

Sareb: socio-economic impact







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Scope



Scope

Purpose of the report

The Management Company for Assets Arising from the Banking Sector Reorganisation (Sareb) was created in November 2012 as part of the Spanish banking sector's restructuring and recapitalization. Sareb's creation was included in the agreement over financial assistance arranged in June 2012 between the Spanish authorities and the European Commission, with the participation of the International Monetary Fund and set out in the Memorandum of Understanding on Financial-sector Policy Conditionality (the "MoU").

Sareb was set up with the mission of managing efficiently and divesting in an orderly fashion the portfolio of financial and real estate assets of the nine banks that received public support (BFA-Bankia, Catalunya Banc, Novagalicia, Banco Gallego, Banco de Valencia, BMN, Liberbank, Caja 3 and CEISS).

In its first five years of operation, Sareb has endeavored to carry out its business with rigor and professionalism, striving to make a sustainable and responsible contribution to Spain's economic and social recovery, and minimize the impact on taxpayers. The purpose of this report, prepared by EY at Sareb's request, is to analyze Sareb's economic and social impact in Spain in the 2013-2017 period.

This document provides a description of the scenario before and after Sareb's creation regarding the outlook for certain macroeconomic indicators, and identifies and describes the main socio-economic impacts of Sareb's activity from 2013 to 2017.

The contents were prepared using the following information sources:

- ▶ Public information from official organizations (sourced in each case)
- ▶ Financial, purchasing and corporate information of Sareb⁽¹⁾ from 2013 to 2017⁽²⁾
- ▶ Information obtained applying the input-output methodology to calculations based on a table of symmetrical inputs and outputs that represent the socio-economic interrelationship among branches of economic activity. This approach is used to measure an activity's multiplier effect on its value chain in order to obtain its indirect and induced contribution⁽³⁾

Clarifications on the treatment of the information presented are provided where appropriate in the document.

⁽¹⁾ Information on Sareb included in the analysis has not been verified by EY

⁽²⁾ Information for the second half of 2017 is estimated by the areas of Sareb in charge of reporting each figure

⁽³⁾ See section on "Approach" for more details

Approach



Input-output methodology

EY's input-output methodology for calculating the indirect and induced economic contribution and indirect and induced job creation uses tables of symmetrical inputs and outputs to represent the socio-economic interdependencies between sectors of economic activity in Spain. Through the interaction of this modeling of the economy with elements such as employment, average wages and gross value added of each branch of activity, Sareb's indirect and induced impacts on the economy and society can be obtained. Purchases made in Spain and corporate information (no. of employees and wages paid) for each financial year the impacts are calculated are considered as the company's economic information. Secondary figures used in the calculation (e.g, input and output data, household consumption by sector, gross value added at base prices per sector, total full time equivalents and employment per sector, wages and salaries per sector) correspond to available data and public data of *World Input-Output Database* (WIOD 56 sectors) and the Spanish National Statistics Institute (INE). All calculations are based on the latest tables available.



Direct contribution

Sareb's direct economic contribution (gross value added) in Spain relates to earnings before tax, interest, depreciation and amortization and the salaries of company employees from 2013 to 2017. Direct social contribution in Spain relates to the number of company employees in Spain in each of these years.



Indirect contribution

Sareb's indirect contribution in Spain was calculated taking purchasing data in Spain for each year covered in the report mapped according to the sectors in the WIOD input-output tables for Spain to analyze their impact on employment, wages and the economy's gross value added.



Induced contribution

Sareb's induced contribution in Spain was calculated by extracting the portion of net wages generated directly and indirectly earmarked for saving. The household saving rate in the 2013-2017 period excluding non-profit institutions serving households (NPISHs) was used. Net wages generated directly and indirectly were taken as inputs in the local economy, according to total household consumption in the various sectors of the Spanish economy, to analyze their impact on employment, wages and the economy's gross value added.



Fiscal contribution

Sareb's fiscal contribution was calculated taking in account the taxes it pays and collects, including value added tax (VAT), personal income tax withholdings, contributions to Social Security, corporate income tax, property tax, business tax, and other taxes and duties. Accordingly, it includes both taxes related to Sareb's activities (i.e. those imply an expense and impact its profit or loss) and those collected on behalf of third parties.



