Spain is 17.24%. The specifications of our sample are shown in Table 1.

³ As of 30/04/04 the total population was 116 management institutions.

Technical specifications of the sample

TABLE 1

Universe	116 management entities (23/04/04)
Scope	Spain
Answers received	47 management entities
Sample error	±9.32%
Confidence level	95%
Sampling procedure	Submission of questionnaires to the whole universe
Field work	May – September 2004

Source: Prepared by autor.

5 Descriptive analysis of the data

5.1 The level of socially responsible investment and social corporate responsibility in fund management entities in Spain

First, an analysis was made of the relation between marketing and/or management of SRI funds and the entity's commitment to CSR. This was done by asking the managers about the existence of an explicit (in writing) CSR policy. Although only 31.9% of those surveyed had this tool, when this information is cross-checked with the management of SRI funds, the data confirm the close relation between the implementation of CSR in the entity's own management and the offer of SRI instruments: 73.3% of the entities with a CSR policy manage or market SRI funds, while 55% of entities that manage or market SRI funds have an explicit CSR policy (see table 2).

Management of SRI funds and implementation of a CSR policy

TABLE 2

		Does the entity have a CSR policy in writing?			
		No	Yes	Total	
Does it manage or market SRI funds in Spain or abroad?	No	Number	23	4	27 (57.4%)
		% of category	71.8%	26.6%	100%
	Yes	Number	9	11	20 (42.6%)
		% of category	28.1%	73.3%	100%
	Total	Number	32	15	47
		% of total	68.1%	31.9%	100%

Source: Prepared by autor.

Among the various reasons given to explain why an entity has decided to manage or market SRI funds the most important, at 80% of the total, is the fact that the entities that offer SRI funds do so because they consider that it is a product they should offer to their customers. Of all the reasons analysed it can be seen that none of the management entities markets or manages SRI funds because they consider that it is a more profitable product in the long term than other funds. From this it can be seen that management entities have some "doubts" about the profitability of SRI funds.

With regard to CSR policies, 84.2% of the entities say that they have promoted their adoption coherently and in line with the principles of the firm.

5.2 Profitability and risk of socially responsible investment

The survey analyses how managers perceive the attitude of investors to SRI in terms of profitability and risk. A total of 55% of the entities that manage or market SRI funds consider that investors reckon SRI funds provide a slightly lower or much lower return than traditional investment. Of the entities that do not manage SRI funds, 29.6% share this opinion. In addition, 22.2% of the entities that do not manage SRI funds consider that investors reckon that this kind of investment offers a very similar return to traditional investment, and this opinion is shared by 30% of the entities that manage SRI funds (see Table 3).

SRI fund profitability and traditional fund profitability

TABLE 3

		What do you believe that investors consider SRI returns to be compared with traditional investments?						
			Much lower return	Slightly lower return	Similar return	Slightly higher return	DK/NA	Total
Does your entity manage or market SRI funds in Spain or abroad?	No	Number	3	5	6	1	12	27
		% of category	11.1%	18.5%	22.2%	3.7%	44.4%	100% (57.4%)
	Yes	Number	1	10	6	0	3	20
		% of category	5.0%	50.0%	30.0%	0.0%	15.0%	100% (42.6%)
Total	Total	Number	4	15	12	1	15	47
		% of total	8.5%	31.9%	25.5%	2.1%	31.9%	100%

Source: Prepared by autor.

In the case of perception of risk, the result obtained is fairly uniform. Most entities managing SRI funds as well as those that do not manage such funds (45% and 37% respectively) believe that investors reckon SRI offers a similar risk to traditional investment.

5.3 Development of socially responsible investment

It is interesting to see whether there are significant differences in the perception of the development of SRI between those entities that manage or market SRI funds and those that do not manage such funds. Among those that do not manage SRI funds, 48.1% consider that in recent years interest in SRI has increased. However, this opinion is only shared by 30% of the entities that manage SRI funds, which mainly (50%) consider that the situation has not changed (Table 4).

Development of SRI

TABLE 4

		How has interest in SRI developed over recent years?					
			Not changed		Increased	DK/NA	Total
			Decreased	changed	Increased	DK/NA	Total
Does your entity manage or market SRI funds in Spain or abroad?	No	Number	3	6	13	5	27
		% of category	11.1%	22.2%	48.1%	18.5%	100% (57.4%)
	Yes	Number	2	10	6	2	20
		% of category	10.0%	50.0%	30.0%	10.0%	100% (42.6%)
Total	Total	Number	5	16	19	7	47
		% of total	10.6%	34.0%	40.4%	14.9%	100%

Source: Prepared by autor.

This difference in perception about the progress of SRI may be explained by the increase in news related to CSR, and by the way this news is reflected in the media, rather than the real development of these products.

6 Empirical analysis of the data

A number of pieces of research have been carried out to analyse socially responsible relations and attitudes using probabilistic models such as Tobit, Probit or the logistic regression model (Chevalier and Ellison, 1996; Tranter and White, 2001; Säve-Söderbergh, 2004). We have used these studies as a basis for offering three logistic regression models to analyse the relations between SRI and CSR and to identify the variables which may have the greatest influence on the management and marketing of SRI funds and the implementation of a CSR policy in Spanish managing entities. As a first step to setting up these models, a research hypothesis has been defined for a preliminary analysis of the relations between SRI and CSR in different spheres of action of the management entities.

6.1 Approach and checking the hypotheses

Hypotheses were established for the two lines of study: SRI and CSR. Checking the results obtained in the verification of the hypotheses, Table 5 indicates those that have been significant for the analysis of CSR.

Summary table Hypothesis testing

TABLE 5

Dependent Variable	Hypothesis	Independent variables	Relation?	Nature of relation
Management and marketing of SRI funds	H1	Implementation of a CSR policy	Yes	Positive
	H2	Transparency in management processes	No	---
	H3	Corporate management	Yes	Positive
	H4	Responsibility to stakeholders	No	---
	H5	Positive valuation of CSR policies (fundamental analysis)	Yes	Positive
	H6	Development of CSR policies	Yes	Positive
	H7	Benchmark with CSR criteria	Yes	Positive
	H8	Information on SRI funds	Yes	Positive
	H9	Best-advice systems	No	---
Implementation of a CSR policy	H10	Institutional investors	Yes	Positive
	H11	Management and marketing of SRI funds	Yes	Positive
	H12	Transparency in management processes	No	---
	H13	Final profitability of the firm	No	---
	H14	Corporate management	Yes	Positive
	H15	Responsibility to stakeholders	No	---
	H16	Positive valuation of CSR policies (fundamental analysis)	Yes	Positive
	H17	Development of CSR policies	Yes	Positive
	H18	Benchmark with CSR criteria	No	---
	H19	Information on SRI funds	No	---
	H20	Best-advice systems	Yes	Positive

Source: Prepared by autor.

From this preliminary analysis, we can conclude that there is a positive relation between SRI and CSR, i.e. between the management and marketing of SRI funds and the implementation of a CSR policy in the management entities.

6.2 Analysis of the relations and simple model of logistic regression for the management and marketing of socially responsible investment funds

This section analyses the relations between management and marketing of SRI funds and each of the independent variables that have resulted significant (according to the hypothesis) using a simple logistic regression model. The aim is to analyse how the presence or absence of certain factors influences the probability of managing or marketing SRI funds. Table 6 includes the results for what have been the most significant variables.

Interpretation of the results of the simple logistic regression model for the management and marketing of SRI funds TABLE 6

Area of analysis	Independent variables	Estimated probability of managing or marketing SRI funds	Odds	Interpretation of the odds
Does the entity have a CSR policy in writing?				
CSR policies in the entity	Yes	0.73	2.75	Is 2.75 times more likely to manage or market SRI funds than not to manage or market them.
	No	0.28	0.391	Is 2.55 times more likely not to manage or market SRI funds than to manage or market them.
What value do you give to the development of CSR policies when evaluating a company?				
Management of mutual funds	Not important	0.06	0.063	Is 15 times more likely not to manage or market SRI funds than to manage or market them.
	Important	0.43	0.758	Is 1.3 times more likely not to manage or market SRI funds than to manage or market them.
	Very important	0.90	9	Is 9 times more likely to manage or market SRI funds than not to manage or market them.
When investors ask for investment advice, do you inform them of the possibility of investing in SRI funds?				
Investors	Always	0.95	19	Is 19 times more likely to manage or market SRI funds than not to manage or market them.
	Frequently	0.80	4	Is 4 times more likely to manage or market SRI funds than not to manage or market them.
	Occasionally	0.46	0.835	Is 1.1 times more likely not to manage or market SRI funds than to manage or market them.
	Never	0.15	0.173	Is 5.7 times more likely not to manage or market SRI funds than to manage or market them.

Source: Prepared by autor.

One of the main results of Table 6 is that the management entities with a greater estimated chance of managing or marketing SRI funds are those that always inform of the possibility of managing or marketing SRI funds (with an estimated probability of 0.95 of managing or marketing SRI funds), as are those that consider it the development of CSR policies very important when they evaluate a company (they offer an estimated probability of 0.90 of managing or trading SRI funds). These data confirm that a positive evaluation of CSR of companies by managers provides a boost for SRI fund management.

However, those entities that have a CSR policy in writing offer an estimated probability of 0.73 of managing and marketing SRI funds. Although this is a high probability, it indicates that there are other factors which may exercise greater weight in the decision to manage or market SRI funds, as can be seen in the results analysed. Among these factors are the existence of information mechanisms for investors, the positive assessment of CSR policies developed by companies and the development of institutional investment.

6.3 Analysis of the relations and simple logistic regression model for the implementation of a policy of corporate social responsibility

This section presents the variables forming part of the simple logistic regression model of the implementation of a CSR policy in writing in the management entities. Table 7 includes the results of what have been the most significant variables in estimating the values for the dependent variable analysing the implementation of a CSR policy in writing.

The analysis shows that the management entities with the greatest probability of implementing an explicit CSR policy are those that consider it very important for companies analysed by the institution according to fundamental analysis to apply and incorporate CSR policies (with an estimated probability of 0.86 that the management entity has an explicit CSR policy). Closely related to this variable is the variable that measures how to assess the development of CSR policies when evaluating a company. It obtains an estimated probability for having an explicit CSR policy of 0.79 when this variable is considered very important.

These variables coincide with those obtained in the analysis of the management and marketing of SRI funds, as in both regression models the assessment of the CSR policies as very important in the analysis of the companies in which the fund invests influences positively both the probability of implementing a CSR policy in the management entities and in the management of SRI funds. This result confirms that the management institutions which "condition" some of their actions in CSR and SRI to the actions of the companies they evaluate present a greater chance of implementing CSR policies in writing, and of managing and marketing SRI funds. From this it can be deduced that the process of CSR and SRI involves numerous agents (companies, financial intermediaries and participants) and that its success and development in our country depends to a large extent on the communication and connection between the different agents, with the management institutions being an important point of connection between them all.

The interpretation of the results of the simple logistic regression model for the implementation of a CSR policy in writing

TABLE 7

Area of analysis	Independent variables	Estimated probability of implementing a CSR policy in writing	Odds	Interpretation of the Odds
Does the entity manage or market SRI funds in Spain or abroad?				
Management and marketing of SRI funds	Yes	0.55	1.2	It is 1.2 times more likely for a CSR policy to exist in writing than not to exist.
	No	0.15	0.173	It is 5.7 times more likely for a CSR policy not to exist in writing than to exist.
When you evaluate an action using fundamental analysis, what importance do you give to the application and incorporation of CSR policies by the company?				
Management of mutual funds	Not important	0.01	0.006	It is 166 times more likely for a CSR policy not to exist in writing than to exist.
	Not very important	0.03	0.035	It is 28 times more likely for a CSR policy not to exist in writing than to exist.
	Slightly important	0.16	0.195	It is 5.1 times more likely for a CSR policy not to exist in writing than to exist.
	Important	0.52	1.07	It is 1.07 times more likely for a CSR policy to exist in writing than not to exist.
	Very important	0.86	5.92	It is 5.2 times more likely for a CSR policy to exist in writing than not to exist.
What value do you give to the development of CSR policies when evaluating a company?				
Investors	Not important	0.05	0.047	It is 21 times more likely for a CSR policy not to exist in writing than to exist.
	Important	0.30	0.421	It is 2.3 times more likely for a CSR policy not to exist in writing than to exist.
	Very important	0.79	3.7	It is 3.7 times more likely for a CSR policy to exist in writing than not to exist.
Do you ever use the best-advice system to help choose SRI funds?				
Investors	Yes	0.62	1.6	It is 1.6 times more likely for a CSR policy to exist in writing than not to exist.
	No	0.24	0.307	It is 3.2 times more likely for a CSR policy not to exist in writing than to exist.

Source: Prepared by autor.

6.4 Analysis of the relations and multiple model of logistic regression for the management and marketing of socially responsible investment funds

This section undertakes an analysis of the management and marketing of SRI funds through a multiple logistic regression analysis. It is worth pointing out that the choice of variables is based on the simple regression analysis of each of the variables individually. The interpretation of the results is shown in Table 8.

Interpretation of the results of the multiple logistic regression model of the management and marketing of SRI funds

TABLE 8

Area of analysis	Independent variables		Estimated probability of managing or marketing SRI funds		Interpretation of the odds
	Does the entity have a CSR policy in writing?	Do institutional investors ask for SRI funds?	funds	Odds	
CSR policies in the entity and the investors	Yes	Yes	0.91	10	Is 10 times more likely to manage or market SRI funds than not to manage or market these products when there is a CSR policy in writing and when the demand for SRI funds is from institutional investors.
	Yes	No	0.56	1.2	Is 1.2 times more likely to manage or market SRI funds than not to manage or market these products when there is a CSR policy in writing and when the demand for SRI funds is not from institutional investors.
	No	Yes	0.58	1.3	Is 1.3 times more likely to manage or market SRI funds than not to manage or market these products when there is no CSR policy in writing and when the demand for SRI funds is from institutional investors.
	No	No	0.14	0.17	Is 5.8 times more likely not to manage or market SRI funds than to manage or market these products when there is no CSR policy in writing and when the demand for SRI funds is not from institutional investors.

Source: Prepared by autor.

These results once more confirm the starting theory of the analysis: that there is a positive relation between SRI and CSR. It confirms that the demand for SRI funds by institutional investors is a key factor directly influencing the management and marketing of SRI funds. Thus those entities that have an explicit CSR policy and also have institutional investors among their clients who demand SRI funds present a probability of managing or marketing SRI funds of 0.91, while for those entities that have a defined CSR policy but do not have institutional investors among their socially responsible investors, the probability is 0.56.

Another important piece of data revealed by the research is that the estimated probability of managing SRI funds is greater for those entities where the demand for funds among investors comes from institutional investors (a probability of 0.58), than for those institutions that have an explicit CSR policy (a probability of 0.56).

7 Conclusions

Management companies decide on the portfolios of the funds they manage according to their expected profitability. In the case of managing SRI funds the choice of securities to include in the portfolio takes into account not only the profitability but also socially responsible criteria on which the fund is based; in other words, a positive valuation is given if it can be assimilated into a previously established ethical strategy.

The aim of this procedure is to construct a portfolio suitable for shareholders in the fund who want to obtain financial benefits and also a social benefit by supporting companies that operate in a socially responsible way. In this process, the role carried out by management entities is very important. They act as a nexus between the market and the investors, and thus their actions are key for the development of SRI.

One of the most important pieces of evidence from the descriptive analysis carried out is that most entities that manage SRI funds as well as those that do not consider that investors believe this kind of fund offers a similar or worse return and a similar risk to that of traditional investments. The most notable difference between the managers which deal in these kinds of funds and those that do not is the perception of how interest in SRI has developed in our country. The entities that manage SRI funds consider that interest in SRI has not changed, whereas those that do not manage SRI consider that interest in SRI has increased. These results suggest there should be more information about the operation and methodology of these products, particularly in questions related to risk and return.

In addition, the application of a logistic regression model confirms the existence of a positive relation between SRI and CSR. It can be seen that a key factor for the development of SRI and CSR in our country is the evaluation that the management entities make of the CSR policies applied by companies, given that those which consider the application of these CSR policies very important are more likely to manage and market SRI funds, as well as implementing an explicit CSR policy.

In conclusion, if we want to increase and consolidate SRI in our country, CSR criteria should be adopted in corporate management systems, without disregarding the aim of creating shareholder value. The dissemination of these kinds of strategies will stimulate the management entities of mutual funds to decide to adopt them in turn, and thus offer SRI funds.

In other words there has to be a clear committed opinion on the part of all the economic agents that CSR generates value in the company and is a component to be considered when selecting investments. This makes it essential to increase information about SRI, and particularly to highlight the fact that these criteria are compatible with a financial profitability similar to that of traditional mutual funds.

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IV Regulatory Novelties

The Initiative against Market Abuse (“ICAM”) and liquidity contracts

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1 Introduction

The term “market abuse” (in Spanish *abuso de mercado* translated from the English) covers three types of unlawful conduct: (i) the use of inside information to obtain profits in the securities market, (ii) the manipulation of listings and transactions, generating misleading signals to the market or artificial price movements, and (iii) the dissemination of misleading information. The first is usually colloquially known as “insider trading” and the latter two as “market manipulation”.

Although it may seem surprising, the pursuit and penalising of conduct constituting market abuse has not been a constant factor in the history of securities markets and its development is a relatively recent phenomenon.

In 1990 less than 10 countries had rules defining conduct by operating in the market with inside information (insider trading) as unlawful. A decade later all developed markets had incorporated some type of prohibition and penalty in respect of this conduct in their regulations. Nevertheless for decades there has been a debate in the academic community (particularly in the US) which questioned the extent to which the use of inside information was prejudicial or otherwise to issuer companies or to the market as a whole.

