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Summary of Government Interventions
Spain

Overview

In order to address the liquidity problems adversely affecting banks' lending to the economy in Spain, the Spanish government has adopted special measures which take into account national particularities of the banking market in Spain while ensuring the coherence necessary to maintain a level playing field for all European banks. The measures adopted in Spain include:

- state guarantee scheme covering against remuneration, the issuance of notes, bonds and obligations admitted to the official secondary market in Spain;
- extended coverage of bank deposit guarantees; and
- creation of the Financial Assets Acquisition Fund managed by the Spanish Treasury to purchases top quality financial assets of Spanish credit institutions and SPVs to enhance flow of credit to companies and individuals.

In addition, in March 2009, Spain announced various measures including a EUR 38bn stimulus package to cushion the effects of the global financial crisis on the real economy. The stimulus package includes EUR 6bn in tax cuts, the provision of EUR 4bn of liquidity to credit-strapped companies and households and an extra EUR 11bn will be spent on public works.

State guarantee scheme

State guarantee for finance transactions

The Spanish Government has adopted a State guarantee scheme under which unconditional and irrevocable state guarantees are available to guarantee transactions closed prior to 13 October 2008. The guarantee scheme is temporary and the guarantees are available until 31 December 2009. Under the scheme, the Spanish government may grant state guarantees to all credit institutions that were residents in Spain as of 13 October 2008 or to subsidiaries of foreign entities provided they have substantial operations in Spain.

The State guarantees may be granted in connection with debt issuance (issues in Spain of promissory notes, bonds and debentures by way of individual transactions or issue programs, non-subordinated debt or debt which is not secured with any other type of guarantees, in each case admitted to the official secondary market in Spain) and other banking instruments. While the maturity of the financial instruments would be in principle between three months and three years, guarantees could be extended to instruments with a maturity of up to five years in exceptional circumstances, with a favourable prior report of the Bank of Spain. The guarantee will only secure payment of the principal and ordinary interests of the secured obligation.

The government will charge a fee dependent on the type of secured obligation and the issuer and payable upon the issuance of a guarantee.

The Spanish Government has decided to distribute the maximum amount to be guaranteed each year to the applicants pro rata according to their market share as shown in the Statistics Bulletin of the Bank of Spain. Guarantees given from the 2008 Budget's account have been granted by 31 December 2008.

The scheme's overall budget was initially capped at EUR 100bn but with a possibility to increase it to EUR 200bn, if the market conditions require. Only solvent banks have access to the guarantee scheme.

On 23 December 2008, the scheme was approved by the European Commission for a period of six months. (The EU press release is available here.) http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/2049]

Bank deposit guarantee

By the Royal Decree 1642/2008 of 10 October 2008, the Spanish government extended the coverage of its deposit and investment guarantees from EUR 20,000 to EUR 100,000 per depositor and institution.

Government Intervention Package

Financial Asset Acquisition Fund

Spain has set up a Financial Asset Acquisition Fund ("**FAAF**") of up to EUR 50bn (USD 67.23bn) to facilitate medium-term funding of banks through the purchase of high quality financial assets issued by credit entities and securitisation funds and backed by credit granted to individuals, corporations and non-financial institutions. FAAF has been created under the Royal Decree-Law 6/2008 and the Order EHA/3118/2008 as an entity with no legal personality, controlled by the Spanish Treasury through a management board and an executive committee which together decide on the investments of FAAF and the characteristics and conditions of the asset purchases. It has been decided that FAAF would acquire the assets through an 'adverse' auction process.

To ensure diversification of assets purchased by FAAF:

- a portfolio of assets cannot hold more than 10 per cent. of securities issued by the same issuer;
- the transactions entered into with any financial institution cannot make up more than 10 per cent. of the portfolio of the reverse repurchase agreements;
- for each group of assets the maximum amount to be allocated to a financial institution shall be the lower of the following:
  - 10 per cent. of the maximum volume to be acquired by FAAF in the relevant auction; and

- the product of 2.5 multiplied by the entity's credit share, as published by the Bank of Spain before the calling of the auction, and by the maximum volume to be acquired by FAAF in the auction.

- 25 per cent. of the total volume awarded in the auctions (the "non-competitive tranche") is reserved for the institutions contributing to new loans to non-financial companies and households.