Other impacts

Sareb's financial contribution (via the redemption of bonds guaranteed by the State and the payment of interest on the bonds), sector impact and social impact, through the provision of housing to people at the risk of exclusion, were calculated directly with data provided by Sareb.

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Scenario before Sareb's creation



Scenario before Sareb's creation

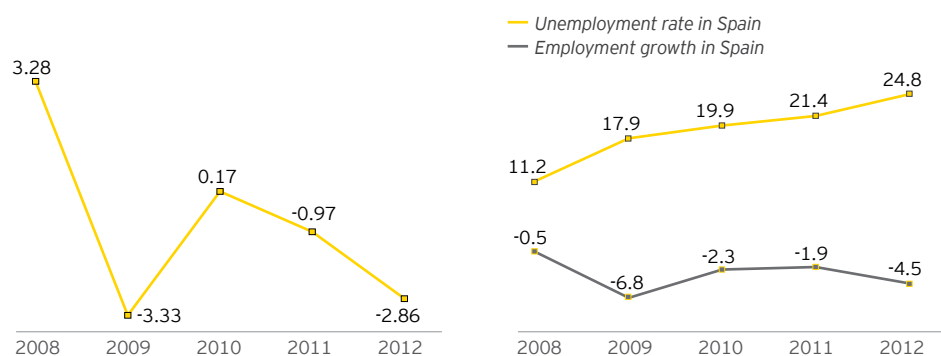
Macroeconomic trends

The systemic impact of the global financial crisis that arose in 2007 fed through quickly to the Spanish economy, as borne out by some of its key indicators.



From 2008, the crisis in Spain affected GDP growth, employment and the risk premium. In 2012, GDP contracted by 2.9%, the unemployment rate⁽¹⁾ reached 24.8%, and the risk premium⁽²⁾ set a new all-time high (at around 640 basis points)

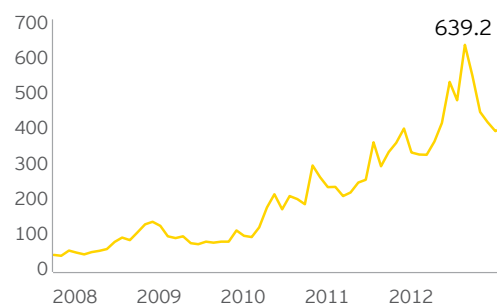
Annual GDP growth and unemployment rate in Spain ⁽¹⁾



Spain's gross domestic product went from growth of over 3% in 2008 to contraction of nearly 3% in 2012.

This also had implications for employment. The unemployment rate peaked in 2012 (at 24.8%), with the steepest fall in employment (-6.8%) registered in 2009.

Spain risk premium ⁽²⁾



The risk premium; i.e. the difference between the interest rates on debt issued by a country with riskier assets and those by a country with less risk, rose continuously, reaching its highest level in July 2012.

Asset prices eroded and credit was restricted, affecting growth, SMEs and households.

⁽¹⁾ Source: National Statistics Institute (INE)

⁽²⁾ Source: Bloomberg

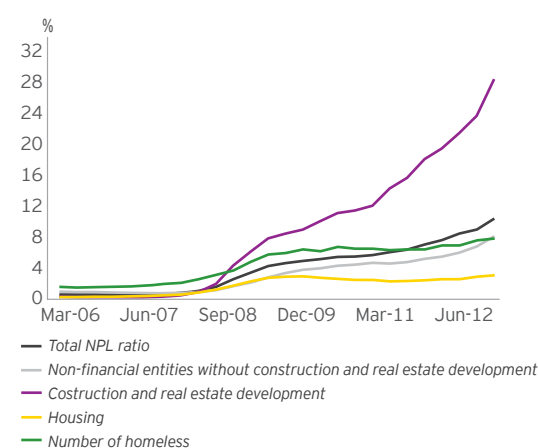
Impact of the real estate crisis on the financial sector

In 2007, the Spanish financial sector was heavily exposed to construction and real estate lending. The financial crisis caused non-performing loan (NPL) ratios to soar in the ensuing years. Housing prices dwindled, exacerbating the effects of the crisis.