In defence of the use of inside information some considered that its utilisation by executives of companies made a positive contribution to instantaneous dissemination of information (by means of the transactions which they ordered) to a market which they described as efficient (which instantly takes account of all available information). Others considered that the possibility of using internal information of a company bolstered business innovation and aligned its interests with those of shareholders. Furthermore, on occasions the use of inside information was considered by non-primary insiders (other than executives) as a method which would tend to stimulate market research and “intelligence”, making it more efficient.

On the other hand, critics argued that information is not disseminated instantaneously (or, which is the same thing, the market does not always reflect the influence on prices of transactions by a few insiders), but that it benefited the insiders and prejudiced other investors. Furthermore, the idea that two levels of information exist (that of insiders and that of other investors) took liquidity, confidence and integrity away from the market since many of those who do not have access to inside information decide not to operate in an uncertain and opaque environment. These arguments are even more powerful if we focus on the weakest link in the market: potential investors, with less access to information.

There are few empirical studies which throw light on the degree of influence of market abuse in developed countries. The most interesting are probably those which focus on analysing the degree of market anticipation of major news which

inevitably affects the price of a security, such as launching a takeover bid. According to some authors, it can be seen that between 20% (Spain) and 35%-40% (United Kingdom and the United States of America) of takeover bids launched are anticipated by the market in stock exchange sessions before their official announcement. Although it can far from be concluded that all anticipation is a result of the use of inside information (and even less that it originates directly from executives) it seems that the phenomenon has not, despite existing regulation, been eliminated from principal securities markets and therefore constitutes a real problem.

This article reviews various recent initiatives to prevent and combat market abuse. In particular, it reviews the Initiative Against Market Abuse (*Iniciativa contra el Abuso de Mercado* – “ICAM”) and within this the regulation of liquidity contracts recently approved by the CNMV. The article is structured as follows: the second section reviews the basic legislation on market abuse, the third describes the ICAM and its components, the fourth describes the rules on Liquidity Contracts and the fifth summarises conclusions.

2 Legislation on market abuse

Independently of the academic debate, the fact is that legislators and supervisors of principal markets have for years taken a position of not tolerating such conduct in the firm conviction that it has a highly adverse effect on the integrity of markets. Community legislation in the field of market abuse was thus framed by European Parliament and Council Directive 2003/6/EC, of 28 January 2003, for the first time establishing a complete unitary regime covering market abuse at European level, since as well as regulating the use of inside information it covers market manipulation. This Directive was developed and completed by a further three Directives and one Regulation:

- Directive 2003/124/EC, of 22 December, on definition of inside information and market manipulation.
- Directive 2003/125/EC, of 22 December, on fair presentation of investment recommendations and disclosure of conflicts of interest.
- Directive 2004/72/EC, of 29 April, on accepted market practices, definition of inside information in relation to derivatives on commodities, the drawing up of lists of insiders, notification of managers’ transactions notification of suspicious transactions.
- Commission Regulation 2273/2003, of 22 December, on exemptions for buy-back programmes and stabilisation of financial instruments.

This Community legislation has been integrated into the Spanish legal system by transposition, mainly through Acts 44/2002, 12/2006 and 6/2007 which reform the

Securities Market Act, in particular Sections 81 to 83 quater, of Royal Decree 1333/2005, of 11 November, on market abuse.

The basic framework seeks to achieve the following objectives:

- Prohibition on manipulative techniques in respect of quoted prices and volumes and dissemination of false or misleading information.
- Diligence and the implementation of organisational measures by issuers when handling sensitive business information.
- Measures for safeguarding and prohibiting use of inside information.
- Obligations of issuers to notify relevant information.
- Organisational measures by intermediaries to prevent the use of inside information.
- Obligation to give notice of suspicious transactions.

These confirm positions which hold that combating market abuse is in no way the exclusive task of supervisory bodies. On the contrary, each and every one of the participants in the market, beginning with issuers and taking in intermediaries and ending up with information disseminators have a role (and obligations to comply with) regarding the prevention of market abuse.

3 The Initiative Against Market Abuse

Awareness that market abuse constitutes a serious handicap to the competitiveness and integrity of any capital market for the multiple agents involved, combined with entry into force of Community legislation in this field, has led to Community countries proposing, debating and promulgating complementary measures which help to eradicate these practices which are so harmful to the markets in which they appear.

In this context, on 29 January 2007 the CNMV submitted a series of preventative measures against market abuse for public consultation, which took the form of an Initiative Against Market Abuse (“ICAM”).

At the end of the public consultation period and in the light of the comments received, the ICAM was restricted to a list of measures, some of which are already in operation, such as:

- **Liquidity contracts as accepted market practice:** This is the result of the work carried out by a group of market experts under the auspices of the CNMV, which studied the desirability of accepting operations carried out

pursuant to a liquidity contract as market practice in Spain, provided that certain conditions are respected, regulated by Circular 3/2007 whose contents are detailed later.

- **CNMV criteria on operations for the placing or purchase of large blocks of shares:** Establishment of these criteria was motivated by frequent questions from the sector to the CNMV on certain aspects of their implementation. Debated within an expert working party, as with the previous measure these criteria, approved by the CNMV Board on 19 December 2007, have the objective of minimising the impact on the market of block trades and insofar as possible preventing the use of inside information.

Other measures in the process of preparation are:

- **Legislative development of obligations to notify relevant information:** The current wording of Section 82 of the Securities Market Act, 24/1988 of 28 July, establishes an obligation for issuers of securities to immediately publicise and disseminate to the market all relevant information and provides that notification to the CNMV must take place simultaneously with dissemination by any other means.

In order to contribute to identifying relevant information, in 2007 the CNMV created a working party comprising experts from the market, whose conclusions are being used in legislative development in the field of relevant information, in process of preparation, in which it is also planned to provide for the designation of at least one authorised interlocutor for each issuer with the CNMV.

- **Procedure for notifying suspicious transactions:** In the first quarter of 2008 the CNMV convened a group of market experts in the field to work on preparation of a procedure facilitating compliance with the duty to notify suspicious transactions as provided by Section 83 quater of the Securities Market Act.

The preparation is planned at a later stage of:

- **A protocol for CNMV action in the event of indications of market abuse** regulating the action of the CNMV when it perceives anomalies in trading or is aware of relevant rumours or news which could be an indication of potential market abuse. The intention of this protocol is to limit as far as possible the cases in which it is necessary to suspend a security.
- **A guide for action in respect of communicating information to third parties** which serves as support for professionals in the Spanish market faced with the doubts which may arise regarding the public or non-public nature of the information which they may provide to third parties during trading or preparation of financial or corporate operations. The intention is thereby to facilitate the said operations without infringing Section 81.2.b of the Securities Market Act on prohibition on all those with inside

information from communicating it to third parties except in the normal exercise of their work, profession or position.

4 Liquidity contracts as accepted market practice

On 12 January last, CNMV Circular 3/2007, of 19 December, was published in the Official State Gazette on liquidity contracts and the effects of their acceptance as market practice.

As indicated in the preamble, a lack of liquidity in equity securities constitutes a drawback to adequate development and functioning of the market, and can lead to prejudice to investors and intermediaries. In line with the provisions of other European Union securities' supervisors, the use of certain mechanisms which assist in increasing liquidity of a security may be appropriate, if they act in a manner which minimises the issue of misleading signals and do not hamper orderly functioning of the market.

These mechanisms include contracts for provision of liquidity by a financial intermediary who, acting on commission from the issuer, carries out purchase and sale transactions in the official secondary market in the shares of the said issuer. These are the so-called liquidity contracts.

This activity could constitute market manipulation since the transactions carried out by a financial intermediary on behalf of the issuer could generate signals which induce confusion amongst market participants insofar as they are not motivated by buyer and seller interests based on investment policies, but by an attempt by the issuer to increase the counterparties which investors can find when entering and undoing their positions. These potentially misleading signals, which may induce confusion, would affect perceptions of actual supply and demand for securities at any time and also, if transactions take place incorrectly, their prices. The distortion in prices and volumes could be significantly aggravated if at the same time the issuer acts in relation to its own shares, buying or selling them, without the market being aware of these circumstances beforehand.

As a result of the foregoing, it was considered that liquidity contract activities should, subject to various conditions set out below, be recognised as "accepted market practice". This term, directly obtained from European legislation, is used for practices which, even though they can fall within the definition of market abuse, are expressly accepted by securities market supervisors in each country, such that a person who follows them for legitimate purposes cannot be penalised for breach of market abuse legislation.

The CNMV thus defines a secure manner, insofar as it eliminates the risk of penalty, of increasing the liquidity of shares with low capitalisation and free-float. In symmetrical manner, liquidity contracts which do not fulfil the requirements of the Circular are exposed to penalty if their distorting effect is verified if they generate volume or price effects which could send out misleading signals to the market

4.1 Requirements of the Contract

In order for operations in the framework of a liquidity contract to be considered accepted practice they must fulfil the following requirements:

a. Sole purpose

The contract must have the sole purpose of a pure provision of liquidity, excluding those others linked to the price of the share or its volatility. It was thus a question of not accepting a practice tending to moderate or accentuate price trends or to reduce the volatility of a share, by considering that this purpose borders on the concept of market abuse without having any positive effect on the liquidity of the security, and therefore for investors.

b. Independence of the financial intermediary

The independence of action of the financial intermediary as liquidity provider in respect of the issuer must be set out in the contract and the former may not receive any instructions aimed at guiding its intervention in relation to sale and purchase trades in the issuer's shares.

Consequently, the financial intermediary must have an internal organisational structure which guarantees the independence of employees responsible for taking decisions on trades covered by the contract.

Furthermore, the conditions laid down in the contract regarding remuneration of the financial intermediary must not undermine the principle of its independence or encourage it to artificially influence quoted price and/or volume. In no event will remuneration be considered acceptable which is based on the number of trades carried out.

This aspect is extremely important and in itself marks the difference between the traditional operating procedure of trading in own shares and the liquidity contract. In the former, the intermediary follows the instructions of the issuer at all times and operates at the times and in the amounts and at the prices which the issuer determines. In the liquidity contract, on the other hand, real independence is sought of the intermediary, which takes its own decisions regarding the manner, time and amount of its activity in providing liquidity. The result is that the obvious conflicts of interests which are generated by the trading in own share procedure are reduced to a minimum in the case of liquidity contracts.

c. Action in official markets and identification of exclusive intermediary

This accepted practice is limited to operations carried out in official secondary markets with electronic trading mechanisms, although the CNMV does not rule out in the future that if the alternative trading mechanisms patently enhance liquidity it may be extended to them. What is vital is public identification of the intermediary before the commencement of operations, since this enables the market, at least partially, to locate the source of orders originated by the contract. This activity is obviously only conceivable if it is restricted to a single intermediary

and there may not be simultaneous or successive action through more than one intermediary since this would generate clearly confusing signals to the market.

d. Proportionality and continuity of activity

The resources devoted by the issuer, shares and cash, to the activities regulated by the liquidity contract must maintain a balance in themselves and at the same time be proportional to the objective established in it. In line with this, the financial intermediary must act in a manner which ensures the continuity of the liquidity contract and can decide not to operate in cases in which continuity is compromised in provision of the service. To this end it must procure that a provision of securities and cash is maintained which enables it to offer liquidity in a regular manner and therefore it must avoid “over-intervention” at times of excessive volatility if this may give rise to the resources devoted to the contract becoming exhausted.

4.2 Information requirements

The Circular further provides for information obligations which particularly include those aimed at the market being aware of the existence and implementation of the contract and thereby calibrate actual supply and demand which exists in respect of each security.

a. Public information

As well as the information obligations relating to portfolio of own shares which listed companies are subject to, all issuers which enter into a liquidity contract must inform the market of the following:

- Before it comes into effect, of the identity of the financial intermediary with which the contract is entered into, detailing the security and market in which transactions will be carried out, its term and the resources, shares and cash, allocated to these transactions.
- Quarterly, or at the end of the contract, details of the transactions carried out in the period and the balances on accounts associated with it.
- Termination of the liquidity contract when this takes place.
- Any change in the information notified to the market in relation to the liquidity contract.

b. Information to be sent to the CNMV

An issuer who enters into a liquidity contract must, as well as complying with the information obligations previously described, send a copy of the contract to the CNMV.

4.3 Operating conditions

Transactions carried out by the financial intermediary in its activity of providing liquidity must take certain aspects into account which in particular include the following:

- Accepted market practice limits transactions to those carried out in official Spanish secondary markets through the order market in accordance with trading rules and within their normal trading times.
- The financial intermediary must never exercise a dominant position in trading in shares of the issuer, and in no event exceed 25% of daily average orders of the official secondary market in the previous 30 sessions.
- The financial intermediary must prevent its action having a decisive influence on the evolution of prices during periods of auction, and particularly at closing.
- Transactions pursuant to a liquidity contract must in any event never artificially give rise to deviations in list price in relation to market trend, obstruct its normal functioning or induce error amongst third parties.

To this end, the Circular provides that purchase orders must be made at a price which does not exceed the higher of that of the most recent transaction carried out in the market by independent parties and the highest contained in a purchase order in the order book, and that sale orders must be made at a price not less than the lesser of the most recent transaction carried out in the market by independent parties and the lowest contained in a sale order in the order book.

This series of measures is intended insofar as possible to limit the potential distorting effect of orders made by the intermediary. In particular they concentrate on price elements since of the two types of misleading signals which a procedure of this type can generate, those relating to price are generally more pernicious than those relating to volume. By means of these measures, although it is not possible to completely eliminate the possible distortion which a contract of this type can generate in the market, it is aimed to reduce it to a tolerable level which is clearly compensated by the positive effects on liquidity which it contributes.

4.4 Restrictions

One of the aspects of regulation of liquidity contracts which generates most interest tends to be the fact that they are considered an exclusive means (incompatible with others) for an issuer to act in the secondary market in its own shares. Thus, in order for transactions carried out in the context of a liquidity contract to be classified as “accepted market practice” it is a necessary condition that the issuer does not directly or indirectly engage in any additional transaction in its own shares whilst it remains in force.

Furthermore, the operation of a liquidity contract must be suspended in the following events:

- On public offerings for sale and subscription of shares of the issuer, during the 30 calendar days after the date that they are first quoted.
- From announcement to the market of a public bid for takeover of the issuer until its settlement.
- While programmes are implemented for the repurchase of shares of the issuer, unless the latter complies with the provisions of the aforesaid Regulation (EC) 2273/2003.

The reason for not allowing liquidity contracts to be combined with other forms of action on own shares of the issuer is simple and forceful: the multiplicity of simultaneous actions in turn multiplies the risk of manipulation to intolerable levels and therefore not capable of being considered accepted market practice. If an issuer acts for own account through its portfolio of own shares, and at the same time commissions an intermediary to provide liquidity and begin a buy-back programme all at the same time, the volumes (and probably prices) seen in the market will differ considerably from free interaction between buyers and sellers. The Circular thus lays down a clear border: issuers who wish to promote the liquidity of their securities in a secure manner with certainty from the outset that they do so in accordance with the law must abstain from simultaneous transactions of another type in their own shares.

5 Conclusions

Circular 3/2007 represents a further element in construction of a framework which channels market practices towards areas fully compatible with European regulation without thereby obstructing the development of markets. In construction of this framework, the CNMV is firmly determined to lead initiatives which combat and eradicate market abuse in Spain and for years has been very actively committed in the European information and cooperation exchange group between supervisors, known as CESR-Pol. Nevertheless, without the cooperation of all agents involved in financial markets the results will be incomplete.

No country in our environment tackles the fight against market abuse solely by the work of supervisors, since it is generally understood that their role is necessary but not sufficient. Collaboration in the field of identifying good practices, notification of suspicious transactions by secondary markets and by intermediaries and organisational measures which minimise leakage of information, to give a few examples, are areas where a combination of efforts between the financial sector and the market supervisor is vital.

A special mention must be given to financial institutions as a result of the central role which they play, since they constitute a very high percentage of investment

service provision and maintain a link between investors and issuers which makes their participation essential in the collective effort aimed at increasing the standards of quality of our market. When all is said and done the integrity and prestige of the Spanish capital market is a public asset which must be protected and a very valuable asset to institutional participants, which translates into tangible variables such as depth, liquidity and cost of capital. The different ICAM measures are aimed at protecting this public asset and facilitating compliance with obligations by all market participants.

With respect to liquidity contracts, the basic idea underlying the declaration of accepted market practice is to stimulate and promote issuers who wish to strengthen the liquidity of their securities by doing so this way, which is the only one which offers complete legal certainty, instead of other mechanisms such as discretionary management of own shares which, although legal, does not have any protection in relation to its potential effect of market manipulation.

In scarcely two months since its publication a half dozen listed companies have already joined into this practice and, although it is too soon to extract conclusions on its efficacy, the CNMV maintains permanent contact with the sector in order to detect those aspects capable of improvement which, after a prudent passage of time, will enable the regulation of this practice to be improved, adapting it to observed reality.

Comments on Circular 5/2007 on relevant events of collective investment undertakings

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1 Introduction

Listed companies are under an obligation publicly to provide transparent, reliable, complete and up to date information with enables investors to form a grounded judgment of the situation of the company, which contributes to proper functioning and transparency of the securities market. There are two types of information which must be provided to investors: firstly the periodic information, generally linked to aspects of ordinary activities and financial data on the company, which is regularly made public by all issuers; and secondly information on relevant events which occur at times which do not coincide with the periodic information.

