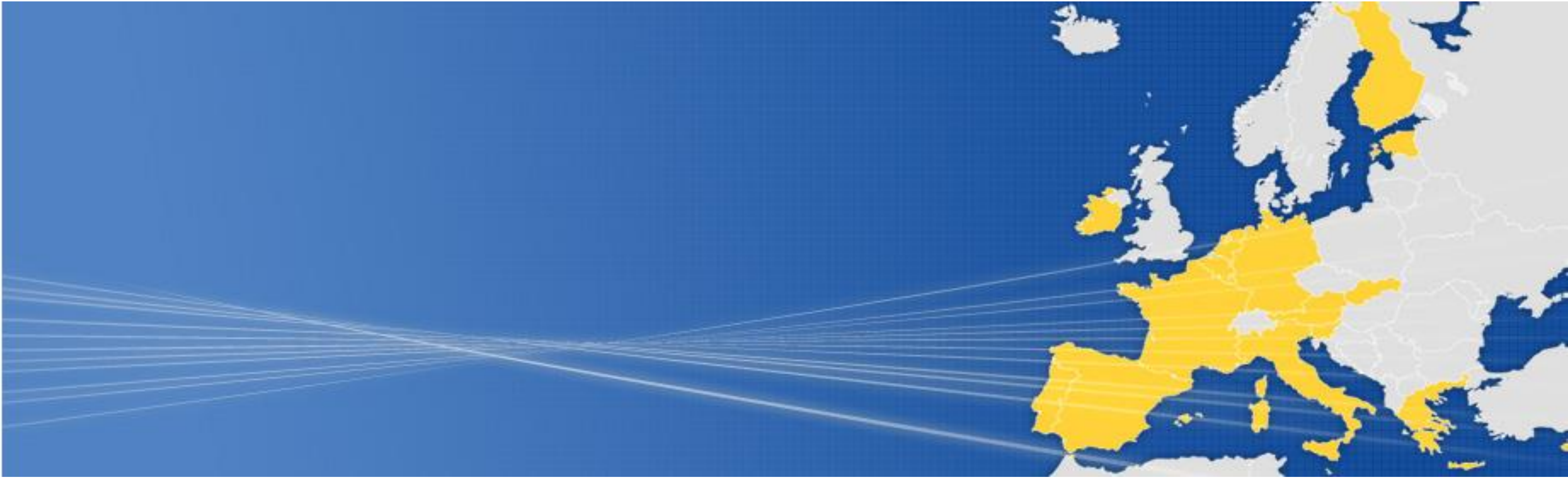


Conclusion of ESM financial assistance programme for Spain: an overview

31 December 2013

European Stability Mechanism
esm

The situation of Spanish banks has improved

- Process of **bank restructuring** is well underway
- **Transfer of impaired assets** to SAREB (asset management company) has been completed
- Steady **reduction of Eurosystem financing**: banks improved their access to private funding markets thanks to their holdings of ESM bonds and regained soundness
- Overall **positive earnings results** of Spanish banks over 2013
- Markets acknowledge **Spain's progress;** sovereign and corporate yields have dropped

The origins of Spain's banking crisis

- **Significant housing bubble** (house prices nearly tripled between 1997 and 2008)
- Construction boom fuelled by **excessive credit expansion**
- **External competitiveness** deteriorated during credit boom
- **Credit crunch** in the US markets precipitated the bursting of the bubble
- **Features** of crisis in Spain:
  - Sharp fall in property prices; loan losses for banks
  - Decline of aggregate demand and GDP, very high unemployment
  - High level of private debt (businesses and households)

Financial assistance granted

- Spanish authorities requested financial assistance for the **recapitalisation** of the banking sector on 25 June 2012
- **Assistance was approved**, along with bank and financial sector policy conditions, by the Eurogroup on 20 July 2012
- Financial assistance was granted to Spain for **up to €100 billion**
- This was designed to cover the **capital shortfall** of Spanish banks, with a safety margin
- The facility was transferred from the EFSF to the ESM in November 2012