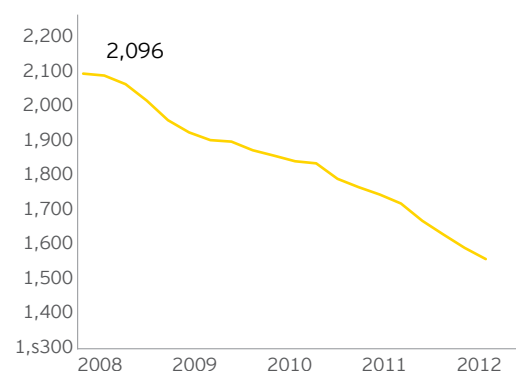
Lofty credit and rising NPL ratios impacted the financial sector as a whole during the crisis. From 2008 to 2012, housing prices⁽³⁾ slumped by approximately 21.5%

NPL ratios by sector⁽¹⁾



Construction and real estate loans represented roughly 60% of the total in 2007⁽²⁾. This loan concentration posed a serious risk for the Spanish economy, which materialized in 2007, when the non-performing loan ratio (the ratio of loans with a low probability of repayment and at least three months in arrears to total loans) rose in all sectors of activity and especially in construction and real estate.

Market rate housing (€/m²) ⁽³⁾



The price per square meter of market rate homes in Spain peaked at €2,096 in 2008, rising steadily from 1,400 €/m² in 2004.

Prices fell from 2008 to 2014. In 2012, the cumulative decline was around 21.5%.

⁽¹⁾ Source: Bank of Spain (2012). November 2012 Financial Stability Report

⁽²⁾ Source: Bank of Spain. (2014). 2014 Annual Report

⁽³⁾ Source: National Statistics Institute (INE)

Memorandum of Understanding (MoU)

In the midst of the financial crisis and the potential worsening of the effects described previously, the Spanish government, in conjunction with the European Union, adopted a series of control measures that led to the signing of the Memorandum of Understanding on Financial-sector Policy Conditionality (MoU) in 2012. This was key to Europe's recapitalization program and comprised three elements:

A

Identification of individual bank capital needs through a comprehensive asset quality review of the banking sector and a bank-by-bank stress test

B

Recapitalization, restructuring and/or resolution of weak banks, based on plans to address any capital shortfalls identified in the stress test

C

Segregation of assets in those banks receiving public support in their recapitalization effort and the transfer of the impaired assets to an external management company, which was called Sareb

After the stress test outlined in the MoU, Spanish banks was categorized into four groups:

Group 0

Bank for which no capital shortfall was identified and no further action was required

Group 1

Banks already owned by the Fund for Orderly Bank Restructuring (FROB, in Spanish).

Group 2

Banks with capital shortfalls unable to meet those shortfalls privately without having recourse to State aid

Group 3

Banks with capital shortfalls with credible recapitalization plans and able to meet those shortfalls privately without recourse to State aid

Government-price setting for the assets

The problematic assets identified in the banks were removed from their balance sheets and transferred to Sareb at a price set by the government



Group 1:

- ▶ BFA-Bankia
- ▶ Catalunya Banc
- ▶ Novagalicia Banco
- ▶ Banco Gallego
- ▶ Banco de Valencia

Group 2:

- ▶ BMN
- ▶ Liberbank
- ▶ Caja 3
- ▶ CEISS


€50,781Mn
of assets⁽¹⁾

⁽¹⁾ Transfer price set by the authorities

Constitution and characteristics of Sareb

In compliance with the third point of the MoU, on November 28, 2012, the Fund for Orderly Bank Restructuring (FROB, in Spanish), created The Management Company for Assets Arising from the Banking Sector Reorganisation, known as Sareb, with the following characteristics:



Time horizon

15 years
(2012-2027)



Ownership

45.9%

Public
(FROB)

54.1%

Private
(Spanish banks and
insurance companies)