This principle is further applicable to other agents who participate in the market. In the case of collective investment undertakings (*instituciones de inversión colectiva* – “CIUs”) information on relevant events which may influence a reasonable investor in acquiring or disposing of shares or holdings in CIUs and which can therefore markedly influence their liquidating value acquires particular importance. This information is particularly sensitive if we take into account that the most common way in which Spanish small investors gain access to financial markets is through collective investment. This is so much so that the number of investors with positions in CIUs at the end of 2007 was over eight and a half million.

The growth which has taken place in the number of CIUs in recent years has given rise to an increase in the number of relevant events notified by these undertakings for dissemination. Figure 1 shows the evolution in the number of notifications sent by CIUs for dissemination through the CNMV. Between 2003 and 2007 they increased from 2,938 published in 2003 to 5,276 in 2007, a 79.58% increase. Faced with growth on this scale, the CNMV has redoubled its efforts to speed up as far as possible the process of making the relevant information on the CIU available to the public.

Relevant events of CIUs published in the last 5 years

FIGURE 1



Source: CNMV.

In this article the actions taken by the CNMV in the field of communicating relevant investments of CIUs are examined, in particular the contents of recently published CNMV Circular 5/2007 which should contribute to improving the transparency of collective investment vehicles and thereby facilitate decisions by participants. The article is structured as follows: the second section will deal with the measures taken by the CNMV to speed up the publication of relevant events, the third section will examine the objectives of the Circular on relevant events of CIUs, section four deals with the types of relevant events of collective investment vehicles, and section five reviews the publicity given by the CNMV to notifications of relevant events. Finally, section six summarises the principal conclusions reached in the article.

2 Measures for speeding up publicity on relevant events

The Collective Investment Undertakings Act, 35/2003 of 4 November (the CIU Act) in Section 19 on relevant events¹ makes general reference to the Securities Market Act (*Ley del Mercado de Valores*). The amendment of the latter by Act 6/2007, of 12 April, introduced an important novelty affecting both securities issuers and CIUs when providing that dissemination to the market of relevant events shall take place simultaneously with notification to the CNMV. This has led to a substantial speeding up of the process of making relevant events available to the public since they do not need to be sent to the CNMV before they are made available to the public as occurred previously.

To supplement the novelty, since 13 August 2007 it has been possible for CIUs to send their notifications of relevant events by electronic means through the CIFRADO system. This system enables the notification sent to be disseminated to the public immediately through the CNMV website, without prejudice to a review of its contents after publication. Investors are thus guaranteed access to information which could affect the liquidating value of CIUs in a more rapid manner.

Furthermore, since 19 October 2007 the CNMV has been automatically publishing those relevant events which are associated with the prior administrative authorisation or registration process and which are therefore considered to be notified *ex officio*. After processing the corresponding matter notifications of relevant events are automatically generated and immediately published on the CNMV website. By the middle of February more than 850 relevant events were published by this system without the need for undertakings to send any additional documentation. The section on types of relevant events details those which are being published *ex officio*.

¹ Section 19 of the CIU Act provides that “Relevant events connected with the undertaking shall be made public in the manner laid down by regulations in accordance with the provisions of the Securities Market Act, with the CNMV being informed thereof and they shall be included in successive reports for the information of shareholders and participants”.

Finally, publication of the Circular on relevant events of CIUs is the culmination of this process of speeding up provision to investors of all information of interest relating to their investment vehicles.

3 Objectives of the Circular on relevant events of CIUs

The procedure which existed previously for sending relevant information enabled it to be sent by fax, post or on paper with the original document in any event having to pass through the General Registry in order to assign it an incoming number and date in the register. This procedure gave rise to considerable delay in making this information available to investors and therefore it became necessary to rationalise the manner of notifying relevant events of CIUs. This led to the decision by the CNMV to prepare a Circular enabling access by investors to relevant information on CIUs to be speeded up.

Consequently, and pursuant to the powers expressly granted to it by Sections 15² of the CIU Act and 28.2³ of the Collective Investment Undertakings Regulations promulgated by Royal Decree 1309 of 4 November 2005 (the CIU Regulations), the CNMV published the Circular on relevant events of CIUs which came into force on 6 February 2008.

The Circular has several objectives:

- To speed up the provision to investors of relevant information on CIUs by imposing electronic notification.

As previously indicated, the IT application for undertakings to send relevant events relating to CIUs has been available since 13 August. The Circular provides, however, that it is mandatory to send the notification by this system since there were very few undertakings which had been making use of it.

The benefit to investors is clear, since this system enables them to have the relevant information with maximum speed by not making notifications on paper. For undertakings under an obligation to notify there are also substantial benefits since the CNMV has made an easily used system available to them which enables notifications to be sent 24 hours a day, seven days a week, and constitutes a substantial cost saving.

² Section 15 of the CIU Act on foreign CIUs marketed in Spain provides that *"The CIU must take the measures which the CNMV considers necessary to facilitate payments to shareholders and participants, acquisition by the CIU of its shares or reimbursement of holdings, the dissemination of information which must be supplied to shareholders and participants resident in Spain, and exercise by the latter of their rights in general"*.

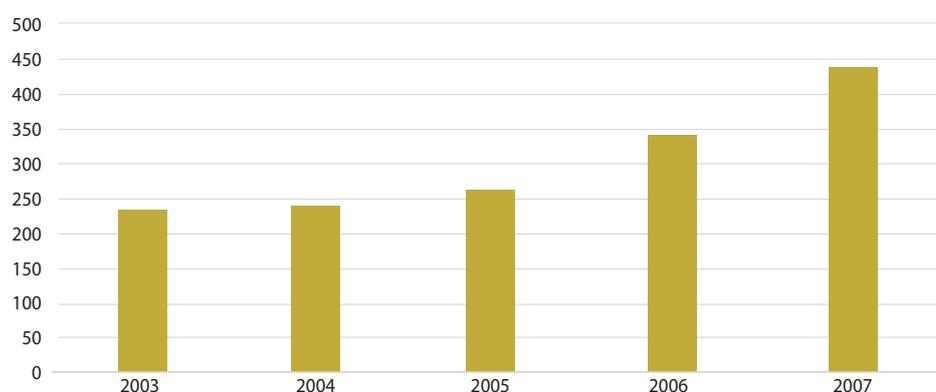
³ Section 28 of the CIU Regulations relating to relevant events provides that *"The CNMV is authorised to determine the manner, content and periods for notifying relevant events"*.

- To clarify the obligations to send relevant information on foreign CIUs marketed in Spain.

As can be seen in Figure 2 there has been a substantial increase in the number of foreign CIUs marketed in Spain. In the last five years there has been a growth of 89%. At 31 December 2007 the number of foreign CIUs registered in Spain for commercialisation was 440, with a total of 3,667 compartments and 16,166 classes of shares. The compartments are more comparable to Spanish funds since they are distinguished from each other as a result of having different investment policies, whilst the different classes are distinguished by applying different commissions.

Evolution of the number of foreign CIUs marketed in Spain

FIGURE 2



Source: CNMV.

At the present time the foreign CIUs marketed in Spain are European: the bulk of them comprise CIUs based in Luxembourg, which account for 52% of the total, followed by French and Irish CIUs, at 28% and 12% respectively. The volume of investment in these CIUs by Spanish investors has also undergone considerable growth in the last five years. At 31 December 2007 investment in foreign CIUs was some 14.54% of total investment in domestic investment funds, compared with 4.35% in 2003.

The clarification included in the Circular regarding the obligations of foreign CIUs marketed in Spain means that the entitlement to information of investors who acquire shares or holdings in foreign CIUs in this country becomes equivalent to those of investors in the country of origin. It does not seem that the Circular will constitute an additional burden for foreign CIUs marketed in Spain since in their marketing Memoranda they already undertook to inform Spanish investors of the relevant information. The only novelty incorporated is that they must do so through the CNMV and by electronic means.

In addition, designating as persons under an obligation to notify relevant events those who are already notifying information relating to foreign CIUs facilitates the operating procedure with the CNMV since the Circular does not establish any additional requirement for sending the relevant information.

4 Types of relevant events of CIUs

Council Directive 85/611/EEC of 2 December 1985, which regulates the general rules which Community CIUs must comply with, does not contain any provisions relating to relevant information nor, therefore, does it lay down any circumstances which must be treated as such. Consequently, each European Union member country has had the power to deal with this aspect in the manner it considers most appropriate.

In most European countries, such as France, Italy, Luxembourg and Germany, there is a general provision making it obligatory to give notice of events of particular relevance but without establishing specific cases. Our legislation, on the other hand, does specify some events which are relevant and as such must be notified to the CNMV for publication as well as being included by the CIU in following periodic reports.

The Circular on relevant events of CIUs, in Rule two, sets out the circumstances which are considered relevant events for both Spanish and foreign CIUs marketed in Spain. With respect to Spanish CIUs two groups can be distinguished, those which are published *ex officio* by the CNMV without the need for notification by the undertaking concerned or its manager, and those which must be notified by CIUs themselves.

1) Types of relevant event published *ex officio* by the CNMV:

The CNMV publishes those relevant events on an *ex officio* basis which are associated with a prior process of authorisation (replacement of management company or depository, mergers of funds and modifications of their management regulations) or registration (of basic modifications to the prospectuses of CIUs). Investment fund holders have a right of prior information linked to a right of withdrawal by which they must be individually informed of the changes which will take place in order, if they so wish, that they can be reimbursed or transfer their holdings at no cost during a period of one month. These changes will not take effect until at least that month has elapsed from individual notification to holders.

- Replacement of a management company or depository of investment funds and changes which take place in control of the former. These changes mainly take place after corporate operations in the financial sector. Holders must be aware of them since they could affect the evolution of the funds in which they invest.
- All decisions which give rise to an obligation to update the basic contents of the prospectus. These modifications, treated as basic, may only take effect after registration of the CIU prospectus with the CNMV and they are detailed in CNMV Circular 3/2006 of 26 October on CIU prospectuses (hereinafter the CIU Prospectus Circular). Of these we can highlight: changes in investment policy, increase in management and depository commissions, contracting investment advisers or delegation of asset management to a third party undertaking.

In addition, the CIU Prospectus Circular provides that in the period which elapses from when the CIU manager takes the decision to modify a basic element of the prospectus until registration thereof takes place, investors who wish to enter the CIU must be informed of these basic modifications pending registration. Furthermore, the manager must also have this information available for consultation by electronic means. The right of information of a possible investor interested in acquiring holdings in the CIU is thereby ensured. With respect to those who are also holders of the CIU, they must be informed by letter of the changes which may most affect them. For those other modifications for which as a result of their minor importance an individual communication need not be sent they will have information in the following periodic report sent by the Manager.

- Authorisation of a merger process in which an investment fund is involved. In this case, the holder must also be individually informed previously and announcements must be published in the Official State Gazette (*Boletín Oficial del Estado*) and in two national newspapers.
 - Any modification of the regulations of an investment fund which require prior authorisation of the CNMV. Transformation of an investment fund into a hedge fund provides a clear example of a regulatory modification which would require prior authorisation, since the characteristics of the investment and requirements of the product will be totally different.
 - Relevant events deriving from a decision of the CNMV.
- 2) Types of relevant event which must notified to the CNMV by CIUs for general information of investors:
- Reduction in the capital of investment companies in circulation or reimbursement in investment funds which exceed 20% of their capital or net worth respectively. A wholesale departure of investors from an undertaking may be a symptom that the CIU is not following a suitable investment strategy and the holder or shareholder must be aware of this situation.
 - Debt operations which exceed 5% of the net worth of the CIU, except in the case of a hedge fund since the latter have much more flexible debt limits than ordinary CIUs. A high level of debt on a continuous basis might mean that the fund does not have sufficient liquidity and that the management may not be the most suitable.
 - In the case of investment companies, the impossibility for the company to place more shares in circulation as a result of lacking shares in portfolio and the maximum capital pursuant to its articles of association having already been paid up. Collective investment companies (*SICAVs*) have an initial capital and maximum capital pursuant to their articles of association between which they fluctuate without the need for a resolutions of the general meeting. When this maximum capital pursuant

to the articles of association is reached a shareholders general meeting must be convened to increase their capital in order to permit the entry of new shareholders into the company as soon as possible, thereby recovering its status as an open-ended investment undertaking.

- Resolutions for dissolution and liquidation. This information must be notified as soon as possible since it may be highly relevant, particularly to an investor who may be interested in subscribing for holdings in the CIU.
- Suspension and resumption of trading of shares and suspension and resumption of subscription and reimbursement of holdings in investment funds. Any information which may detract from the free transferability of shares or holdings in the CIU is of maximum importance.
- Exclusions from stock exchange trading when the shares are traded on an organised securities trading system or market. With the birth of the MAB (Alternative Stock Exchange Market - *Mercado Alternativo Bursátil*) virtually all SICAVs whose shares are listed on any Stock Exchange have become traded on this alternative market.

Finally, there is a general case which provides that CIUs must also notify any other event which may reasonably affect an investor for the purpose of acquiring or transferring shares or holdings in the CIU, and therefore which could have a sensitive effect its liquidating value. The broad conflictive circumstances of financial markets in general, and of collective investment instruments in particular, makes the cataloguing of each and every one of the circumstances which would have to be considered a relevant event a virtually impossible exercise, and therefore it is necessary for this generic type to exist.

With respect to the notification obligations of foreign CIUs marketed in Spain, it is clarified that this relates to all of the information required by the legislation of the State in which it is based, on the same terms and within the same periods laid down in the legislation of origin.

Council Directive 85/611/EEC of 2 December 1985 does not refer to relevant information of CIUs and therefore does not lay down any circumstances which must be treated as such. Consequently, an election has been made to respect the circumstances which are notified by CIUs in their respective States of origin, ensuring that the information received by Spanish investors is equivalent to that of investors in the country of origin of the CIU.

5 Publicity of relevant events

Notifications of relevant information, both those published by the CNMV *ex officio* and those sent electronically by undertakings under an obligation to give notice, are immediately made available to the public on the CNMV website.

All relevant events are automatically incorporated in the public register maintained by the CNMV, which permits simple and rapid consultation by investors. In the information on “Consultation of official records” and the section “Relevant events and other notifications”, investors have a broad range of search options enabling them to select from the following types, which can be combined:

- Name of the undertaking which notifies the relevant event.
- Relevant events published on a particular date or dates.
- Notifications made in recent days.
- Type of relevant event.

Investors can therefore quickly and efficiently obtain all information enabling them to have adequate elements for forming a judgment when making their investment decisions.

As a general rule relevant information in respect of CIUs is published exclusively in the section of the CNMV website relating to the CIU in question, since information such as changes in investment policy, modification of applicable commissions or the fact that a CIU will be merged with another is information of interest to a future investor or a current holder or shareholder of the CIU but not to the market as a whole.

There are circumstances, however, which constitute an exception to the rule laid down in the previous paragraph. This was the case during the recent *sub prime* mortgage crisis in the USA which affected financial markets and gave rise to several foreign CIUs marketed in Spain being obliged to suspend subscriptions and reimbursement of holdings.

At that time, faced with the uncertainty regarding the possible extent of the widespread instability in markets in the Spanish collective investment sector, it became necessary for notifications from CIUs to be made available to both analysts and information disseminators as well as the public in general as soon as possible. Hence the importance of providing the sector with the most advanced technical means for achieving the greatest speed in making the relevant information available to the public.

6 Conclusions

The Circular on relevant events of CIUs is the culmination of a process of speeding up the procedure for making relevant information on CIUs available to the public. This process began with the possibility of sending notifications of relevant information on CIUs by electronic means and their automatic publication on the CNMV websites, which meant making an office open 24 hours a day available to users. This initiative preceded the decision to automatically publish

those relevant events which are associated with administrative authorisation and registration processes without the need for the undertakings to make any additional notification.

Furthermore, the clarification included in the Circular regarding obligations of foreign CIUs marketed in Spain to notify relevant information means that the right of information of investors who acquire their shares or holdings becomes equivalent to that of investors in their country of origin. This substantially increases the transparency of foreign undertakings, which is appropriate taking into account the substantial growth which has taken place in foreign CIUs marketed in Spain in recent years.

In short, taking into account that collective investment vehicles are the normal form by which small Spanish investors gain access to financial markets, it is of particular importance to improve the mechanisms which ensure that they receive all information which may affect their decisions to acquire or transfer shares or holdings in CIUs in a reliable, transparent, speedy and up to date manner. Equality of treatment and opportunity between investors is thereby guaranteed and transparency of the collective investment market ensured.

V Statistics Annex

1 Markets

1.1 Equity

Share issues and public offerings¹

TABLE 1.1

	2005	2006	2007	2007				2008
				I	II	III	IV	I ²
CASH VALUE ³ (Million euro)	2,960.5	5,021.7	23,757.9	803.9	11,218.1	4,337.2	7,398.7	9.5
Capital increases	2,803.4	2,562.9	21,689.5	696.1	9,896.5	4,273.8	6,823.1	0.0
Of which, primary offerings	0.0	644.9	8,502.7	0.0	334.2	3,485.2	4,683.3	0.0
With Spanish tranche	0.0	303.0	4,821.4	0.0	334.2	2,449.6	2,037.6	0.0
With international tranche	0.0	342.0	3,681.4	0.0	0.0	1,035.6	2,645.8	0.0
Secondary offerings	157.1	2,458.8	2,068.5	107.8	1,321.6	63.4	575.6	9.5
With Spanish tranche	54.7	1,568.1	1,517.1	107.8	913.5	63.4	432.4	9.5
With international tranche	102.5	890.7	551.4	0.0	408.1	0.0	143.3	0.0
NO. OF FILES ⁴	27	30	35	7	10	6	12	1
Capital increases	25	21	26	6	8	5	7	0
Of which, primary offerings	0	8	8	0	2	2	4	0
Of which, bonus issues	6	0	0	0	0	0	0	0
Secondary offerings	2	14	12	1	3	1	7	1
NO. OF ISSUERS ⁴	24	23	29	7	10	6	10	1
Capital increases	23	18	24	6	8	5	7	0
Of which, primary offerings	0	6	6	0	2	2	4	0
Secondary offerings	1	10	8	1	3	1	5	1

¹ Total files registered with the CNMV (including supplements of initial files).