Financial assistance provided by ESM

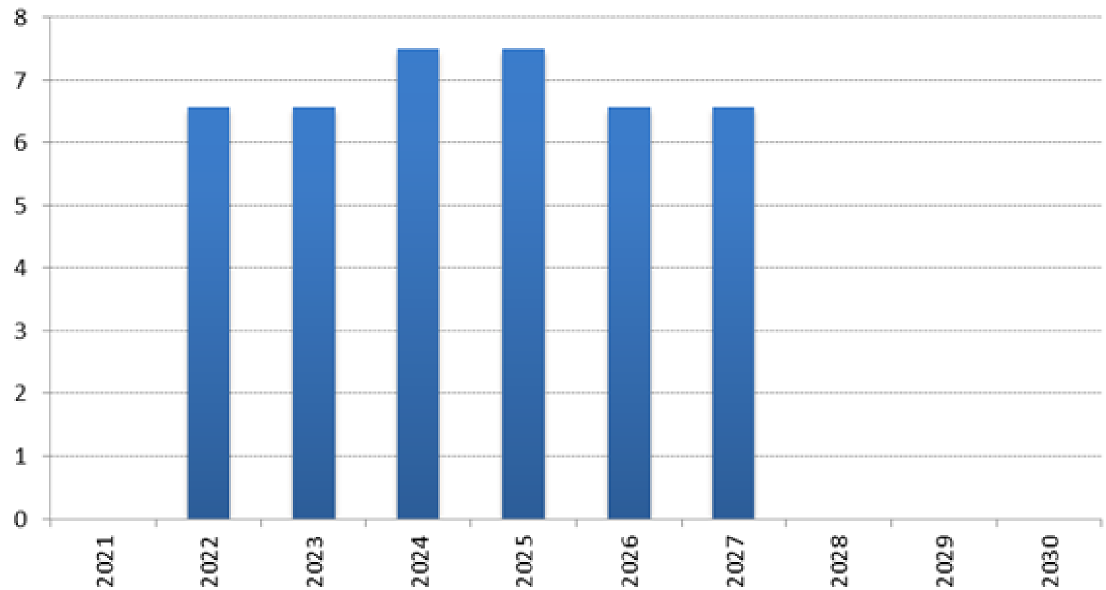
- First disbursement of over **€39 billion** was requested by Spain in December 2012 and carried out by the ESM; second disbursement of over **€1.8 billion** in February 2013
- Funds were disbursed in the form of **ESM bills and floating rate notes** with maturities ranging from 10 months to 3 years
- No further disbursement was requested by Spain, thus, **total amount** of financial assistance was **€41.3 billion**

Date of disbursement	Amount (€ billion)
11/12/2013	39.47
05/02/2013	1.86
Total	**41.33**

Loan repayment

- **Repayment** of loan principal by Spain starts in 2022 and ends in 2027
- **Average maturity of** loan tranches is 12.5 years

