

SPANISH DEPRESSION

There is no signal of economic recovery for Spain, not even in the long term. All the indicators point towards a protracted and extremely deep recession. The rise in the unemployment count shows numbers which are seriously worrying, virtually every sector of the economy continue to contract, the government balance is progressively worsening and in spite of the series of fiscal initiatives taken to rescue the economy, there seems to be nothing which can prevent the economy to fall apart.

Nothing left

The GDP contraction over the fourth quarter of last year was slightly less than expected, at -1% (-3.8% at an annual rate). Far from being interpreted as a positive signal, the decomposition of the contraction shows the depth of the crisis. Private consumption has contracted over the fourth quarter of 1.4% QoQ. Investments continue to be drastically scaled down with the residential component down -5.7% QoQ, after the already sharp contractions of the last three quarters. Nonetheless, the most sharp downturn was, as predicted, in productive investments which passed within a quarter from -0.6% to -6.3%, with the equipment goods component at a record contraction of -7.5%, the worst in more than a decade but likely to be followed by similar numbers over the coming months. As we already mentioned in our previous analysis, the crisis hitting Spain is not anymore a real estate and construction sector affair but it is instead a total collapse of the economy which has awfully spread out to virtually all productive sectors. If the final GDP contraction seems less bad than the contractions observed in other economies is only due to a positive net trade contribution, in turn resulting from the fact that the dreadful fall in exports (-10.1% QoQ) was more than offset by an even worse drop in imports (-11.9%).

The decline of both private consumption and imports is evidently the result of an abrupt arrest of households spending. This might be justified by precautionary saving based on expectations that the economic outlook will not improve in the near future, but it is mostly the result of the already felt reduction in household income, with employees nominal remuneration slowing in the fourth quarter from 4.4% to 1.6%, mostly as a result of the reduction in the level of unemployment. As a result, and in line with the evolutions in other parts of Europe, durable goods in general, and the automotive sector in particular are badly hit. This represents further bad news for an economy whose automotive industry makes up to one-fifth of the country's exports and 6% of GDP.

Overall, the steady fall in external demand and the further tightening of Spaniards' pockets should continue to weight on growth until the end of the year. We expect annual GDP growth at -2.7%, with fixed capital accumulation receding of roughly 15% and private consumption in the contraction zone for most of the year. Unemployment rate will further increase to almost 18% of the active population.

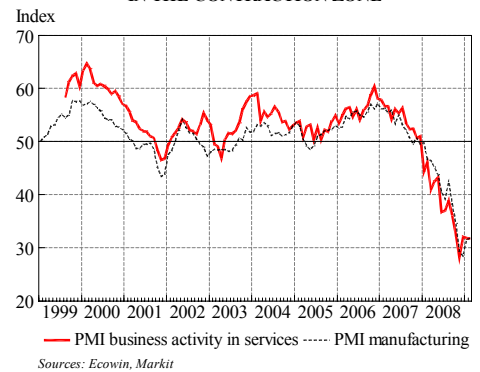
More troubles ahead for the Spanish banks

According to recent estimates, the Spanish banking system would have on its balance sheets €50bn of property assets, mostly as a result of the take-over of three of the largest real estate company of the country: Colonial, Martin-Fadesa and Metrovacesa. The take-overs of the previous months were the point of the iceberg represented by the unsustainable amount of lending to builders and real estate developers. Loans to developers make up to more than 20% of total bank lending; if we add lending to real-estate related activities and households mortgages the amount gets close to 70% of total lending.

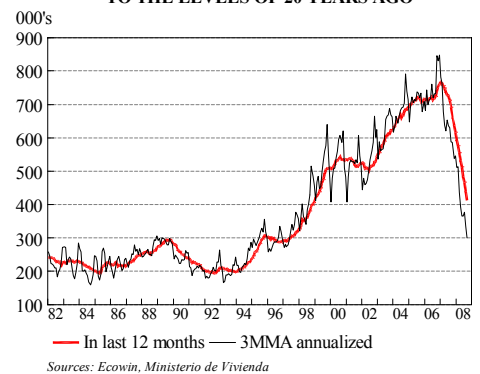
Big part of the pool of assets which is forcedly transferred to the balance sheets of financial institutions is constituted by more than 1 million unsold house. That easily explains the will of investors to withdraw from the bank's real estate funds, first on the list Santander's Banif Inmobiliario, the country's largest real estate fund, with requests of withdrawal equal to 80% of its overall capital, likely to force the bank, in spite of its recent attempts to freeze payments, to sell its assets at fire-sale prices in order to repay investors. The enormous amounts of depreciating real estate assets on the banks' balance sheets, together with the mounting amount of NPL are set to put the Spanish banking system in serious troubles, to further tighten lending and, in turn, to worsen the economic recession which is hitting the Spain.

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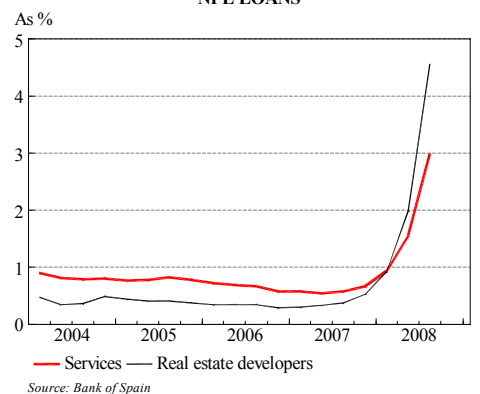
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NEW HOUSING SET TO FALL
TO THE LEVELS OF 20 YEARS AGO



NPL LOANS



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