² Available data: February 2008.

³ Does not include registered amounts that were not carried out.

⁴ Includes all registered offerings, including the issues that were not carried out.

Primary and secondary offerings. By type of subscriber

TABLE 1.2

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
PRIMARY OFFERINGS	0.0	644.9	8,502.7	0.0	334.2	3,485.2	4,683.3	0.0
Spanish tranche	0.0	303.0	4,646.2	0.0	334.2	2,277.0	2,035.0	0.0
Private subscribers	0.0	8.7	2,841.0	0.0	112.0	1,898.5	830.5	0.0
Institutional subscribers	0.0	294.3	1,805.2	0.0	222.2	378.5	1,204.5	0.0
International tranche	0.0	342.0	3,681.4	0.0	0.0	1,035.6	2,645.8	0.0
Employees	0.0	0.0	175.2	0.0	0.0	172.6	2.6	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
SECONDARY OFFERINGS	157.1	2,458.8	2,068.5	107.8	1,321.6	63.4	575.6	9.5
Spanish tranche	54.7	1,565.0	1,505.7	107.8	903.6	63.4	430.8	9.5
Private subscribers	27.3	390.0	393.9	16.2	289.4	0.0	88.4	0.0
Institutional subscribers	27.3	1,175.0	1,111.8	91.7	614.3	63.4	342.4	9.5
International tranche	102.5	890.7	551.4	0.0	408.1	0.0	143.3	0.0
Employees	0.0	3.1	11.4	0.0	9.9	0.0	1.6	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

¹ Available data: February 2008.

Admission to listing. Files registered at the CNMV

TABLE 1.3

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
NOMINAL VALUE (Million euro)								
With issuance prospectus	498.0	963.4	5,894.3	69.1	91.2	171.8	5,562.1	13.3
Capital increases	494.0	575.9	5,687.2	69.1	6.6	171.8	5,439.6	13.3
Of which, primary offerings	0.0	145.3	5,424.4	0.0	4.5	0.0	5,419.8	0.0
Secondary offerings	4.0	387.5	207.1	0.0	84.6	0.0	122.5	0.0
Without issuance prospectus	167.3	564.7	8,366.1	320.4	1,166.4	440.9	6,438.4	7.3
NO. OF FILES								
With issuance prospectus	26	18	22	5	5	4	8	2
Capital increases	25	13	18	5	3	4	6	2
Of which, primary offerings	0	5	6	0	2	0	4	0
Secondary offerings	1	9	7	0	3	0	4	0
Without issuance prospectus	27	61	72	17	19	20	16	7

¹ Available data: February 2008.

Companies listed¹

TABLE 1.4

	2005	2006	2007	2007				2008
				I	II	III	IV	I ²
Total electronic market ³	126	135	143	135	137	136	143	141
Of which, without Nuevo Mercado.	115	124	142	124	127	126	142	141
Of which, Nuevo Mercado.	11	11	1	11	10	10	1	0
Of which, foreign companies	5	6	5	6	6	6	5	5
Second Market	14	12	11	12	11	11	11	10
Madrid	2	2	2	2	2	2	2	2
Barcelona	10	9	9	9	8	9	9	8
Bilbao	0	0	0	0	0	0	0	0
Valencia	2	1	0	1	1	0	0	0
Open outcry ex SICAV	47	38	31	34	33	32	31	30
Madrid	22	16	13	15	14	14	13	14
Barcelona	28	24	20	21	20	20	20	19
Bilbao	14	10	9	9	9	9	9	9
Valencia	18	13	9	11	11	10	9	8
Open outcry SICAV	3,111	744	7	81	23	9	7	5
MAB ⁴	-	2,405	3,283	3,096	3,193	3,241	3,283	3,313
Latibex	32	34	34	34	34	34	34	34

1 Data at the end of period.

2 Available data: February 2008.

3 Without ETF (Exchange Traded Funds).

4 Alternative Stock Market.

Capitalisation¹

TABLE 1.5

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ²
Total electronic market ³	616,659.5	813,765.1	892,053.8	885,715.7	895,117.9	840,333.3	892,053.8	773,172.9
Of which, without Nuevo Mercado	607,167.8	800,148.0	891,875.7	870,818.8	884,128.5	829,721.5	891,875.7	773,172.9
Of which, Nuevo Mercado	9,491.8	13,617.1	178.1	14,896.9	10,989.4	10,611.9	178.1	0.0
Of which, foreign companies	64,312.7	105,600.9	134,768.6	137,856.1	137,570.1	104,807.9	134,768.6	121,053.6
lbex 35	411,712.5	512,828.0	524,651.0	533,589.0	537,038.9	527,210.1	524,651.0	452,308.3
Second Market	444.2	392.7	286.8	713.3	610.3	295.7	286.8	220.1
Madrid	9.2	18.9	27.8	32.6	37.3	24.6	27.8	25.0
Barcelona	291.2	184.2	259.0	404.2	234.2	271.1	259.0	195.1
Bilbao	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valencia	143.8	189.6	0.0	276.4	338.8	0.0	0.0	0.0
Open outcry ex SICAV	6,874.8	7,905.3	7,444.9	8,989.9	8,713.0	8,890.0	7,444.9	7,338.9
Madrid	3,486.7	2,698.1	1,840.6	3,159.6	3,050.6	2,796.4	1,840.6	1,783.2
Barcelona	3,129.2	4,966.3	4,627.8	5,333.9	5,159.5	5,247.4	4,627.8	5,111.0
Bilbao	405.9	59.5	108.2	56.2	137.1	137.1	108.2	108.2
Valencia	836.1	741.9	1,206.5	767.6	777.8	1,145.5	1,206.5	1,069.9
Open outcry SICAV	33,171.1	9,284.1	245.4	2,189.6	1,289.6	990.1	245.4	201.8
MAB ⁴	-	29,866.3	41,576.8	38,711.3	41,196.5	41,259.2	41,576.8	39,906.6
Latibex	216,111.3	271,641.8	427,773.6	278,554.2	346,492.3	387,064.2	427,773.6	435,484.2

1 Data at the end of period.

2 Available data: February 2008.

3 Without ETF (Exchange Traded Funds).

4 Alternative Stock Market.

Trading

TABLE 1.6

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Total electronic market ²	847,663.7	1,144,562.9	1,653,354.8	414,929.6	438,830.9	369,572.5	430,021.7	283,742.7
Of which, without Nuevo Mercado	817,834.7	1,118,546.1	1,627,369.5	404,057.1	433,444.8	364,309.6	425,558.0	283,731.3
Of which, Nuevo Mercado	29,829.0	26,016.8	25,985.3	10,872.5	5,386.2	5,262.9	4,463.7	11.4
Of which, foreign companies	15,115.1	11,550.3	7,499.3	4,228.5	1,313.2	939.4	1,018.2	446.1
Second Market	25.9	49.3	192.9	121.9	21.4	37.7	11.8	3.1
Madrid	1.8	7.2	8.9	4.7	2.4	0.9	0.8	0.4
Barcelona	22.9	41.6	182.3	116.6	18.7	36.0	11.0	2.7
Bilbao	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valencia	1.3	0.5	1.7	0.6	0.3	0.7	0.0	0.0
Open outcry ex SICAV	860.6	736.3	792.7	316.4	152.4	65.4	258.6	28.4
Madrid	187.8	257.6	236.1	66.6	55.4	21.3	92.7	16.5
Barcelona	667.0	297.8	402.8	239.2	94.5	40.1	29.1	10.5
Bilbao	1.1	159.2	0.1	0.0	0.0	0.0	0.0	0.0
Valencia	4.6	21.8	153.8	10.6	2.5	3.9	136.7	1.4
Open outcry SICAV	5,037.9	4,581.9	361.6	257.6	56.4	32.4	15.2	4.0
MAB ³	-	1,814.2	6,985.2	1,770.9	1,604.9	1,369.1	2,240.4	1,462.9
Latibex	556.7	723.3	868.2	217.0	226.5	209.1	215.6	98.2

1 Available data: February 2008.

2 Without ETF (Exchange Traded Funds).

3 Alternative Stock Market.

Trading on the electronic market by type of transaction¹

TABLE 1.7

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ²
Regular trading	798,934.5	1,080,117.5	1,573,875.0	401,231.1	423,056.8	359,745.1	389,841.9	264,784.4
Orders	488,416.3	658,839.2	981,713.1	255,425.4	247,466.7	232,805.5	246,015.5	178,930.2
Put-throughs	82,403.1	105,910.7	155,085.1	39,297.4	42,731.3	34,295.0	38,761.4	24,335.3
Block trades	228,115.1	315,367.7	437,076.8	106,508.3	132,858.9	92,644.6	105,064.9	61,519.0
Off-hours	27,863.0	11,651.6	18,301.5	3,644.2	5,191.6	3,563.2	5,902.5	2,776.4
Authorised trades	4,773.4	4,052.0	4,189.6	1,455.1	1,789.6	304.6	640.3	327.6
Art. 36.1 SML trades	1.3	6,439.7	0.0	0.0	0.0	0.0	0.0	0.0
Tender offers	6,682.8	18,094.6	26,284.3	4,158.7	50.0	1,995.7	20,079.8	14,049.1
Public offerings for sale	226.3	3,264.0	14,551.9	0.0	5,314.0	0.0	9,237.9	0.0
Declared trades	2,298.9	10,347.9	2,954.4	2,280.0	268.3	172.5	233.6	836.3
Options	5,268.0	8,279.8	10,240.4	1,608.2	2,609.6	2,795.7	3,227.0	117.2
Hedge transactions	1,615.4	2,315.7	2,957.8	552.3	550.9	995.9	858.8	851.7

1 Without ETF (Exchange Traded Funds).

2 Available data: February 2008.

Margin trading for sales and securities lending

TABLE 1.8

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
TRADING								
Securities lending ²	393,964.1	550,850.4	835,326.9	196,697.8	245,021.9	179,969.9	213,637.3	126,639.4
Margin trading for sales of securities ³	152.2	379.9	555.4	129.3	123.2	166.6	136.3	123.0
Margin trading for securities purchases ³	465.0	511.9	411.3	146.1	108.2	72.5	84.5	39.0
OUTSTANDING BALANCE								
Securities lending ²	66,737.5	62,058.2	79,532.9	75,199.6	103,293.4	92,265.1	79,532.9	64,363.7
Margin trading for sales of securities ³	28.5	73.6	112.4	103.8	94.6	133.7	112.4	77.0
Margin trading for securities purchases ³	52.3	70.1	59.4	74.5	64.0	45.3	59.4	35.3

1 Available data: February 2008.

2 Regulated by Article 36.7 of the Securities Market Law and Order ECO/764/2004.

3 Transactions performed in accordance with Ministerial Order dated 25 March 1991 on the margin system in spot transactions.

1.2 Fixed-income

Gross issues registered¹ at the CNMV

TABLE 1.9

	2005	2006	2007	2007				2008
				I	II	III	IV	I ²
NO. OF ISSUERS	155	159	173	60	66	53	75	38
Mortgage covered bonds	9	11	10	6	4	6	4	5
Territorial covered bonds	2	5	4	2	1	2	1	4
Non-convertible bonds and debentures	49	46	41	21	20	16	3	4
Convertible bonds and debentures	4	1	0	0	0	0	0	0
Backed securities	53	61	77	13	22	16	34	6
Commercial paper	68	68	80	28	22	18	35	20
Of which, asset-backed	3	3	3	0	2	1	0	0
Of which, non-asset-backed	65	65	77	28	20	17	35	20
Other fixed-income issues	1	0	2	0	1	2	0	0
Preference shares	6	9	5	2	1	2	0	4
NO. OF ISSUES	263	335	334	88	86	76	84	47
Mortgage covered bonds	21	37	32	8	10	9	5	7
Territorial covered bonds	3	6	8	2	1	4	1	4
Non-convertible bonds and debentures	93	115	79	31	25	20	3	6
Convertible bonds and debentures	4	1	0	0	0	0	0	0
Backed securities	54	82	101	17	25	19	40	6
Commercial paper	80	83	106	28	23	20	35	20
Of which, asset-backed	3	3	3	0	2	1	0	0
Of which, non-asset-backed	77	80	103	28	21	19	35	20
Other fixed-income issues	1	0	3	0	1	2	0	0
Preference shares	7	11	5	2	1	2	0	4
NOMINAL AMOUNT (Million euro)	414,253.9	523,131.4	648,757.0	173,448.3	156,957.4	163,782.9	154,568.4	71,281.8
Mortgage covered bonds	35,560.0	44,250.0	24,695.5	8,400.0	7,245.5	6,525.0	2,525.0	1,100.0
Territorial covered bonds	1,775.0	5,150.0	5,060.0	1,450.0	1,500.0	2,000.0	110.0	470.0
Non-convertible bonds and debentures	41,907.1	46,687.5	27,416.0	9,982.0	9,427.0	7,750.0	257.0	595.3
Convertible bonds and debentures	162.8	68.1	0.0	0.0	0.0	0.0	0.0	0.0
Backed securities	69,044.3	91,607.7	141,627.0	39,392.2	31,517.5	17,898.3	52,819.0	7,334.8
Spanish tranche	63,908.3	85,099.9	141,627.0	39,392.2	31,517.5	17,898.3	52,819.0	7,334.8
International tranche	5,136.0	6,507.8	0.0	0.0	0.0	0.0	0.0	0.0
Commercial paper ³	264,359.5	334,457.0	442,433.5	114,144.1	106,967.4	122,464.6	98,857.4	61,685.6
Of which, asset-backed	2,767.5	1,992.7	464.8	156.0	138.8	85.0	85.0	133.0
Of which, non-asset-backed	261,592.0	332,464.3	441,968.7	113,988.1	106,828.6	122,379.6	98,772.4	61,552.6
Other fixed-income issues	89.3	0.0	7,300.0	0.0	225.0	7,075.0	0.0	0.0
Preference shares	1,356.0	911.0	225.0	80.0	75.0	70.0	0.0	96.0
Pro memoria:								
Subordinated issues	11,078.5	27,361.5	47,158.3	14,481.7	3,777.6	12,702.1	16,196.9	881.0
Underwritten issues	94,368.0	92,213.5	121,608.5	39,392.2	31,616.5	17,898.3	32,701.5	1,777.1

1 This Includes the volume of issues admitted to trading without register issuance prospectuses.

2 Available data: February 2008.

3 The figures for commercial paper refer to the amount placed in the year.

Issues admitted to trading on AIAF

TABLE 1.10

Nominal amount in million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Total	425,137.4	507,525.3	640,096.2	175,388.7	147,084.9	172,663.4	144,959.2	84,632.6
Commercial paper	263,728.9	332,328.4	439,787.3	115,064.7	105,314.5	120,587.0	98,821.1	65,257.2
Bonds and debentures	56,771.5	45,155.4	30,006.9	10,632.0	7,295.0	9,375.0	2,704.9	107.0
Mortgage covered bonds	31,600.0	43,720.0	27,195.5	9,550.0	6,495.5	8,575.0	2,575.0	1,000.0
Territorial covered bonds	1,775.0	2,650.0	7,450.0	2,950.0	1,000.0	3,500.0	0.0	510.0
Backed securities	67,480.5	83,042.5	135,149.5	36,830.0	26,904.9	30,556.5	40,858.1	17,662.4
Preference shares	3,781.5	629.0	507.0	362.0	75.0	70.0	0.0	96.0
Matador bonds	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

1 Available data: February 2008.

AIAF. Issuers, issues and outstanding balance

TABLE 1.11

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
NO. OF ISSUERS	384	438	492	448	457	472	492	505
Commercial paper	66	69	73	68	66	71	73	74
Bonds and debentures	82	80	92	93	92	92	92	92
Mortgage covered bonds	12	14	14	15	15	14	14	16
Territorial covered bonds	3	5	7	7	7	7	7	10
Backed securities	211	257	316	268	280	297	316	329
Preference shares	42	46	50	49	49	50	50	52
Matador bonds	20	20	15	18	17	16	15	15
NO. OF ISSUES	2,836	3,681	4,314	3,985	4,143	4,293	4,314	4,407
Commercial paper	1,724	2,242	2,493	2,451	2,539	2,552	2,493	2,500
Bonds and debentures	329	398	445	423	430	452	445	444
Mortgage covered bonds	54	83	111	90	98	106	111	116
Territorial covered bonds	8	11	19	14	15	19	19	23
Backed securities	631	856	1,157	916	971	1,074	1,157	1,231
Preference shares	58	65	71	69	70	71	71	75
Matador bonds	32	26	18	22	20	19	18	18
OUTSTANDING BALANCE² (Million euro)	448,679.3	588,942.3	758,559.8	645,466.6	675,996.4	729,774.6	758,559.8	768,784.3
Commercial paper	57,719.4	70,778.6	98,467.6	77,054.5	81,591.4	97,795.9	98,467.6	99,320.7
Bonds and debentures	103,250.7	131,107.8	139,586.3	138,282.1	136,090.3	142,655.3	139,586.3	134,693.3
Mortgage covered bonds	90,550.0	129,710.0	150,905.5	139,260.0	145,755.5	151,330.5	150,905.5	151,905.5
Territorial covered bonds	7,575.0	9,525.0	16,375.0	12,475.0	13,475.0	16,375.0	16,375.0	16,885.0
Backed securities	164,810.0	222,866.1	328,924.6	253,378.5	274,173.0	297,196.9	328,924.6	341,583.0
Preference shares	22,486.6	23,115.6	23,062.6	23,417.6	23,492.6	23,062.6	23,062.6	23,158.6
Matador bonds	2,287.6	1,839.2	1,238.2	1,598.8	1,418.5	1,358.4	1,238.2	1,238.2