Spain's loan repayment profile



Unit: billion EUR
Source: ESM

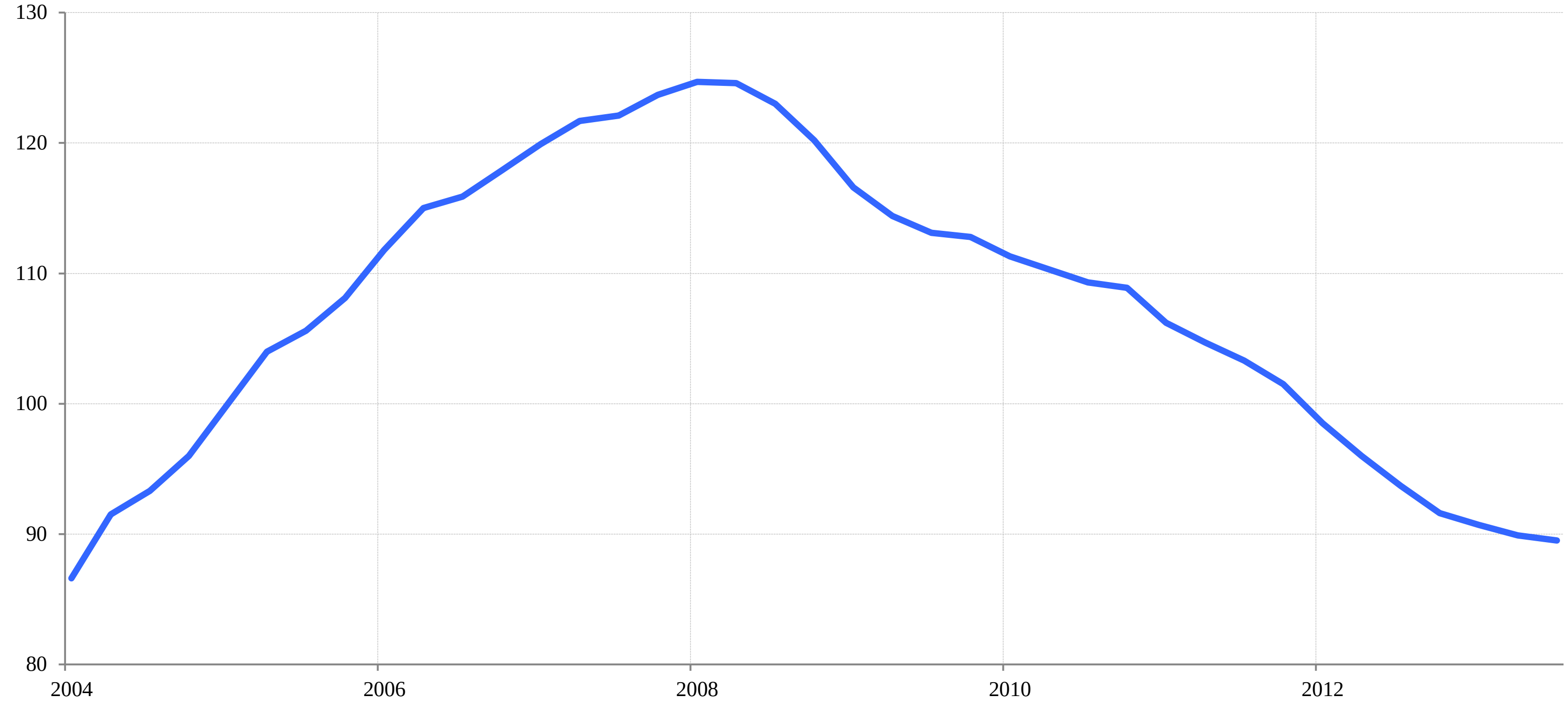
Conditionality of financial assistance

- **Bank-specific** conditionality
  - Identifying bank capital needs through asset quality review and stress-test
  - Recapitalisation and restructuring of weak banks
  - Segregation and transfer of impaired assets to SAREB
- **Sector-wide** conditionality to strengthen banking sector as a whole, including:
  - Regulatory capital targets
  - Improved bank governance rules
  - Upgrade of reporting requirements
  - More effective supervisory procedures