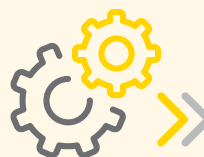
Main activities

- ▶ Loan management and settlement
- ▶ Property management and divestment



Objectives

- ▶ Manage and divest, in an orderly manner, the real estate loans and assets received from participating banks
- ▶ Provide liquidity to the participating banks
- ▶ Drive the revitalization of the real estate market



Responsibilities

- ▶ Optimize levels of recovery and value preservation
- ▶ Minimize the impact of the financial crisis
- ▶ Minimize costs and the burden on taxpayers
- ▶ Repay its liabilities in full
- ▶ Utilize capital efficiently



Portfolio

€50,781Mn
of assets



Value of
financial assets

€39,438Mn

No. of financial
assets

90,765



Value of real
estate assets

€11,343Mn

No. of real estate
assets

107,446

Transferred by Groups 1 (December 31, 2012) and 2 (February 28, 2013) to Sareb in exchange for bonds issued by Sareb and guaranteed by the State. A significant portion of the amount paid (€19,900Mn⁽¹⁾) was considered State aid by the European Commission, although it was provided by Sareb.

⁽¹⁾ Source: European Commission. Directorate-General for Competition

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Scenario after Sareb's creation



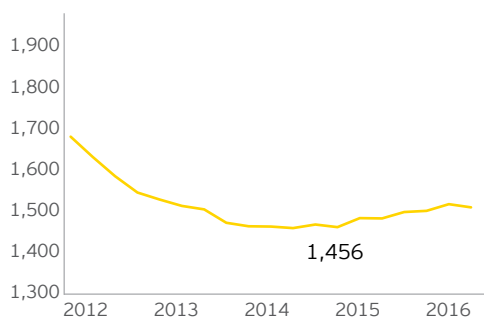
Construction and real estate sector trends

The creation of Sareb, coupled with the implementation of the rest of the measures in the Spanish bank restructuring process, drove improvement in key and representative indicators for the construction and real estate sector. Market rate housing prices stabilized and foreign investment in the sector rebounded after real estate transactions were completed providing a benchmark.



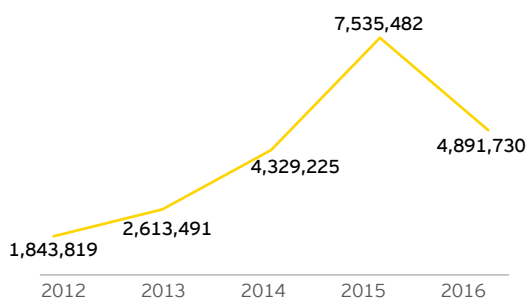
Housing prices stabilized and foreign investment in the Spanish construction and real estate sector began rebounding in 2012

Market rate housing (€/m²)⁽¹⁾



The price per m² of market rate housing in Spain declined continuously until 2014, when it reached €1,456, before stabilizing and rising gradually from the beginning of 2015.

Foreign investment in construction and real estate activities (thousand of euros)⁽²⁾



The improvement in the construction and real estate sector brought in international investors, which viewed the Spanish economy as an opportunity.

Sareb carried out real estate transactions with investors that provided a benchmark and starting point for the sector's revitalization. Foreign investment soared more than 300% in the 2012-2015 period.

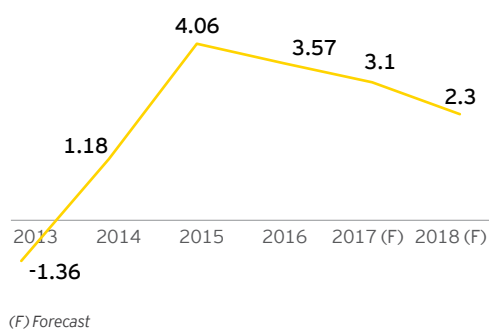
⁽¹⁾ Source: National Statistics Institute (INE)

⁽²⁾ Source: Ministry of Economy, Industry and Competitiveness

Macroeconomic trends

The pickup by the construction and real estate sector fed through to important macroeconomic indicators, such as gross domestic product (GDP), which began growing, and the risk premium, which fell sharply.