1 Available data: February 2008.

2 Nominal amount.

AIAF. Trading

TABLE 1.12

Nominal amount in million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
BY TYPE OF ASSET	877,812.1	910,493.9	1,127,477.7	286,592.8	262,799.2	287,044.2	291,041.6	218,102.5
Commercial paper	408,185.0	489,069.5	568,009.6	153,727.0	140,611.4	148,715.3	124,955.9	92,194.7
Bonds and debentures	86,585.7	82,421.1	87,035.7	27,157.8	25,082.6	19,214.4	15,580.9	12,852.6
Mortgage covered bonds	60,060.9	70,113.5	80,811.2	21,036.3	19,535.9	16,042.3	24,196.7	13,147.7
Territorial covered bonds	2,740.1	3,659.1	7,749.8	1,216.9	568.4	4,315.0	1,649.6	4,569.7
Backed securities	313,778.5	257,628.9	378,005.2	81,489.8	75,463.1	97,548.2	123,504.1	94,601.4
Preference shares	4,046.2	4,647.8	4,492.4	1,409.7	1,031.7	897.7	1,153.4	730.4
Matador bonds	2,415.7	2,954.1	1,373.8	555.2	506.2	311.4	0.9	6.0
BY TYPE OF TRANSACTION	877,812.1	910,493.9	1,127,477.7	286,592.8	262,799.2	287,044.2	291,041.6	218,102.5
Outright	322,819.1	386,368.8	416,477.9	114,617.8	100,039.0	104,013.7	97,807.4	71,523.4
Repos	284,520.0	330,839.9	441,362.7	120,468.5	117,077.4	109,684.9	94,131.8	61,487.7
Sell-buybacks/Buy-sellbacks	270,473.0	193,285.1	269,637.1	51,506.4	45,682.8	73,345.6	99,102.3	85,091.5

1 Available data: February 2008.

AIAF. Third-party trading. By purchaser sector

TABLE 1.13

Nominal amount in million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Total	591,837.2	702,608.8	837,308.5	231,736.2	211,982.4	209,271.8	184,318.1	129,715.5
Non-financial companies	218,139.5	260,108.1	364,490.6	88,151.6	102,730.2	91,476.3	82,132.5	52,582.1
Financial institutions	218,381.1	247,876.4	282,816.9	68,858.1	71,023.9	73,910.0	69,024.8	48,977.0
Credit institutions	71,118.9	83,999.1	99,492.0	20,027.7	26,406.4	26,507.9	26,550.0	17,688.6
CIS ² , insurance and pension funds	138,580.4	145,911.5	152,429.2	40,317.3	38,310.3	39,606.4	34,195.3	27,378.1
Other financial institutions	8,681.8	17,965.8	30,895.6	8,513.2	6,307.3	7,795.7	8,279.5	3,910.2
General government	5,629.4	7,058.9	7,762.4	2,514.1	2,195.6	1,944.6	1,108.1	908.1
Households and NPISHs ³	14,433.3	23,675.9	28,534.8	16,310.4	4,427.7	4,047.5	3,749.2	2,549.3
Rest of the world	135,253.9	163,889.4	153,703.8	55,902.0	31,605.1	37,893.3	28,303.5	24,699.1

1 Available data: February 2008.

2 Collective Investment Schemes.

3 Non-profit institutions serving households.

Issues admitted to trading on equity markets. Files registered at the CNMV

TABLE 1.14

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
NOMINAL AMOUNTS (Million euro)	1,234.6	68.1	7,000.0	0.0	0.0	0.0	7,000.0	0.0
Non-convertible bonds and debentures	1,140.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Convertible bonds and debentures	94.6	68.1	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	7,000.0	0.0	0.0	0.0	7,000.0	0.0
NO. OF FILES	6	1	1	0	0	0	1	0
Non-convertible bonds and debentures	3	0	0	0	0	0	0	0
Convertible bonds and debentures	3	1	0	0	0	0	0	0
Others	0	0	1	0	0	0	1	0

¹ Available data: February 2008.

Equity markets. Issuers, issues and outstanding balances

TABLE 1.15

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
NO. OF ISSUERS	56	57	53	56	53	51	53	54
Private issuers	39	40	40	40	38	38	40	41
Non-financial companies	12	10	6	10	8	8	6	6
Financial institutions	27	30	34	30	30	30	34	35
General government ³	17	17	13	16	15	13	13	13
Regional governments	3	3	3	3	3	3	3	3
NO. OF ISSUES	267	264	249	252	247	244	249	247
Private issuers	122	131	133	129	121	121	133	135
Non-financial companies	22	18	12	17	14	14	12	12
Financial institutions	100	113	121	112	107	107	121	123
General government ³	145	133	116	123	126	123	116	112
Regional governments	92	89	83	87	91	89	83	81
OUTSTANDING BALANCES² (Million euro)	16,323.0	17,105.4	25,654.7	16,952.6	16,594.7	16,918.2	25,654.7	25,506.2
Private issuers	5,507.3	6,784.3	14,958.1	6,596.0	6,183.0	6,055.4	14,958.1	14,980.8
Non-financial companies	835.4	492.1	452.5	486.3	454.0	454.0	452.5	453.3
Financial institutions	4,671.9	6,292.2	14,505.6	6,109.7	5,729.0	5,601.4	14,505.6	14,527.5
General government ³	10,816.1	10,321.1	10,696.6	10,356.6	10,411.7	10,862.8	10,696.6	10,525.4
Regional governments	8,457.2	8,319.8	8,862.6	8,665.6	8,721.4	8,788.0	8,862.6	8,755.0

¹ Available data: February 2008.

² Nominal amount.

³ Without public book-entry debt.

Trading on equity markets

TABLE 1.16

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Nominal amounts in million euro								
Electronic market	220.0	257.3	444.8	87.2	23.5	17.8	316.3	248.2
Open outcry	4,538.3	5,009.9	7,154.3	2,067.1	592.6	471.1	4,023.6	1,745.2
Madrid	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Barcelona	4,404.2	4,879.6	7,040.1	2,033.0	563.6	445.3	3,998.2	1,711.5
Bilbao	9.2	24.8	7.5	1.6	2.0	1.7	2.1	1.2
Valencia	124.8	105.5	106.7	32.4	27.0	24.1	23.2	32.4
Public book-entry debt	36.1	35.6	33.6	7.7	10.4	6.9	8.7	6.2
Regional governments debt	83,204.0	84,443.6	84,178.3	20,980.3	21,295.2	20,750.1	21,152.6	11,771.9

¹ Available data: February 2008.

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

TABLE 1.17

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Nominal amounts in million euro								
Total	219.6	175.1	95.8	26.1	22.9	14.1	32.8	22.3
Outright	71.0	94.3	58.6	17.3	14.1	12.0	15.2	16.5
Sell-buybacks/Buy-sellbacks	148.5	80.2	37.2	8.8	8.8	2.0	17.6	5.8
Others	0.1	0.6	0.0	0.0	0.0	0.0	0.0	0.0

¹ Available data: February 2008.

1.3 Derivatives and other products

1.3.1 Financial derivatives markets: MEFF

Trading on MEFF

TABLE 1.18

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Number of contracts								
Debt products	46	15	13	1	4	4	4	2
Debt futures ²	46	15	13	1	4	4	4	2
Ibex 35 products ^{3,4}	5,490,958	7,119,853	9,288,909	2,246,165	2,443,146	2,423,272	2,176,326	1,641,347
Ibex 35 plus futures	4,935,648	6,408,961	8,435,258	2,056,808	2,235,602	2,211,103	1,931,745	1,433,303
Ibex 35 mini futures	114,563	159,830	286,574	62,981	70,034	78,006	75,552	61,000
Call mini options	232,825	288,542	227,535	48,028	53,850	43,365	82,293	51,394
Put mini options	207,922	262,521	339,542	78,348	83,661	90,798	86,736	95,649
Stock products ⁵	29,728,916	33,655,790	34,887,808	6,916,993	6,818,146	8,141,493	13,011,176	5,941,933
Futures	18,813,689	21,229,811	21,294,315	3,777,996	3,773,666	5,105,492	8,637,161	3,572,025
Call options	6,803,863	7,664,125	6,775,525	1,624,490	1,655,261	1,398,403	2,097,371	1,001,540
Put options	4,111,364	4,761,854	6,817,968	1,514,507	1,389,219	1,637,598	2,276,644	1,368,368
Pro-memoria: MEFF trading on Eurex								
Debt products ⁶	1,440,370	1,117,956	1,059,113	242,092	303,004	294,058	219,959	230,355
Index products ⁷	1,080,801	1,423,441	1,371,250	338,709	401,267	365,491	265,783	237,762

1 Available data: February 2008.

2 Contract size: 100 thousand euros.

3 The number of Ibex 35 mini futures (multiples of 1 euro) was standardised to the size of the Ibex 35 plus futures (multiples of 10 euro).

4 Contract size: Ibex 35 * 10 euros.

5 Contract size: 100 Stocks.

6 Bund, Bobl and Schatz futures.

7 Dax 30, DJ EuroStoxx 50 and DJ Stoxx 50 futures.

1.3.2 Warrants, option buying and selling contracts, and ETF (Exchange Traded Funds)

Issues registered at the CNMV

TABLE 1.19

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
WARRANTS²								
Premium amount (Million euro)	1,840.0	5,144.3	8,920.3	1,942.1	1,492.9	2,971.6	2,513.7	2,931.1
On stocks	1,180.8	3,697.6	6,215.1	1,411.9	1,077.8	1,888.6	1,836.7	2,169.3
On indexes	559.9	1,064.9	2,311.2	449.4	380.9	951.7	529.1	676.2
Other underlyings ³	99.3	381.8	394.0	80.7	34.2	131.2	147.8	85.6
Number of issues	1,720	4,063	7,005	1,667	1,404	1,808	2,126	2,676
Number of issuers	6	8	7	7	6	7	7	6
OPTION BUYING AND SELLING CONTRACTS								
Nominal amounts (Million euro)	112.2	206.8	151.0	61.0	45.0	25.0	20.0	12.0
On stocks	87.8	196.2	145.0	55.0	45.0	25.0	20.0	12.0
On indexes	16.4	0.6	0.0	0.0	0.0	0.0	0.0	0.0
Other underlyings ³	8.0	10.0	6.0	6.0	0.0	0.0	0.0	0.0
Number of issuers	13	12	9	4	2	1	2	1
Number of issues	4	4	3	3	1	1	1	1

1 Available data: February 2008.

2 Includes issues not requiring a prospectus by application of the new regulations.

3 Includes the following underlying: baskets of stocks, exchange rates, interest rates and commodities.

Equity markets. Warrants and ETF trading

TABLE 1.20

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
WARRANTS								
Trading (Million euro)	2,142.3	2,907.4	5,129.6	1,169.4	1,323.8	1,429.6	1,206.7	627.5
On Spanish stocks	1,431.7	1,803.9	3,200.7	784.1	823.3	805.4	788.0	383.1
On foreign stocks	155.8	294.7	474.2	120.8	133.6	115.1	104.6	35.2
On indexes	516.8	727.4	1,376.6	237.8	351.3	489.9	297.7	195.5
Other underlyings ²	38.0	81.4	78.1	26.8	15.6	19.3	16.5	13.8
Number of issues ³	2,520	4,284	7,837	3,073	3,440	3,848	4,083	3,293
Number of issuers ³	8	9	9	9	9	9	9	8
CERTIFICATES								
Trading (Million euro)	69.8	58.8	57.5	15.3	14.3	14.7	13.3	4.4
Number of issues ³	15	14	18	10	12	11	17	17
Number of issuers ³	5	5	4	3	3	3	4	4
ETF								
Trading (Million euro)	-	-	4,664.5	927.2	832.8	844.9	2,059.6	2,690.1
Number of funds	-	-	21	5	5	12	21	26
Assets ⁴ (Million euro)	-	-	885.8	507.8	521.6	511.8	885.8	na

1 Available data: February 2008.

2 Includes the following underlying: baskets of stocks, exchange rates, interest rates and commodities.

3 Issues or issuers which were traded in each period.

4 Foreign collective investment schemes including the investment volume marketed in Spain.

na: No available data.

1.3.3 Non-financial derivatives

Trading on MFAO¹

TABLE 1.21

	2005	2006	2007	2007				2008
				I	II	III	IV	I ²
Number of contracts								
On olive oil								
Extra – virgin olive oil futures ³	21,145	35,079	46,405	16,679	14,173	5,832	9,721	9,583

1 Olive oil futures market.

2 Available data: February 2008.

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

2 Investment services

Investment services. Spanish firms, branches and agents

TABLE 2.1

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Broker – dealers								
Spanish firms	46	47	46	45	46	46	46	48
Branches	96	108	102	95	97	100	102	109
Agents	6,562	6,610	6,657	6,466	6,614	6,618	6,657	6,631
Brokers								
Spanish firms	56	57	53	55	55	54	53	51
Branches	11	11	12	11	12	12	12	8
Agents	516	589	625	601	644	647	625	620
Portfolio management companies								
Spanish firms	17	15	11	14	13	12	11	11
Branches	4	4	4	4	4	4	4	4
Agents	14	5	6	5	5	6	6	5
Credit institutions²								
Spanish firms	206	204	201	204	202	202	201	200

1 Available data: February 2008.

2 Source: Banco de España.

Investment services. Foreign firms

TABLE 2.2

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Total	1,196	1,321	1,766	1,357	1,386	1,432	1,766	1,885
European Economic Area investment services firms	867	973	1,394	1,005	1,027	1,068	1,394	1,510
Branches	18	22	29	24	25	26	29	30
Free provision of services	849	951	1,365	981	1,002	1,042	1,365	1,480
Credit institutions ²	329	348	372	352	359	364	372	375
From EU member states	320	339	363	344	351	355	363	366
Branches	38	44	52	45	49	50	52	54
Free provision of services	281	294	310	298	301	304	310	311
Subsidiaries of free provision of services institutions	1	1	1	1	1	1	1	1
From non-EU states	9	9	9	8	8	9	9	9
Branches	8	8	8	7	7	8	8	8
Free provision of services	1	1	1	1	1	1	1	1

1 Available data: February 2008.

2 Source: Banco de España.

Intermediation of spot transactions

TABLE 2.3

Million euro	IV 2006				IV 2007			
	Spanish Stock Exchange	Other Spanish markets	Foreign markets	Total	Spanish Stock Exchange	Other Spanish markets	Foreign markets	Total
FIXED – INCOME								
Total	4,395	2,695,533	280,170	2,980,098	8,645	2,496,431	453,365	2,958,441
Broker-dealers	4,280	251,823	41,799	297,902	8,040	269,220	39,618	316,878
Brokers	115	2,443,710	238,371	2,682,196	605	2,227,211	413,747	2,641,563
EQUITY								
Total	536,382	2,542	25,130	564,054	595,346	1,927	34,824	632,097
Broker-dealers	495,729	1,480	20,836	518,045	558,712	960	30,762	590,434
Brokers	40,653	1,062	4,294	46,009	36,634	967	4,062	41,663

Intermediation of derivative transactions¹

TABLE 2.4

Million euro	IV 2006				IV 2007			
	Spanish organised markets	Foreign organised markets	Non organised markets	Total	Spanish organised markets	Foreign organised markets	Non organised markets	Total
Total	215,709	1,833,111	1,052,004	3,100,824	277,649	2,155,430	790,808	3,223,887
Broker – dealers	108,923	253,953	5,164	368,040	92,617	406,129	28,577	527,323
Brokers	106,786	1,579,158	1,046,840	2,732,784	185,032	1,749,301	762,231	2,696,564

1 The amount of the buy and sell transactions of financial assets, financial futures on values and interest rates, and other transactions on interest rates will be the securities nominal or notional value or the principal to which the contract reaches. The amount of the transactions on options will be the strike price of the underlying asset multiplied by the number of instruments committed.

Portfolio management. Number of portfolios and assets under management

TABLE 2.5

	IV 2006			IV 2007		
	Total	IIC ¹	Other ²	Total	IIC ¹	Other ²
NUMBER OF PORTFOLIOS						
Total	16,278	85	16,193	19,084	105	18,979
Broker – dealers	8,230	22	8,208	10,839	30	10,809
Brokers	3,977	28	3,949	4,128	40	4,088
Portfolio management companies	4,071	35	4,036	4,117	35	4,082
ASSETS UNDER MANAGEMENT (Thousand euro)						
Total	12,940,268	1,256,154	11,684,114	14,486,231	1,840,994	12,645,237
Broker – dealers	5,195,618	646,377	4,549,241	6,193,570	929,707	5,263,863
Brokers	3,498,993	328,284	3,170,709	3,661,245	636,580	3,024,665
Portfolio management companies	4,245,657	281,493	3,964,164	4,631,416	274,707	4,356,709

1 IIC: Collective investment schemes.

2 Includes the rest of clients, both covered and not covered by the Investment Guarantee Fund, an investor compensation scheme regulated by Royal Decree 948/2001.