Programme success: exit without further external financial assistance

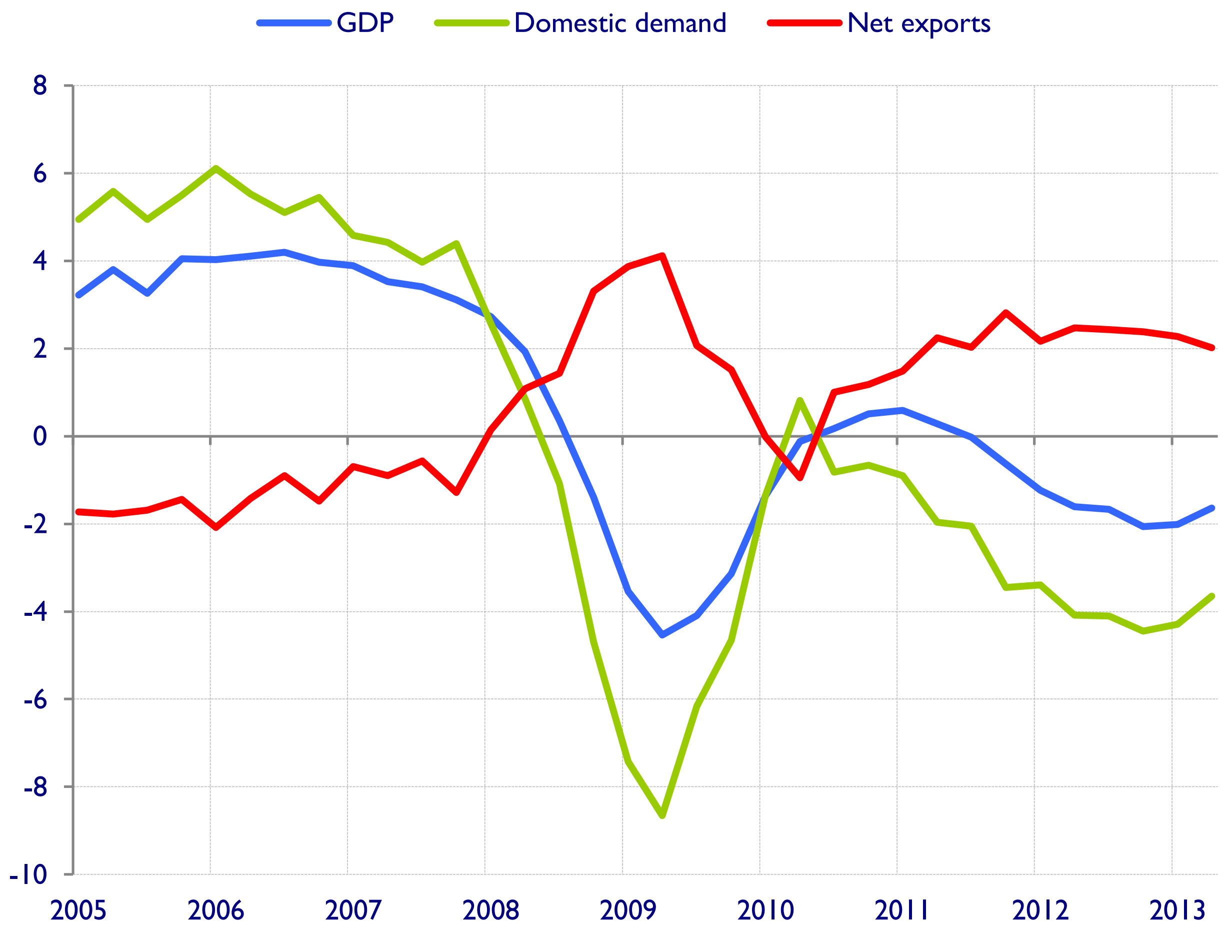
- Five successful reviews by European Commission and ECB with no delays or setbacks
- Findings during 5th review (Dec. 2013) confirm achievements:
  - Bank **restructuring is progressing well**
  - Banks are **refocusing their business models** on retail and SME lending
  - Banks' **financing structure has improved**: access to private funding markets is comfortable and bank deposits are rising
  - 10-year sovereign **bond yields down about 350 bp** since start of the programme
- Economic recovery is starting to gain momentum; **GDP is expected to grow in 2014**
- Spanish decision of a exit **without further financial assistance** supported by EC and ECB

The housing market is correcting: prices have fallen substantially since their peak