Annual GDP growth and forecasts ⁽¹⁾

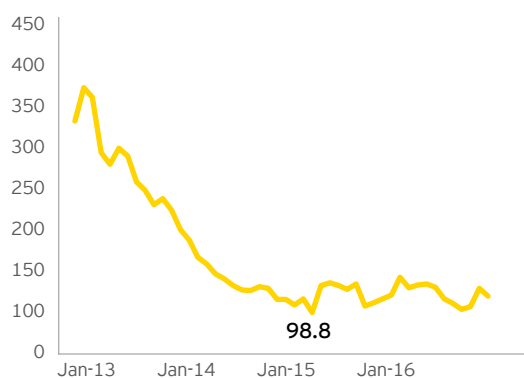


Spain's gross domestic product improved from negative growth of 1.5% in 2013 to positive growth 4% at the beginning of 2015, with forecasts pointing to stabilization in the short term.



Since the actions outlined in the MoU were implemented, Spain's GDP has expanded and its risk premium stabilized after a prolonged period of declines

Spain risk premium ⁽²⁾



The risk premium for Spain began falling steadily in 2013 until leveling off towards the end of 2014 at around 100 basis points.

The release of non-performing assets from the banking and their management by Sareb helped revive credit and gradually reduce the level of non-performing construction and real estate loans on banks' balance sheets.

⁽¹⁾ Source: National Statistics Institute (INE) Forecasts: Bank of Spain

⁽²⁾ Source: Bloomberg

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Sareb: socio-economic impact



Sareb: socio-economic impact

Type of impacts

The impacts generated by Sareb in its first five years of operations can be classified into three types:



Aggregate impact on the economy

Economic contribution

- ▶ Sareb's direct economic contribution in Spain (gross value added)
- ▶ Sareb's indirect economic contribution in Spain (via purchases from suppliers)
- ▶ Sareb's induced economic contribution in Spain (via spending by its and suppliers' employees)

Financial contribution

- ▶ Redemption of the bonds guaranteed by the State
- ▶ Payment of interest on the bonds guaranteed by the State

Fiscal contribution

- ▶ Sareb's fiscal contribution in Spain by type of tax



Sector impact

- ▶ Contribution to the financial and real estate sector
- ▶ Breakdown of expenditure related to management of the real estate asset portfolio by region
- ▶ Revitalization of local economies and the construction and real estate sector



Social impact

Job creation

- ▶ Sareb's direction contribution to employment in Spain (generation of direct employment)
- ▶ Sareb's indirect contribution to employment in Spain (via purchases from suppliers)
- ▶ Sareb's induced contribution to employment in Spain (via spending of employee salaries and suppliers)

Social housing

- ▶ Number of houses provided to groups at risk of exclusion from transfers to town councils and regional governments
- ▶ Number of beneficiaries of social housing programs

Aggregate impact on the economy



Sareb's aggregate impact⁽¹⁾ is 0.43% of Spain's cumulative GDP for the 2013-2017 period⁽²⁾

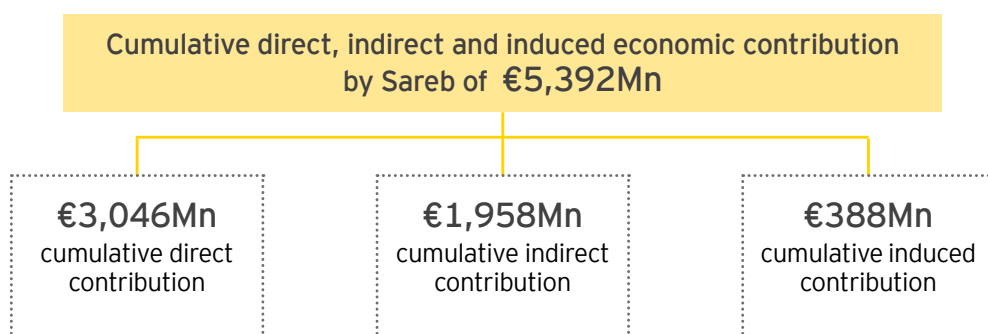
€1 of gross value added generated by Sareb helped generate €0.77 of the Spanish economy's gross value added in the company's five years of operations⁽³⁾

€23,248Mn Sareb's cumulative economic, financial and fiscal contribution⁽¹⁾ to the Spanish economy in its five years of operation



Economic contribution

In carrying out its work, Sareb contributes to the Spanish economy directly by generating gross value added (operating profit + personnel expenses + depreciation and amortization), indirectly by the gross value added generated in the sectors that benefit indirectly from the expenses of the company's suppliers and indirectly through the multiplier effect of employees (both its own and those of suppliers) when they spend their wages in the general economy.