Aggregated income statement. Broker – dealers

TABLE 2.6

Thousand euro ¹				2007				2008
	2005	2006	2007	I	II	III	IV	I ²
I. FINANCIAL INCOME	57,653	17,325	-29,968	8,484	11,025	-15,840	-29,968	-5,787
II. NET INCOME FROM SECURITIES TRADING	200,360	48,335	-224,173	38,135	-166,565	-214,615	-224,173	23,188
III. NET COMMISSION	653,273	775,377	893,803	240,751	485,244	680,927	893,803	80,112
Commission revenues	847,524	1,009,089	1,181,772	312,113	624,257	894,244	1,181,772	111,591
Brokering	526,241	629,952	775,418	215,607	409,875	588,741	775,418	80,154
Placement and underwriting	58,685	73,278	62,145	9,161	31,775	47,019	62,145	5,251
Securities deposit and recording	17,593	22,367	25,351	5,743	12,455	18,665	25,351	2,034
Portfolio management	20,599	23,883	29,649	6,757	14,570	20,388	29,649	2,032
Design and advising	52,180	55,918	65,083	20,736	40,110	51,793	65,083	4,591
Stocks search and placement	6	0	9	9	9	9	9	6
Market credit transactions	56	33	23	5	11	17	23	2
IIC subscription and redemption	118,871	141,312	138,481	34,771	70,425	105,659	138,481	10,234
Other	53,293	62,346	85,613	19,324	45,027	61,953	85,613	7,287
Commission expenses	194,251	233,712	287,969	71,362	139,013	213,317	287,969	31,479
IV. TOTAL NET REVENUES	911,286	841,037	639,662	287,370	329,704	450,472	639,662	97,513
V. OPERATING INCOME	498,362	395,105	180,892	173,463	98,455	113,320	180,892	58,650
VI. EARNINGS AFTER TAXES	266,734	430,651	540,390	280,510	482,067	674,057	540,390	75,591

1 Added amounts from the beginning of the year to the last day of every quarter. From 2005 it includes companies removed through out the year.

2 Available data: January 2008.

Results of proprietary trading. Broker – dealers

TABLE 2.7

Thousand euro ¹	Total		Financial income		Securities portfolio		Other charges	
	IV 2006	IV 2007	IV 2006	IV 2007	IV 2006	IV 2007	IV 2006	IV 2007
Total	65,239	-316,875	17,325	-29,968	48,335	-224,173	-421	-62,734
Money market assets and public debt	2,408	-22,720	9,464	4,441	-7,056	-27,161	0	0
Other fixed – income securities	50,950	83,172	40,820	60,809	10,130	22,363	0	0
Domestic portfolio	46,650	87,596	37,172	56,076	9,478	31,520	0	0
Foreign portfolio	4,300	-4,424	3,648	4,733	652	-9,157	0	0
Equities	192,668	293,609	69,584	100,151	123,084	193,458	0	0
Domestic portfolio	219,189	181,877	39,294	46,633	179,895	135,244	0	0
Foreign portfolio	-26,521	111,732	30,290	53,518	-56,811	58,214	0	0
Derivatives	-66,372	-397,299	0	0	-66,372	-397,299	0	0
Repurchase agreements	-13,452	-8,345	-13,452	-8,345	0	0	0	0
Market credit transactions	0	0	0	0	0	0	0	0
Deposits and other transactions with financial Intermediaries	-128,602	-212,675	-128,602	-212,675	0	0	0	0
Other transactions	27,639	-52,617	39,511	25,651	-11,451	-15,534	-421	-62,734

1 Added amounts from the beginning of the year to the last day of every quarter. From 2005 it includes companies removed through out the year.

Aggregated income statement. Brokers

TABLE 2.8

Thousand euro ¹				2007				2008
	2005	2006	2007	I	II	III	IV	I ²
I. FINANCIAL INCOME	10,665	12,934	14,395	3,275	6,899	10,500	14,395	1,181
II. NET INCOME FROM SECURITIES TRADING	3,306	3,906	580	437	1,120	651	580	-779
III. NET COMMISSION	184,113	233,447	237,403	62,888	121,309	177,379	237,403	16,254
Commission revenues	229,752	297,030	310,892	81,545	159,573	233,859	310,892	19,347
Brokering	97,948	114,111	131,976	34,088	66,060	96,183	131,976	7,978
Placement and underwriting	3,821	3,183	2,501	465	1,470	2,409	2,501	0
Securities deposit and recording	1,357	1,520	1,680	683	1,005	1,294	1,680	139
Portfolio management	14,868	28,672	27,457	8,177	14,534	20,239	27,457	2,159
Design and advising	2,664	2,360	2,224	423	1,119	1,273	2,224	77
Stocks search and placement	0	0	0	0	0	0	0	0
Market credit transactions	0	0	0	1	1	1	0	0
IIC subscription and redemption	46,171	68,513	74,918	17,629	37,345	57,090	74,918	3,896
Other	62,923	78,671	70,136	20,079	38,039	55,370	70,136	5,098
Commission expenses	45,639	63,583	73,489	18,657	38,264	56,480	73,489	3,093
IV. TOTAL NET REVENUES	198,084	250,287	252,378	66,600	129,328	188,530	252,378	16,656
V. OPERATING INCOME	66,420	95,026	98,596	28,709	53,410	76,858	98,596	5,322
VI. EARNINGS AFTER TAXES	38,264	62,449	86,017	33,484	64,113	85,525	86,017	5,876

1 Added amounts from the beginning of the year to the last day of every quarter. From 2005 it includes companies removed through out the year.

2 Available data: January 2008.

Aggregated income statement. Portfolio management companies

TABLE 2.9

Thousand euro ¹	2005	2006	2007	2007				2008
				I	II	III	IV	I ²
I. FINANCIAL INCOME	575	895	1,442	338	705	1,095	1,442	126
II. NET INCOME FROM SECURITIES TRADING	65	6	21	-1	-16	-8	21	-42
III. NET COMMISSION	17,164	15,195	15,501	3,875	7,485	11,313	15,501	1,186
Commission revenues	25,508	27,625	27,340	7,435	14,804	22,411	27,340	2,414
Portfolio management	18,813	22,068	22,545	6,028	12,371	19,114	22,545	2,076
Design and advising	4,380	4,951	2,614	898	1,380	1,668	2,614	170
IIC subscription and redemption	592	261	1,728	393	820	1,281	1,728	135
Other	1,723	345	453	116	233	348	453	33
Commission expenses	8,344	12,430	11,839	3,560	7,319	11,098	11,839	1,228
IV. TOTAL NET REVENUES	17,804	16,096	16,964	4,212	8,174	12,400	16,964	1,270
V. OPERATING INCOME	6,051	6,352	7,226	1,661	3,171	4,967	7,226	354
VI. EARNINGS AFTER TAXES	3,465	4,112	4,837	1,420	2,477	3,597	4,837	279

1 Added amounts from the beginning of the year to the last day of every quarter. From 2005 it includes companies removed through out the year.

2 Available data: January 2008.

Surplus equity over capital adequacy requirements¹

TABLE 2.10

Thousand euro	Surplus		Number of companies according to its surplus percentage									
	Total amount	% ²	< 50 ³	<100	<150	<200	<300	<400	<500	<750	<1000	>1000
Total	1,172,886	353.25	15	18	11	6	18	7	7	12	5	11
Broker – dealers	1,033,622	418.27	2	5	3	0	8	5	5	7	4	7
Brokers	125,097	202.59	10	11	6	4	9	2	2	5	1	3
Portfolio management companies	14,167	61.18	3	2	2	2	1	0	0	0	0	1

1 Available data: December 2007.

2 Average percentage is weighted by the required equity of each company. It is an indicator of the number of times, in percentage terms, that the surplus contains the required equity in an average company.

3 Includes all registered companies, even if they have not sent information.

Return on equity (ROE) before taxes¹

TABLE 2.11

	Average ²	Losses	Number of companies according to its annualized return								
			0-5%	6-15%	16-30%	31-45%	46-60%	61-75%	76-100%	>100%	
Total	57.34	9	12	20	21	8	11	4	2	23	
Broker – dealers	58.60	2	2	8	9	4	6	1	1	13	
Brokers	55.19	6	8	10	8	4	4	3	1	9	
Portfolio management companies	21.09	1	2	2	4	0	1	0	0	1	

1 Available data: December 2007.

2 Average weighted by equity, %.

3 Collective investment schemes (IIC)¹

Number, management companies and depositories of collective investment schemes registered at the CNMV

TABLE 3.1

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Total financial IIC	5,841	6,006	6,296	6,071	6,169	6,245	6,296	6,331
Mutual funds	2,723	2,850	2,954	2,885	2,921	2,947	2,954	2,958
Investment companies	3,118	3,149	3,290	3,178	3,217	3,251	3,290	3,315
Funds of hedge funds	-	2	31	2	22	30	31	35
Hedge funds	-	5	21	6	9	17	21	23
Total real estate IIC	13	17	18	17	17	19	18	17
Real estate investment funds	7	9	9	9	9	10	9	9
Real estate investment companies	6	8	9	8	8	9	9	8
Total foreign IIC marketed in Spain	260	340	440	354	362	397	440	459
Foreign funds marketed in Spain	115	164	225	169	171	197	225	239
Foreign companies marketed in Spain	145	176	215	185	191	200	215	220
Management companies	112	114	120	116	116	121	120	121
IIC depositories	135	132	126	129	127	127	126	126

1 Available data: February 2008.

In this document, neither hedge funds nor funds of hedge funds are included in the figures referred to mutual funds.

Number of IIC investors and shareholders

TABLE 3.2

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Total financial IIC	8,869,084	9,048,207	8,492,282	9,156,645	9,180,702	8,900,911	8,492,282	-
Mutual funds	8,450,164	8,637,781	8,053,049	8,740,972	8,755,921	8,467,203	8,053,049	7,690,219
Investment companies	418,920	410,403	434,156	415,539	423,142	430,315	434,156	-
Funds of hedge funds ²	-	2	3,950	26	1,456	3,142	3,950	4,006
Hedge funds ²	-	21	1,127	108	183	251	1,127	1,141
Total real estate IIC	119,113	151,053	146,353	153,656	154,426	152,577	146,353	148,416
Real estate investment funds	118,857	150,304	145,510	152,902	153,630	151,916	145,510	147,577
Real estate investment companies	256	749	843	754	796	661	843	839
Total foreign IIC marketed in Spain	560,555	779,165	850,931	782,020	825,771	834,914	850,931	-
Foreign funds marketed in Spain	104,089	144,139	142,782	158,900	176,884	158,925	142,782	-
Foreign companies marketed in Spain	456,466	635,026	708,149	623,120	648,887	675,989	708,149	-

1 Available data: January 2008. Real estate investment companies and foreign IIC send this information quarterly.

2 Provisional data in case of funds of hedge funds and hedge funds.

IIC total net assets

TABLE 3.3

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Total financial IIC	289,810.7	300,584.0	287,968.7	305,058.2	310,144.3	303,306.6	287,968.7	274,320.9
Mutual funds ²	262,200.9	270,406.3	255,040.9	273,412.8	276,600.4	269,907.0	255,040.9	243,271.1
Investment companies	27,609.8	30,152.7	31,481.5	31,516.0	32,791.7	32,360.1	31,481.5	29,550.6
Funds of hedge funds ³	-	0.6	1,000.6	9.5	600.2	829.2	1,000.6	1,023.9
Hedge funds ³	-	24.4	445.8	119.9	152.0	210.2	445.8	475.3
Total real estate IIC	6,690.8	9,052.0	9,121.4	9,240.8	9,416.8	9,409.6	9,121.4	9,020.4
Real estate investment funds	6,476.9	8,595.9	8,608.5	8,781.7	8,929.4	8,905.3	8,608.5	8,676.3
Real estate investment companies	213.9	456.1	512.9	459.2	487.4	504.3	512.9	344.1
Total foreign IIC marketed in Spain	33,668.1	44,102.9	37,092.7	45,113.8	50,141.4	44,847.4	37,092.7	-
Foreign funds marketed in Spain	8,267.3	12,099.3	7,010.3	12,464.3	14,211.5	10,530.7	7,010.3	-
Foreign companies marketed in Spain	25,400.8	32,003.5	30,082.4	32,649.6	35,929.9	34,316.7	30,082.4	-

1 Available data: January 2008. Real estate investment companies and foreign IIC send this information quarterly.

2 For the fourth quarter 2007, mutual funds investments in financial IIC reached 18.2 billion euro

3 Provisional data in case of funds of hedge funds and hedge funds.

Mutual funds asset allocation^{1,2}

TABLE 3.4

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ³
Asset	262,200.9	270,406.9	256,040.2	273,422.3	277,200.6	270,736.3	256,040.2	244,295.0
Cash	8,207.5	10,462.9	15,485.2	11,228.2	11,578.9	14,698.8	15,485.2	14,704.3
Portfolio investment	255,273.6	260,002.9	240,110.5	262,034.2	265,596.0	255,694.9	240,110.5	229,040.9
Domestic securities	123,683.6	127,355.4	134,700.7	130,070.3	131,055.2	137,101.4	134,700.7	131,693.0
Shares	11,602.1	13,806.8	11,600.7	14,389.8	14,196.3	12,619.2	11,600.7	8,576.3
Mutual funds units	17,255.9	17,322.8	18,720.4	17,377.4	18,719.4	19,667.5	18,720.4	19,047.6
Public money market assets	4,149.4	2,887.7	2,206.6	3,306.6	2,539.7	2,329.6	2,206.6	2,772.4
Other public fixed-income	10,088.7	9,891.6	8,708.7	10,178.1	9,715.2	9,488.6	8,708.7	6,679.8
Private money market assets	26,850.7	28,483.2	37,486.9	29,522.6	30,711.7	35,565.7	37,486.9	35,621.5
Other private fixed-income	18,835.6	23,105.3	24,251.5	24,646.1	24,879.8	24,363.4	24,251.5	23,778.3
Spanish warrants and options	483.1	603.3	553.2	578.1	675.3	569.1	553.2	404.3
Repos	34,417.8	31,229.4	31,172.4	30,046.1	29,592.5	32,497.9	31,172.4	34,812.8
Unlisted securities	0.2	25.4	0.2	25.4	25.4	0.2	0.2	0.0
Foreign securities	131,590.0	132,647.4	105,409.8	131,963.9	134,540.7	118,593.5	105,409.8	97,347.9
Euros	118,871.5	118,664.1	94,205.2	118,953.6	120,459.4	106,110.8	94,205.2	88,498.1
Shares	8,925.1	11,418.0	10,772.1	12,823.3	14,247.4	12,735.6	10,772.1	8,045.8
Mutual fund units	15,986.0	23,414.2	13,149.1	22,849.5	23,440.2	16,876.9	13,149.1	10,466.4
Fixed-income	90,220.7	78,933.4	65,972.8	78,365.1	77,447.7	71,585.9	65,972.8	66,998.4
Foreign warrants and options	3,739.7	4,898.7	4,311.2	4,915.7	5,324.0	4,912.4	4,311.2	2,987.6
Unlisted securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	12,718.5	13,983.3	11,204.6	13,010.3	14,081.3	12,482.7	11,204.6	8,849.7
Shares	7,019.5	7,343.0	5,964.0	7,085.0	7,705.1	6,893.3	5,964.0	4,568.6
Mutual fund units	4,395.6	5,491.5	4,477.8	4,812.2	5,343.0	4,774.1	4,477.8	3,652.5
Fixed-income	1,204.8	1,011.7	631.1	978.0	888.4	675.9	631.1	534.2
Foreign warrants and options	97.2	136.0	130.8	134.2	143.7	138.4	130.8	93.6
Unlisted securities	1.4	1.2	0.9	1.0	1.1	1.1	0.9	0.8
Net balance (Debtors -Creditors)	-1,280.3	-58.8	444.5	160.0	25.7	342.5	444.5	549.8

1 Hedge funds are not included in these figures. The information is not available because hedge funds have different accounting regulation.