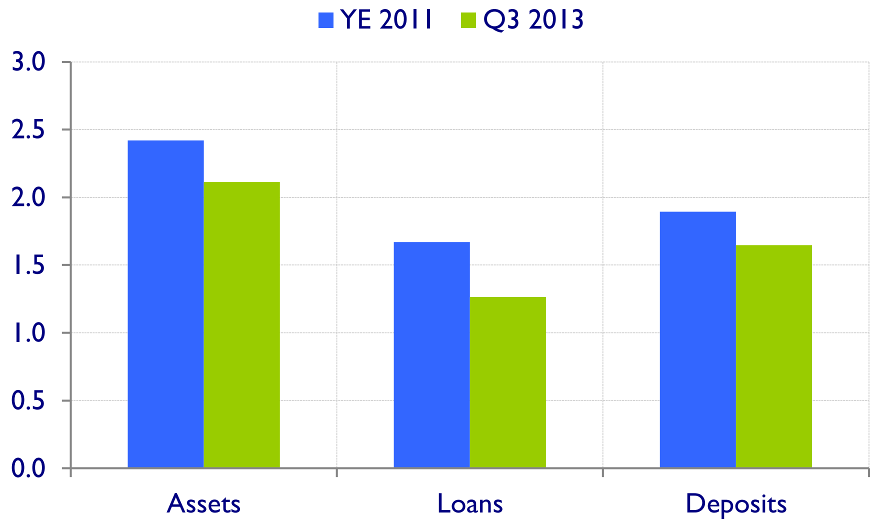
Unit: 2005Q1=100
Source: Ministerio de Fomento
Note: House Price index

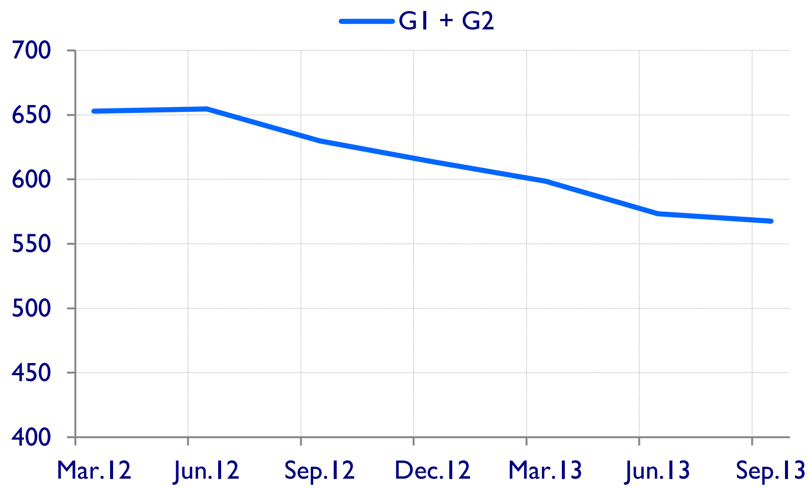
Net exports are contributing positively to GDP growth



Unit: annual % changes
Source: INE
Note: The figures for internal demand and net exports are contributions to growth in percentage points
Latest observation: Q2 2013