The first auction - for repurchase orders, took place on 20 November 2008 in accordance with the following conditions:

- the maximum effective amount to be acquired by FAAF not to exceed EUR 5bn;
- asset acquisition to be executed in combined spot and forward sales, with maturity of two years and annual interest payments;
- assets to include mortgage bonds, asset securitisation bonds and mortgage securitisation bonds, backed by credits granted to individuals, companies and non-financial entities, issued after 1 August 2007 and with a credit rating of at least AA (or equivalent);
- each financial institution allowed to present a competitive or a non-competitive offer, for a minimum amount of EUR 3m.

The second auction – for outright orders, took place on 11 December 2008, in accordance with the following conditions:

- the maximum effective amount to be acquired by FAAF not to exceed EUR 5m (unless the maximum amount due for the first auction has not been awarded, then the excess accrues in the second auction);
- asset acquisition to be executed as a firm cash purchase;
- assets to include mortgage bonds and asset securitisation bonds backed by newly issued mortgage bonds (*Cédulas hipotecarias* and *MBS*) with a AAA rating or equivalent, issued after 15 October 2008 and maturing within three years;
- each financial institution could present a competitive or a non-competitive offer, for a minimum amount of EUR 3m.

Two subsequent auctions took place on 20 January 2009 (repurchase orders) and 30 January 2009 (outright orders). The results of all the auctions are available on: http://www.fondoaaf.es/EN/Subastas.htm

The 30 January 2009 auction took the government's total bank asset purchases to EUR 19bn since November 2008.

Until 31 December 2009, the government may acquire equity holdings in credit institutions resident in Spain to reinforce their regulatory capital ratios. This new measure is on top of the EUR 30-50bn fund the Spanish government had already set up to buy bank assets, designed to run concurrently with and to complement the European Central Bank's liquidity facility and so to enable banks to continue lending to businesses and individuals.

On 27 January 2009, Spain's government confirmed it had no plan to buy up toxic bank assets but was prepared to inject capital into its banking system if necessary.

Notable developments with commercial banks (and other key financial players)

Rise in bad loans

Bad loans rose by 15.3 per cent. in January, the sharpest monthly increase since property group Martinsa Fadesa filed for administration in July.

Although Spanish financial institutions have very little exposure to international toxic assets, credit quality is deteriorating because of the collapse of the construction and property sectors and soaring unemployment.

Banks encouraged to merge

On 13 March 2009, the Spanish Economy Minister indicated that the Spanish government would be prepared to recapitalise healthy banks but those with serious solvency issues should seek a merger rather than state aid. Banks would get capital injections from the privately-funded Deposit Guarantee Fund which has EUR 7.2bn in bank contributions, but the government may nevertheless end up having to contribute some funds for recapitalisation.

Regional banks mergers

Prediction has been made of mergers between Spain's weaker banks, mainly in relation to unlisted *cajas* controlled by regional governments due to increasing ratio of bad loans in their real estate lending portfolios and not enough capital to deal with non-performing loans. Credit rating agencies downgraded many Spanish institutions due to "fairly fast deterioration" in asset quality, amongst those are: Caja de Ahorros del Mediterraneo, Caixa Sabadell, Caja de Ahorros de Castilla la Mancha, Cajasur and Caixa Penedés.

Six banks in the Castilla y Leon region including Caja Espana, Caja Duero, Caja de Burgos, Cajacirculo, Caja Segovia and Caja de Avila, El Norte de Castilla, have been reported to be in talks to consolidate operations by pooling resources and investments but keeping their independent regional identities. *Cajas* cannot be bought or sold but they may sell assets or consolidate by merging with other savings banks within the same region under current Spanish legislation.

Banco Santander

On 10 November 2008, Banco Santander announced an increase in its share capital in nominal amount of EUR 799,405,940 by means of an issuance of 1,598,811,880 new ordinary shares, of the same class and series as the outstanding shares and with pre-emptive subscription rights for the existing shareholders; the issue price of the new shares to be EUR 4.5 per share with the total amount of the issue being EUR 7,194,653,460. The transaction was fully underwritten.

The purpose of the share capital increase was to improve Banco Santander's core capital ratio. The terms and conditions of the capital increase and the procedure for the subscription for new shares in Spain, the United Kingdom, Portugal and Italy are set forth in the share securities note of the share capital increase which was registered with the Spanish Securities Market Commission ("**CNMV**") on 11 November 2008.

On 28 January 2009, Sovereign Bancorp Inc. shareholders approved the acquisition by Banco Santander of the outstanding common stock of Sovereign Bancorp Inc. not yet owned by Banco Santander.