2 Provisional data in case of funds of hedge funds and hedge funds

3 Available data: January 2008.

Investment companies asset allocation

TABLE 3.5

Million euro	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
Asset	27,610.0	30,152.7	31,481.5	31,516.0	32,791.7	32,360.1	31,481.5	29,550.6
Cash	728.9	802.2	1,182.2	870.9	1,004.7	1,021.6	1,182.2	1,259.3
Portfolio investment	26,884.9	29,294.1	30,037.4	30,407.1	31,692.4	31,105.2	30,037.4	28,088.1
Domestic securities	13,851.1	15,553.8	17,075.3	15,929.3	15,905.8	16,841.4	17,075.3	16,899.0
Shares	5,906.5	6,727.3	6,173.6	7,050.5	7,191.8	6,528.1	6,173.6	5,168.6
Mutual funds units	941.2	1,095.0	1,362.3	1,143.6	1,309.5	1,392.5	1,362.3	1,321.6
Public money market assets	128.1	463.4	382.8	362.7	418.1	434.3	382.8	398.4
Other public fixed-income	897.0	678.2	710.2	737.3	802.0	755.0	710.2	529.9
Private money market assets	359.1	555.4	1,568.6	623.6	732.9	1,032.2	1,568.6	1,745.5
Other private fixed-income	397.3	554.8	620.8	571.5	534.9	548.8	620.8	636.4
Spanish warrants and options	15.3	19.7	22.1	21.1	23.0	25.2	22.1	24.7
Repos	5,206.2	5,459.1	6,234.1	5,418.1	4,892.7	6,121.4	6,234.1	7,070.2
Unlisted securities	0.3	0.8	0.8	0.8	0.8	4.0	0.8	3.7
Foreign securities	13,033.8	13,740.3	12,962.2	14,477.8	15,786.6	14,263.8	12,962.2	11,189.1
Euros	9,178.6	9,847.7	9,413.7	10,522.9	11,635.6	10,295.1	9,413.7	8,256.0
Shares	2,885.6	3,379.9	3,367.7	3,676.0	4,414.1	3,928.2	3,367.7	2,633.8
Mutual fund units	3,351.6	4,169.1	3,826.1	4,523.4	5,012.2	4,254.0	3,826.1	3,401.1
Fixed-income	2,755.8	2,041.5	2,006.7	2,061.5	1,984.2	1,877.3	2,006.7	2,024.0
Foreign warrants and options	185.7	257.2	213.1	262.0	225.1	235.7	213.1	197.1
Unlisted securities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	3,855.2	3,892.6	3,548.5	3,954.9	4,151.0	3,968.7	3,548.5	2,933.1
Shares	2,173.9	2,104.7	1,752.2	2,080.2	2,086.3	1,923.8	1,752.2	1,477.6
Mutual fund units	1,403.7	1,517.7	1,600.6	1,672.9	1,852.7	1,816.5	1,600.6	1,278.2
Fixed-income	270.0	234.8	183.2	188.3	199.7	219.5	183.2	167.6
Foreign warrants and options	7.5	11.3	12.5	13.6	12.3	8.9	12.5	9.5
Unlisted securities	0.1	24.1	0.0	0.0	0.0	0.0	0.0	0.1
Net balance (Debtors - Creditors)	-3.8	56.4	261.8	238.0	94.7	233.3	261.8	203.2

1 Available data: January 2008.

Financial mutual funds: number, investors and total net assets by category¹

TABLE 3.6

NO. OF FUNDS	2005	2006	2007	2006		2007			
				IV	I	II	III	IV	
Total financial mutual funds	2,705	2,822	2,926	2,822	2,872	2,919	2,920	2,926	
Fixed-income ²	624	606	600	606	609	606	604	600	
Mixed fixed-income ³	217	212	204	212	207	211	203	204	
Mixed equity ⁴	222	222	207	222	215	216	216	207	
Spanish equity	116	118	123	118	118	118	121	123	
Foreign equity ⁵	454	467	481	467	480	488	485	481	
Guaranteed fixed-income	211	220	251	220	232	237	241	251	
Guaranteed equity	514	559	590	559	577	586	589	590	
Global funds	347	418	470	418	434	457	461	470	
Funds of hedge funds ⁶	-	2	31	2	2	22	30	31	
Hedge funds ⁶	-	5	21	5	6	9	17	21	
INVESTORS									
Total financial mutual funds	8,450,164	8,637,781	8,053,049	8,637,781	8,740,972	8,755,921	8,467,203	8,053,049	
Fixed-income ²	3,071,656	2,960,879	2,763,442	2,960,879	2,933,505	2,881,128	2,869,191	2,763,442	
Mixed fixed-income ³	492,988	524,827	493,786	524,827	551,786	539,799	511,811	493,786	
Mixed equity ⁴	408,757	357,013	331,214	357,013	374,508	376,559	359,667	331,214	
Spanish equity	365,301	317,386	288,210	317,386	341,396	363,017	343,208	288,210	
Foreign equity ⁵	1,199,460	1,258,426	1,089,868	1,258,426	1,274,138	1,263,619	1,184,871	1,089,868	
Guaranteed fixed-income	455,237	497,540	549,108	497,540	518,940	541,442	540,637	549,108	
Guaranteed equity	1,849,626	1,783,867	1,715,144	1,783,867	1,771,469	1,766,834	1,754,596	1,715,144	
Global funds	607,139	937,843	822,277	937,843	975,230	1,023,523	903,222	822,277	
Funds of hedge funds ⁶	-	2	3,950	2	26	1,456	3,142	3,950	
Hedge funds ⁶	-	21	1,127	21	108	183	251	1,127	
TOTAL NET ASSETS (Million euro)									
Total financial mutual funds	262,200.9	270,406.3	255,040.9	270,406.3	273,412.8	276,600.4	269,907.1	255,040.9	
Fixed-income ²	123,890.7	116,511.9	113,234.1	116,511.9	116,963.0	116,344.7	118,489.4	113,234.1	
Mixed fixed-income ³	14,625.8	15,314.5	13,011.9	15,314.5	15,755.0	15,329.1	14,142.3	13,011.9	
Mixed equity ⁴	10,005.6	10,149.2	8,848.0	10,149.2	10,090.7	10,289.1	9,753.4	8,848.0	
Spanish equity	9,741.7	10,416.4	7,839.4	10,416.4	11,238.3	9,523.4	8,353.3	7,839.4	
Foreign equity ⁵	20,925.1	24,799.6	22,698.4	24,799.6	25,759.1	29,428.3	26,453.8	22,698.4	
Guaranteed fixed-income	13,442.0	14,484.8	17,674.4	14,484.8	15,179.1	15,810.4	16,291.2	17,674.4	
Guaranteed equity	45,839.8	44,796.6	42,042.1	44,796.6	43,998.9	44,140.0	43,365.6	42,042.1	
Global funds	23,730.1	33,933.3	29,692.6	33,933.3	34,428.9	35,735.4	33,058.2	29,692.6	
Funds of hedge funds ⁶	-	0.6	1,000.6	0.6	9.5	600.2	829.2	1,000.6	
Hedge funds ⁶	-	24.4	445.8	24.4	119.9	152.0	210.2	445.8	

1 Mutual funds that have sent reports to the CNMV (therefore mutual funds in a process of dissolution or liquidation are not included).

2 This category includes: Short-term fixed income, Long-term fixed income, Foreign fixed-income and Monetary market funds.

3 This category includes: Mixed fixed-income and Foreign mixed fixed-income.

4 This category includes: Mixed equity and Foreign mixed equity.

5 Until 2002 this category includes: Foreign equity and Foreign Equity Euro. From 2002 this category includes: Euro equity, Foreign equity Europe, Foreign equity Japan, Foreign equity USA, Foreign equity emerging countries and Other foreign equity.

6 Provisional data in case of funds of hedge funds and hedge funds.

Financial mutual funds: Detail of investors and total net assets by type of investors

TABLE 3.7

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
INVESTORS	8,450,164	8,637,804	8,058,126	8,741,106	8,757,560	8,470,596	8,058,126	7,695,366
Individuals	8,202,638	8,389,315	7,818,701	8,490,813	8,499,831	8,219,220	7,818,701	7,467,451
Residents	8,101,310	8,292,264	7,725,443	8,394,044	8,402,736	8,123,347	7,725,443	7,374,371
Non-residents	101,328	97,051	93,258	96,769	97,095	95,873	93,258	93,080
Legal entities	247,526	248,489	239,425	250,293	257,729	251,376	239,425	227,915
Credit Institutions	1,634	1,609	2,276	1,576	1,721	1,715	2,276	2,150
Other resident Institutions	244,223	244,980	235,298	246,819	254,123	247,752	235,298	223,905
Non-resident Institutions	1,669	1,900	1,851	1,898	1,885	1,909	1,851	1,860
TOTAL NET ASSETS (Million euro)	262,200.9	270,431.3	256,487.3	273,542.2	277,352.6	270,946.4	256,487.3	244,770.2
Individuals	193,948.6	201,411.0	190,980.6	202,506.4	204,173.3	200,464.5	190,980.6	181,871.0
Residents	190,753.2	198,330.5	188,210.0	199,482.9	201,266.3	197,507.1	188,210.0	179,203.8
Non-residents	3,195.4	3,080.5	2,770.6	3,023.5	3,086.8	2,957.4	2,770.6	2,667.2
Legal entities	68,252.3	69,020.3	65,506.7	71,035.8	72,579.1	70,481.9	65,506.7	62,889.3
Credit Institutions	4,253.2	5,318.0	5,920.9	5,569.0	5,422.3	5,116.4	5,920.9	5,746.2
Other resident Institutions	62,749.8	61,646.6	57,670.6	63,305.8	65,248.3	63,190.9	57,670.6	55,561.9
Non-resident Institutions	1,249.4	2,055.70	1,915.2	2,160.9	2,328.8	2,174.7	1,915.2	1,591.1

1 Available data: January 2008.

Subscriptions and redemptions of financial mutual funds by category¹

TABLE 3.8

Million euro	2005	2006	2007	2006		2007		
				IV	I	II	III	IV
SUBSCRIPTIONS								
Total financial mutual funds ²	169,807.0	194,787.4	180,943.6	46,864.6	52,761.5	44,063.4	42,610.5	41,508.2
Fixed-income	108,566.1	118,705.9	116,323.9	29,310.1	31,678.8	27,498.6	30,580.5	26,566.0
Mixed fixed-income	6,677.3	8,476.6	5,859.4	1,982.5	2,322.7	1,439.3	1,141.7	955.7
Mixed equity	2,065.2	2,783.6	2,749.8	708.7	908.8	753.2	635.6	452.2
Spanish equity	5,588.5	5,590.4	4,402.4	1,406.7	1,984.6	991.9	482.5	943.4
Foreign equity	14,006.2	17,662.3	16,631.5	4,850.4	5,518.9	4,925.4	3,215.9	2,971.3
Guaranteed fixed-income	6,923.9	6,126.2	9,161.3	1,798.7	2,073.6	1,915.3	2,191.3	2,981.1
Guaranteed equity	13,520.7	8,914.1	8,070.6	2,457.2	1,800.2	1,858.3	1,316.4	3,095.7
Global funds	12,459.2	26,528.3	17,744.2	4,350.2	6,474.0	4,681.2	3,046.3	3,542.7
Funds of hedge funds	-	0.6	1,071.2	0.6	8.9	614.0	232.8	215.5
Hedge funds	-	24.4	380.8	24.4	47.0	28.6	62.2	243.0
REDEMPTIONS								
Total financial mutual funds ³	155,304.2	198,600.1	202,827.4	52,565.8	52,566.6	45,164.4	48,647.5	56,448.9
Fixed-income	107,150.9	127,469.1	122,178.3	31,363.9	32,087.4	28,502.6	28,982.4	32,605.9
Mixed fixed-income	4,339.6	7,048.4	7,809.6	2,035.2	1,967.4	1,664.7	2,049.5	2,128.0
Mixed equity	2,602.5	3,644.7	4,023.0	1,166.2	1,023.0	893.9	999.2	1,106.9
Spanish equity	5,323.3	7,824.6	6,723.3	2,401.9	1,750.2	1,861.3	1,429.0	1,682.8
Foreign equity	11,390.2	16,490.9	20,073.1	3,852.6	4,986.4	4,010.5	5,242.4	5,833.8
Guaranteed fixed-income	7,014.0	5,029.3	6,430.6	1,444.6	1,452.0	1,369.5	1,897.1	1,712.0
Guaranteed equity	8,931.6	11,830.1	11,602.6	4,130.0	2,785.1	2,238.1	2,142.1	4,437.3
Global funds	8,552.1	19,263.1	23,986.6	6,171.5	6,515.1	4,623.8	5,905.5	6,942.2
Funds of hedge funds	-	0.0	65.9	0.0	0.0	1.6	11.1	53.2
Hedge funds	-	0.1	2.6	0.1	0.0	0.1	0.45	2.1

1 Estimated data.

2 For the fourth quarter 2007, mutual funds subscriptions in financial IIC reached 3.8 billion euro.

3 For the fourth quarter 2007, mutual funds redemptions in financial IIC reached 4.6 billion euro.

**Financial mutual funds asset change by category:
Net subscriptions/redemptions and return on assets**

TABLE 3.9

Million euro	2005	2006	2007	2006		2007		
				IV	I	II	III	IV
NET SUBSCRIPTIONS/REDEMPTIONS								
Total financial mutual funds	14,444.3	-4,524.5	-21,877.7	-6,469.2	222.7	-1,114.8	-5,995.1	-14,990.5
Fixed-income	1,445.5	-9,423.4	-5,852.4	-2,625.5	-415.0	-1,009.7	1,601.6	-6,029.3
Mixed fixed-income	2,349.6	1,539.2	-1,942.0	-54.4	355.9	-224.7	-909.6	-1,163.6
Mixed equity	-546.5	-854.7	-1,277.0	-460.0	-112.4	-141.0	-367.8	-655.8
Spanish equity	276.0	-2,219.4	-2,314.4	-986.0	242.4	-871.0	-940.2	-745.6
Foreign equity	2,652.4	1,133.8	-3,342.6	928.4	553.5	928.6	-2,007.2	-2,817.5
Guaranteed fixed-income	-354.4	1,018.9	2,714.6	353.5	621.7	623.8	294.6	1,174.5
Guaranteed equity	4,693.6	-3,021.1	-3,604.9	-1,817.2	-982.8	-479.7	-802.2	-1,340.2
Global funds	3,928.2	7,302.1	-6,258.9	-1,808.1	-40.6	58.9	-2,864.3	-3,412.9
Funds of hedge funds	-	0.6	1,005.5	0.6	8.9	612.3	221.7	162.6
Hedge funds	-	24.3	164.7	24.3	47.0	28.5	61.8	27.4
RETURN ON ASSETS								
Total financial mutual funds	11,670.2	12,733.7	6,517.0	5,516.1	2,784.2	4,303.9	-696.7	125.6
Fixed-income	1,837.6	2,260.2	3,073.5	726.6	831.1	747.3	723.6	771.5
Mixed fixed-income	620.3	606.6	271.8	238.4	140.9	145.9	-30.6	15.6
Mixed equity	1,053.4	984.2	261.5	378.7	163.0	258.2	-120.3	-39.4
Spanish equity	1,623.7	2,882.9	768.3	981.2	579.5	203.5	-229.8	215.1
Foreign equity	3,507.1	2,736.1	251.5	1,484.3	420.5	1,678.4	-942.1	-905.3
Guaranteed fixed-income	222.8	112.3	334.7	34.6	87.2	40.7	164.0	42.8
Guaranteed equity	1,635.5	1,995.2	1,105.8	923.7	242.0	694.2	25.0	144.6
Global funds	1,169.8	1,156.2	450.2	748.6	320.0	535.8	-286.3	-119.4
Funds of hedge funds	-	0.0	-9.6	0.0	0.0	2.3	-16.7	4.8
Hedge funds	-	0.1	0.2	-	0.8	3.6	-3.9	-0.3

Financial mutual funds return on assets. Detail by category

TABLE 3.10

% of daily average total net assets ¹	2005	2006	2007	2006		2007		
				IV	I	II	III	IV
MANAGEMENT YIELDS								
Total financial mutual funds	5.87	5.73	3.45	2.15	1.31	1.87	0.02	0.32
Fixed-income	2.31	2.51	3.32	0.67	0.89	0.84	0.79	0.85
Mixed fixed-income	6.18	5.30	2.98	1.89	1.22	1.27	0.11	0.44
Mixed equity	12.96	11.31	4.25	4.14	2.03	2.94	-0.78	-0.01
Spanish equity	20.10	30.10	9.14	9.65	5.77	2.54	-2.13	3.01
Foreign equity	22.82	13.82	2.78	6.75	2.09	6.42	-2.95	-3.19
Guaranteed fixed-income	2.45	1.67	3.25	0.44	0.78	0.46	1.22	1.02
Guaranteed equity	5.26	5.86	3.65	2.39	0.91	1.95	0.44	0.47
Global funds	7.41	4.84	2.57	2.58	1.28	1.88	-0.52	-0.07
Funds of hedge funds	-	ns	-1.36	ns	-0.31	0.96	-1.83	1.04
Hedge funds	-	ns	0.57	ns	1.47	4.50	-1.64	-0.69
EXPENSES. MANAGEMENT FEE								
Total financial mutual funds	1.07	1.04	1.00	0.26	0.26	0.27	0.25	0.24
Fixed-income	0.73	0.63	0.61	0.14	0.16	0.16	0.15	0.15
Mixed fixed-income	1.24	1.21	1.13	0.31	0.29	0.30	0.29	0.29
Mixed equity	1.69	1.63	1.54	0.42	0.40	0.40	0.39	0.39
Spanish equity	1.77	1.83	1.59	0.47	0.45	0.44	0.41	0.42
Foreign equity	1.80	1.78	1.70	0.49	0.43	0.48	0.41	0.41
Guaranteed fixed-income	0.77	0.75	0.62	0.18	0.17	0.17	0.17	0.16
Guaranteed equity	1.38	1.34	1.30	0.33	0.33	0.33	0.34	0.34
Global funds	1.41	1.26	1.16	0.37	0.32	0.35	0.25	0.26
Funds of hedge funds	-	ns	1.15	ns	0.37	0.29	0.42	0.43
Hedge funds	-	ns	1.39	ns	0.40	0.99	0.09	0.67
EXPENSES. DEPOSITORY FEE²								
Total financial mutual funds	0.10	0.09	0.09	0.02	0.02	0.02	0.02	0.02
Fixed-income	0.09	0.08	0.08	0.02	0.02	0.02	0.02	0.02
Mixed fixed-income	0.11	0.10	0.09	0.02	0.02	0.02	0.02	0.02
Mixed equity	0.11	0.11	0.10	0.03	0.03	0.03	0.03	0.03
Spanish equity	0.11	0.11	0.11	0.03	0.03	0.03	0.03	0.03
Foreign equity	0.11	0.11	0.11	0.03	0.03	0.03	0.03	0.03
Guaranteed fixed-income	0.09	0.09	0.08	0.02	0.02	0.02	0.02	0.02
Guaranteed equity	0.11	0.11	0.10	0.03	0.03	0.03	0.03	0.03
Global funds	0.09	0.10	0.10	0.03	0.03	0.03	0.03	0.03
Funds of hedge funds	-	ns	0.06	ns	0.04	0.01	0.02	0.02
Hedge funds	-	ns	0.33	ns	0.04	0.52	0.05	0.05

1 The % refers to monthly average total net assets for the Hedge fund category.

2 Instead of the depository fee, the figures for the Hedge fund category refers to the financial expenses.

ns: it is not significant.