The restructuring of the banking sector





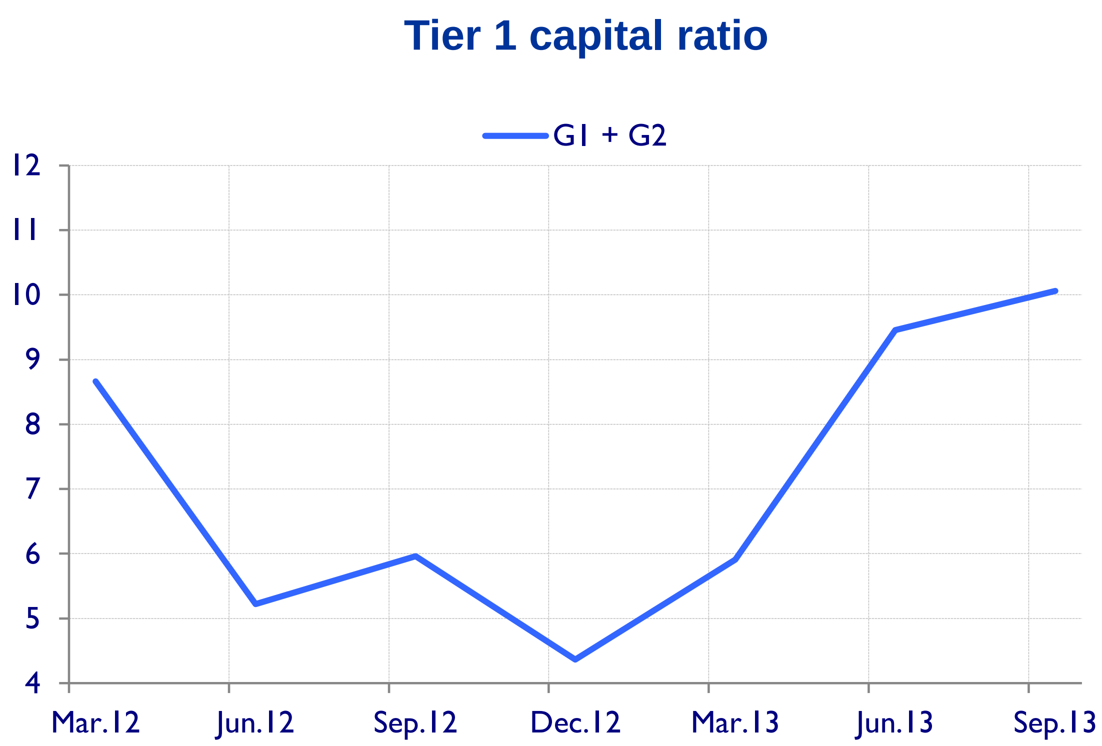
Total assets

- From 2011, the Spanish banking sector started its **restructuring** through a deleveraging of its assets (-13%), loans (-24%) and deposits (-13%)

Unit: Upper chart: Trillion EUR. Lower chart: Billion EUR
G1 and G2 are Group 1 and 2 recapitalised banks
Source: Banco de España