On 16 February 2009, Banco Santander announced that its Banif Inmobiliario Fund FII, the largest property fund in Spain, could not meet an avalanche of redemptions. The bank said that it asked the stock market regulator for permission to suspend payments for up to 2 years. Clients holding 80 per cent. of the fund (EUR 2.62bn) have asked to redeem their investments but Banco Santander said the property fund lacked the cash to do so.

On 31 March 2009, Banco Santander agreed to sell its 32.5% stake in Cepsa, an important company in the Iberian energy sector, to International Petroleum Investment Company, the Abu Dhabi state enterprise which is responsible for all foreign investments in the oil and chemicals sector. The sale of the industrial stake reflects the bank's intentions to focus on their core retail and commercial banking activities.

The Chief Executive of Santander announced on 3 April 2009, that the Bank is comfortable with its position in the domestic banking market and has no immediate plans to buy mid-sized banks.

La Caixa

Spain's largest savings bank La Caixa is planning to issue a 3-year senior bond in the first sale to be guaranteed by the government with BNP Paribas, HSBC, JP Morgan, SocGen and La Caixa itself supposedly managing the deal to be rated triple-A by Moody's Investors Service and Fitch Ratings and AA+ by Standard & Poor's.

Bankinter SA

Bankinter is planning a three-year EUR 5bn bond issue. The bank has appointed itself, Barclays Capital, Calyon, Deutsche Bank and Banco Santander to manage the bond issue, which is to be guaranteed by the Spanish government. Guidance has been refined to mid-swaps plus 76 bps, at the tight end of an initial range of 76 to 79 bps.

Caja de Ahorros del Mediterraneo plans to issue a government-guaranteed three-year euro benchmark bond and Banco Popular and Banco Pastor have also been reported to plan government-guaranteed debt issuances.

Caja Madrid

According to Standard & Poor's, Caja Madrid may be the first Spanish bank to stop interest payments to mortgage-backed bond investors. In December 2008, defaults on mortgages in the bank's EUR 1.8bn of mortgage-backed bonds rose to almost 7%, close to the 8% level that will force the lender to halt payments to junior debt holders, Standard & Poor's said.

Banco Sabadell SA

On 4 February 2009, Banco Sabadell refused to use an option to redeem a subordinated bond issue because refinancing the debt would be too expensive.

Caja Castilla La Mancha

On 29 March 2009, the Spanish Government and the Bank of Spain proceeded with the first major bank rescue in the current financial crisis, by seizing Caja Castilla La Mancha. The Bank of Spain pledged a loan to Caja Castilla La Mancha, backed by a state guarantee of up to EUR 9bn. The Bank of Spain removed the savings bank's directors and replaced them with central bank nominees. The Spanish government reported that Caja Castilla La Mancha remained solvent but had liquidity problems.

European Investment Bank Loan

The European Investment Bank (EIB) granted a €500 million loan to the Instituto de Crédito Oficial (ICO) on the 26 March 2009. The loan is intended to support SME projects in the industrial, tourism and service sectors. The loan may be used to finance both fixed and intangible assets.

Other developments

Credit rating downgrade

On 19 January 2009, Standard & Poor's cut Spain's long-term sovereign credit ratings to AA+ from AAA, with a stable outlook.

Short selling

On 22 September 2008, the National Securities Markets Commission (the "**CNMV**") issued a resolution which entered into force on 24 September 2008, requiring holders of short positions in listed financial institutions to disclose their holdings exceeding 0.25 per cent. of the relevant institution's equity. A 'short position' is defined for these purposes as the net result of all positions in financial instruments, including shares and any derivative that has them as underlying, which give the firm or person a positive (profit) exposure to downward movements in the price of the shares of the specified issuers. Naked short-selling is banned in Spain pursuant to the Exchange Regulations of 1967. The disclosure obligation will remain in force until the CNMV is satisfied that there is no longer a requirement for it.

The affected financial institutions include Banco Bilbao Vizcaya Argentaria, Banco Santander, Bankinter, Banesto, Banco Sabadell and Banco Popular.

Government-backed Bonds

At a press conference on 27 March 2009, Finance Minister Pedro Solbes proposed a government plan to improve the guarantees it provides on government-backed bonds. Solbes suggested that the government will pay interest to investors after a bank defaults and until the debt is repaid.

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