Mutual fund quarterly returns. Detail by category

TABLE 3.11

In %	2005	2006	2007	2006		2007		
				IV	I	II	III	IV
Total financial mutual funds	5.00	5.59	2.73	2.28	1.11	1.65	-0.15	0.10
Fixed-income	1.53	1.95	2.71	0.63	0.72	0.65	0.63	0.68
Mixed fixed-income	5.00	4.18	1.93	1.58	0.94	0.96	-0.16	0.18
Mixed equity	11.85	10.34	2.69	3.78	1.71	2.57	-1.17	-0.40
Spanish equity	20.60	33.25	8.02	9.73	5.78	2.07	-2.42	2.53
Foreign equity	24.18	14.98	2.13	6.60	2.12	6.38	-2.80	-3.28
Guaranteed fixed-income	1.66	0.83	2.78	0.24	0.59	0.29	1.03	0.84
Guaranteed equity	3.95	4.66	2.44	2.12	0.56	1.62	0.13	0.12
Global funds	6.16	4.01	1.47	2.21	0.99	1.57	-0.70	-0.38
Funds of hedge funds	-	ns	-0.43	ns	-0.55	1.08	-2.14	1.22
Hedge funds	-	ns	0.84	ns	1.26	3.18	-2.20	-1.31

ns: it is not significant.

Management companies. Number of portfolios and assets under management

TABLE 3.12

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
NUMBER OF PORTFOLIOS								
Mutual funds	2,723	2,850	2,954	2,885	2,921	2,947	2,954	2,964
Investment companies	2,989	3,049	3,181	3,073	3,112	3,143	3,181	3,193
Funds of hedge funds	-	2	31	2	22	30	31	31
Hedge funds	-	5	21	6	9	17	21	23
Real estate investment fund	7	9	9	9	9	10	9	9
Real estate investment companies	6	8	9	8	8	9	9	8
ASSETS UNDER MANAGEMENT (Million euro)								
Mutual funds	262,200.9	270,406.3	255,040.9	273,412.8	276,600.4	269,907.1	255,040.9	243,271.1
Investment companies	25,486.0	28,992.7	30,300.0	30,293.3	31,523.9	31,125.9	30,300.0	28,470.4
Funds of hedge funds	-	0.6	1,000.6	9.5	600.2	829.2	1,000.6	1,023.9
Hedge funds	-	24.4	445.8	119.9	152.0	210.2	445.8	475.3
Real estate investment fund	6,476.9	8,595.9	8,608.5	8,781.7	8,929.4	8,905.3	8,608.5	8,676.3
Real estate investment companies	213.9	456.1	512.9	459.2	487.4	504.3	512.9	344.1

1 Available data: January 2008.

Foreign Collective Investment schemes marketed in Spain

TABLE 3.13

	2005	2006	2007	2006		2007		
				IV	I	II	III	IV
INVESTMENT VOLUME ¹ (Million euro)	33,614.7	44,102.9	37,092.7	44,102.9	45,113.8	50,141.4	44,847.4	37,092.7
Mutual funds	8,267.2	12,099.3	7,010.3	12,099.3	12,464.3	14,211.5	10,530.7	7,010.3
Investment companies	25,347.4	32,003.5	30,082.4	32,003.5	32,649.6	35,929.9	34,316.7	30,082.4
INVESTORS/SHAREHOLDERS	560,555	779,165	850,931	779,165	782,020	825,771	834,914	850,931
Mutual funds	104,089	144,139	142,782	144,139	158,900	176,884	158,925	142,782
Investment companies	456,466	635,026	708,149	635,026	623,120	648,887	675,989	708,149
NUMBER OF SCHEMES	260	340	440	340	354	362	397	440
Mutual funds	115	164	225	164	169	171	197	225
Investment companies	145	176	215	176	185	191	200	215
COUNTRY								
Luxembourg	161	189	229	189	190	196	210	229
France	47	83	122	83	90	92	105	122
Ireland	35	46	52	46	48	48	50	52
Germany	11	12	15	12	12	12	15	15
UK	5	6	12	6	9	9	11	12
The Netherlands	1	1	1	1	1	1	1	1
Austria	-	1	5	1	1	1	1	5
Belgium	-	1	3	1	2	2	3	3
Malta	-	1	1	1	1	1	1	1

¹ Investment volume: participations or shares owned by the investors/shareholders at the end of the period valued at that moment of time.

Real estate investment schemes

TABLE 3.14

	2005	2006	2007	2007				2008
				I	II	III	IV	I ¹
REAL ESTATE MUTUAL FUNDS								
Number	7	9	9	9	9	10	9	9
Investors	118,857	150,304	145,510	152,902	153,630	151,916	145,510	147,577
Asset (Million euro)	6,476.9	8,595.9	8,608.5	8,781.7	8,929.4	8,905	8,608.5	8,676.3
Return on assets (%)	5.35	6.12	1.27	1.31	1.10	1.53	1.27	0.42
REAL ESTATE INVESTMENT COMPANIES								
Number	6	8	9	8	8	9	9	8
Shareholders	256	749	843	754	769	661	843	839
Asset (Million euro)	213.9	456.1	512.9	459.2	487.4	504.3	512.9	344.1

¹ Available data: January 2008. In this case, the return on assets is monthly.

VI Legislative Annex (*)

(*) This Annex has been prepared by the CNMV Studies and Statistics Department.

New legislation of national scope promulgated since publication of the CNMV Bulletin for the fourth quarter of 2007 includes the following, in chronological order:

- **Circular 2/2007**, of 19 December, promulgated by the Comisión Nacional del Mercado de Valores (CNMV – the Spanish Securities Market Commission), approving model forms for notifying major holdings of directors and executives, transactions by issuers in own shares, and other forms. Official State Gazette of 10/01/2008.

The purpose of the Circular is to lay down the model forms of notification which must be used to send the corresponding information to the Spanish Securities Market Commission. These model forms were drawn up taking into account aspects of the obligations laid down by Sections 39, 43 and 47.4 of Royal Decree 1362/2007, of 19 October, promulgated pursuant to the Securities Market Act, 24/1988, of 28 July, in relation to transparency requirements of information on issuers whose shares are admitted to trading on an official secondary market or other European Union regulated market, and Section 9 of Royal Decree 1333/2005, of 11 November, on market abuse and the different parties under an obligation to notify, i.e. major non-director shareholders, directors, executives, and issuers themselves in the case of notification of transactions in own shares.

- **Circular 3/2007**, of 19 December, issued by the Spanish Securities Market Commission on Liquidity Contracts for the purpose of treating them as accepted market practice. Official State Gazette of 12/01/2008.

The Liquidity Contracts to which the Circular relates have the purpose of provision of liquidity by an intermediary which, acting on behalf of the issuer, engages in purchase and sale transactions in the official secondary market in shares of the issuer concerned. Taking into account that this activity could constitute market manipulation within the meaning of the Securities Market Act and Directive 2003/6/CE, the purpose of the Circular is to determine the limits and conditions under which transactions carried out pursuant to such contracts can be considered as accepted practice for the purposes of the said Section 83.ter.1.a) of Act 24/1988.

- **Circular 4/2007**, of 27 December, issued by the Spanish Securities Market Commission, modifying the model form of annual report on corporate governance of listed joint stock companies. Official State Gazette of 14/01/2008.

On 22 May 2006 the Board of the CNMV approved the Unified Code of Good Governance which listed companies must take as reference when submitting the annual report on corporate governance (hereinafter CGAR) for the 2007 and following financial years. The purpose of the Circular is to replace the model annual report on corporate governance of listed joint stock companies contained in Annex I of CNMV Circular 1/2004, of 17 March, with that laid down in Annex I, which must be completed in accordance with the instructions contained in it.

In order to follow various recommendations of the Unified Code it is necessary

that companies explain certain corporate governance practices in their CGAR. Application of the Unified Code consequently makes it necessary to make various modifications to and include new sections in the model report.

Since one of the basic principles of the Unified Code is the voluntary nature of compliance with recommendations, and listed companies are free to follow the said recommendations or not, completion of some of the new sections included in the model CGAR is not mandatory and it will only be obligatory to complete them in cases in which the company indicates that the associated recommendation has been complied with.

In those cases in which the recommendations of the Unified Code are not followed or are followed in part, the Company must include the appropriate explanations.

The Unified Code provides that listed companies are free to follow the recommendations on good governance or not, but when reporting on whether they comply with them or not they must abide by the meanings given by the Code to the concepts used in it to define them.

- **Circular 5/2007**, of 27 December, issued by the Spanish Securities Market Commission, regarding relevant events of Collective Investment Undertakings. Official State Gazette of 17/01/2008.

This Circular has a threefold purpose: to compile cases of relevant events of Collective Investment Undertakings which which were spread over different legislation (including Sections 24.2 and 26.4 of the Collective Investment Undertakings Act, 14.2 of the Regulations and 2.4 of the Ministerial Order of 6 July 1993), speed up their dissemination and clarify the obligations in this respect which foreign Collective Investment Undertakings must comply with.

- **Act 56/2007**, of 28 December, on Measures to Promote the Information Society. Official State Gazette of 29/12/2007.

Act 56/2007 contains a series of measures adopted for the purpose of developing the Information Society and convergence with Europe and between Autonomous Regions and Cities, set within the “Avanza Plan” approved by the Government in November 2005.

This legislation introduces provisions aimed at promoting the use of electronic invoicing and electronic means at all stages of contracting processes and guaranteeing electronic communication by users and consumers with undertakings which provide certain service of particular economic importance. It also covers the necessary legislative changes to promote the information society and electronic communications.

- **Order EHA/35/2008**, of 14 January, developing rules relating to the accounting of collective investment undertakings, determination of net worth, computation of risk diversification coefficients and certain aspects of collective investment undertakings whose investment policy consists of

reproducing, replicating or taking a stock exchange or fixed income index as reference, and authorising the Spanish Securities Market Commission to develop it. Official State Gazette of 22/01/2008.

Pursuant to the authorisation referred to, the CNMV distinguishes between financial statements of a public nature and those of a reserved nature. It provides that the public model forms must be used in annual financial statements and all those documents in which such statements are made public. With regard to reserved statements, the CNMV may publish combined reserved data as it considers appropriate for statistical purposes.

The Order adapts accounting and financial information standards of Collective Investment Undertaking by compartments or different classes of holdings and series of shares. It provides that diversification coefficients must be measured at compartment level and that in determining net worth each undertaking must indicate the portion attributed to each compartment or class of holdings or series of shares.

It also provides that a Collective Investment Undertaking pursues an investment policy which replicates a stock exchange or fixed income index when the profitability of the CIU does undergo significant deviations with respect to the reference index. The CNMV must establish the maximum permitted deviation from the reference index and the manner of calculating it.

- **Order EHA/114/2008**, of 29 January, regulating compliance with certain obligations of Public Notaries in the field of money laundering prevention. Official State Gazette of 31/01/2008.

The Order focuses on various requirements contained in the Regulations under Act 19/1993, of 28 December. It specifically lays down the manner in which Public Notaries must comply with obligations of: (i) identifying clients, individuals and legal entities, when they act both for their own account and through representatives; (ii) preservation of documents used in the identification of persons and verification of the truthfulness of information for a period of six years; (iii) notification of transactions relating to payment movements; (iv) compliance with internal control and communications procedures; and (v) non-disclosure to either the person executing the document or to third parties in the event that information is sent to the Executive Service or transactions are examined in the context of money laundering prevention legislation.

- **Circular 1/2008**, of 30 January, issued by the Spanish Securities Market Commission, on regular information from issuers with securities admitted to trading on regulated markets relating to half-year financial reports, intermediate management statements, and quarterly financial reports as appropriate. Official State Gazette of 15/02/2008.

One of the novelties of the Circular is the establishment in half-yearly forms of declarations of responsibility which, in accordance with Royal Decree 1362/2007, must be assumed by the directors of the issuer, whose names and positions must be clearly indicated in the half-yearly model forms.

In developing the regular information model forms, three types of format are established based on the nature of the issuer and applicable accounting standards: one general, one for credit institutions, and a third for insurance companies. Furthermore, the half-yearly model forms of individual financial statements are adapted to the new accounting standards.

A further novelty of the Circular relates to specifying the statistical information laid down by Royal Decree 1362/2007. In order to facilitate compliance and prevent the creation of new information forms it was decided to set out the statistical information in Chapter IV of the half-yearly information form.

Furthermore, the current quarterly information is replaced by intermediate management statements, unless the issuer voluntarily publishes quarterly financial reports.

- **Royal Decree 215/2008**, of 15 February, amending Section 59 of the Regulations under Act 35/2003, of 4 November, on collective investment undertakings, promulgated by Royal Decree 1309/2005, of 4 November. Official State Gazette of 16/02/2008.

The purpose of this Royal Decree is to give flexibility to the system of third party financing of Collective Investment Undertakings as a result of various obstacles having been generated to their proper functioning. The general limit of third party financing for real estate CIUs is less than the maximum financing limits under the system of public protected housing, 80% of the maximum legal price. Consequently, it is provided that real estate CIUs need not compute in their debt limits that deriving from any system of public protected housing. The limit is also clarified on indebtedness in order to resolve cash difficulties, established at 10% of assets falling due within 18 months.

- **Royal Decree 217/2008**, of 15 February, on the legal regime of investment firms and other entities which provide investment services and partially modifying the Regulations under Act 35/2003, of 4 November, on Collective Investment Undertakings promulgated by Royal Decree 1309/2005, of 4 November. Official State Gazette of 16/02/2008.

The purpose of this Royal Decree is to complete the transposition of Directive 2006/73/EC on organisational requirements and functioning conditions of investment firms. This Directive develops certain aspects of the MiFID.

The principles underlying the Royal Decree are modernisation of financial markets, strengthening investor protection and ensuring that the organisation of entities is adapted to the range of investment services which they provide.

In relation to the regime governing investment firms (IFs) one important novelty is specification of the concept of financial advice, distinguishing it from other types of recommendation.

With respect to the rules for authorisation of IFs a special system of authorisation is established for financial advisory undertakings. Furthermore, a special type of securities broker is recognised, authorised exclusively to receive and transfer orders without taking funds or financial instruments from their clients, with lesser Requirements. In order to speed up authorisation procedures, the requirement of a report from the CNMV Consultative Committee is also eliminated.

With respect to organisational requirements, the Royal Decree regulates organisational requirements in considerable detail, in aspects such as handling conflicts of interest, delegation of essential functions and investment services to third parties, and maintaining records of activities and transactions. The aim is thereby to seek greater legal certainty among financial intermediaries and facilitate the work of supervisory bodies.

The new legislation incorporates a broad catalogue of rules of conduct in the provision of investment services. In particular, broader information obligations to clients, the requirement to carry out a suitability test of clients before providing the service and establishing detailed rules when executing client orders. It should be indicated that the treatment given is different depending on whether the client is retail or professional.

- **Royal Decree 216/2008**, of 15 February, on own funds of financial institutions. Official State Gazette of 16/02/2008.

This Royal Decree transposes Community legislation and establishes provisions relating to credit institutions (Title One) and investment firms (Title Two). In the same manner as the three pillars of Basel II, for each of these Titles the Royal Decree firstly describes uniform rules and minimum requirements, secondly the system of supervisory review, and thirdly the information to be disclosed to the market. Measures are added which must be taken in the event of failure to comply with own funds requirements.

The provisions relating to credit institutions establish the items which must be included in their own funds, the treatment of different risks, particularly credit and counterparty risks, and the limits on major risks, i.e. those contracted with the same counterparty.

With respect to investment firms the Royal Decree fixes the minimum own funds which they must maintain. It adds that IFs must each year summarise and send to the CNMV their organisational requirements and risk assessment techniques and the mechanism for self-assessment of internal capital. They must furthermore each year prepare a "Solvency Report", although the CNMV may determine an increased regularity for disclosing certain data and information. This Royal Decree specifies the powers of supervision of IFs covered by the Securities Market Act.

- **Order EHA/596/2008**, of 5 March, regulating certain aspects of the legal rules governing the depositaries of collective investment undertakings and lays down the contents of position statements. Official State Gazette of 7/03/2008.

The order firstly deals with the general rules applicable to the function of supervision and oversight of CIU depositories, specifically providing for the cases of hedge funds and CIU CIUs. The general rules, amongst other aspects, specify that depositories must verify that transactions carried out by the management company or directors of the investment company on behalf of the CIU have been carried out on a market basis. They must also verify that transactions comply with the requirements, coefficients and limits laid down by applicable legislation and supervise calculation of the liquidating value of holdings in investment funds and shares in investment companies.

A second aspect of the Order is the function of custody and administration of CIU depositories. These are depositories responsible for custody (physical or in the form of book entry records) of all assets included in the net worth of the CIU. The administration function consists of collecting yields on assets and acting such that assets in custody preserve the value and rights corresponding to them.

Other aspects dealt with by the Order include specification of action by the depository on subscription and repayment of holdings in investment funds and definition of the internal procedure manual of the depository. Finally, the provisions are reiterated regarding position statements contained in the Ministerial Order of 30 July 1992 in order that it can be completely repealed.