European Stability Mechanism

Banks’ capital has strengthened



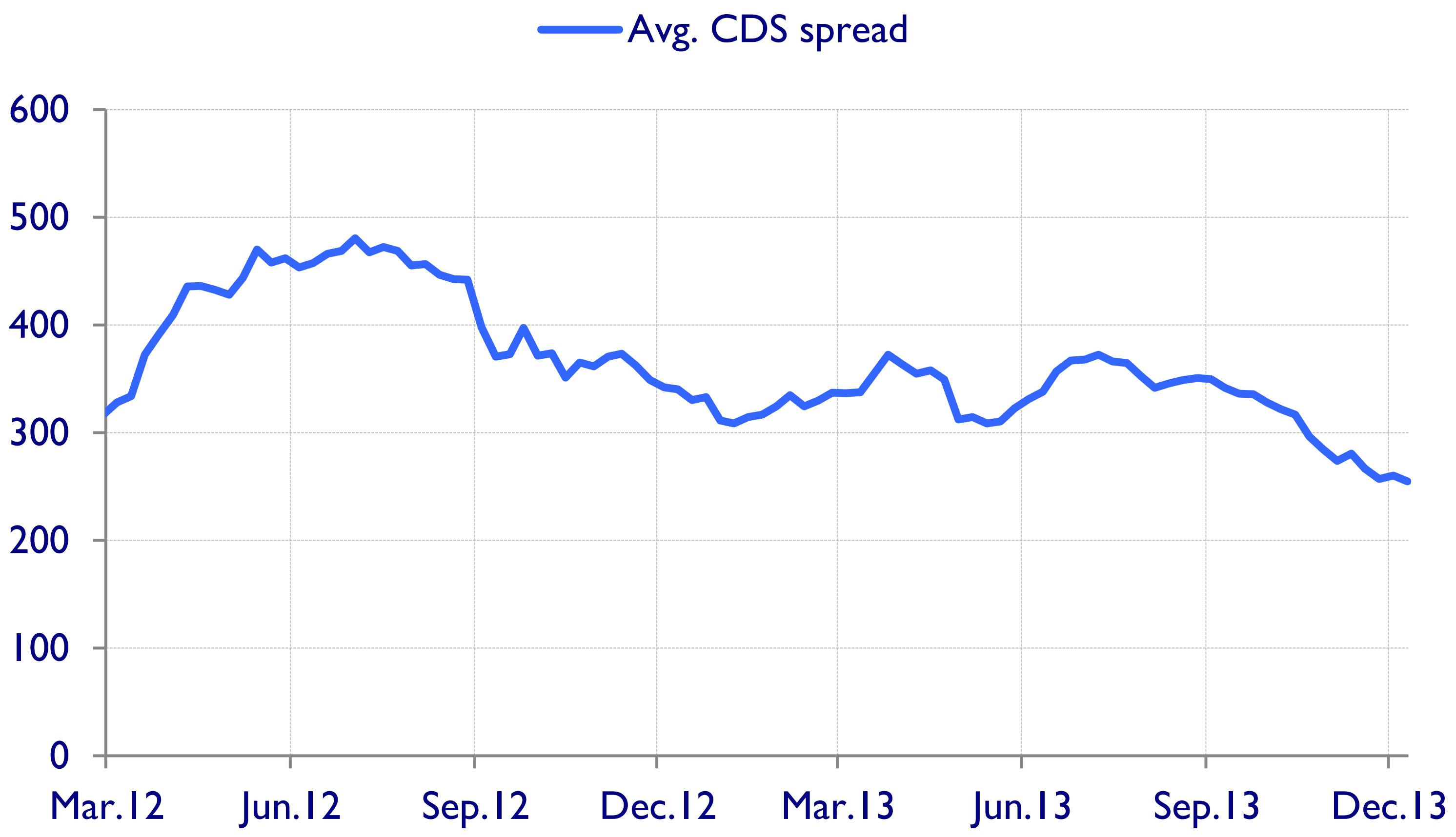
- At end-September 2013, all major banks exceeded the minimum Core Tier 1 capital ratio (EBA Definition) level of 9%

Unit: %
G1 and G2 are Group 1 and 2 recapitalised banks
Source: Banco de España

European Stability Mechanism

Risk in the banking sector is significantly lower

- The risk premium of the Spanish banking sector, measured by CDS spreads, has decreased more than 230 basis points since the second half of 2012



Unit: Basis points
Source: Bloomberg
Note: Average CDS spread of Banco Santander, BBVA, Banco Popular, Banco de Sabadell, Bankinter,

Summary: successful bank restructuring paves the way for real economy rebound

- ESM support has allowed Spain to **recapitalise and restructure** troubled banks
- Advances in **structural reforms and fiscal consolidation** have been made
- Unemployment is still high, but the **trend** seems **to have finally reversed**
- Spain has regained international competitiveness; **net exports** are overperforming
- **GDP is projected to grow** by 0.5% in 2014 and 1.7% in 2015
- Spain has the potential to become a **real growth engine** in Europe in the medium term

European Stability Mechanism

Next steps: Post-programme monitoring

- ESM is required by its Treaty to establish an "**early warning system**" to assess the repayment capacity of a beneficiary country
- Therefore the **ESM will monitor Spain** until the loan has been fully repaid in 2027
- This does **not entail any new conditionality** for Spain
- The ESM will closely collaborate with the **European Commission** in liaison with and the ECB, as they conduct their own monitoring process

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