⁽¹⁾ The aggregate economic impact is the sum of Sareb's direct, indirect and induced economic contributions in the 2013-2017 period, the cumulative financial contribution and the cumulative fiscal contribution (see next page).

⁽²⁾ Corresponds to Sareb's cumulative total contribution in the 2013-2017 period divided by cumulative total Spanish GDP in the same period (GDP data from INE; forecasts from the Bank of Spain).

⁽³⁾ Corresponds to the cumulative indirect and induced contribution divided by the cumulative direct contribution.

The impact generated by Sareb through purchases from its suppliers, and expenditure on its own and suppliers' employees, contributed significantly to nine of Spain's economic sectors. Noteworthy is Sareb's indirect economic contribution to professional, scientific and technical activities and financial and insurance activities.

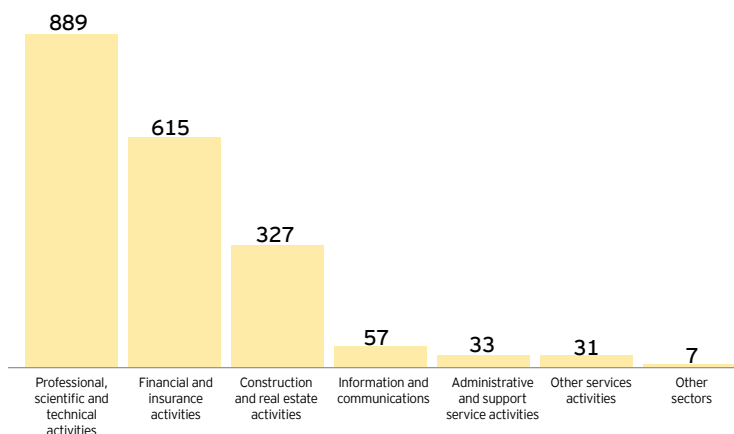


17% of Sareb's indirect economic contribution⁽¹⁾ and 23% of its induced contribution⁽¹⁾ are generated in construction and real estate activities

Cumulative indirect economic contribution⁽¹⁾

€1,958Mn

generated for sectors that benefit indirectly from the amount spent by the company on its suppliers in the 2013-2017 period

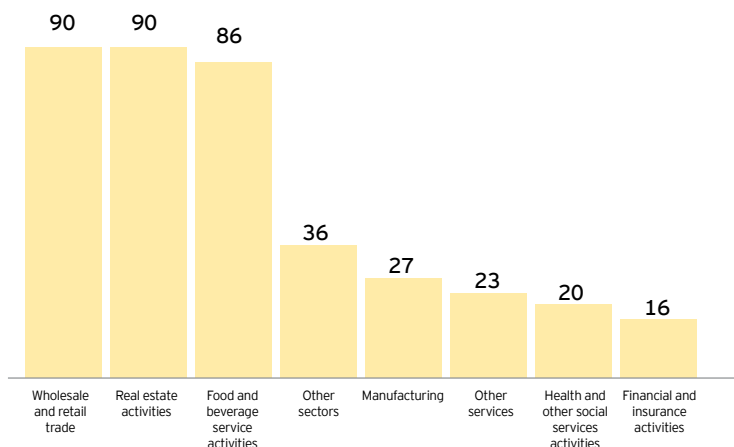


Figures in € million

Cumulative induced economic contribution⁽¹⁾

€388Mn

generated for sectors that benefit from the multiplier effect of spending by the company's and suppliers' employees in the general economy



Figures in € million

⁽¹⁾ Corresponds to the percentage contribution to these sectors of the total indirect and induced economic contribution, respectively.

Aggregate impact on the economy (cont.)



Sareb has redeemed 25.3% of the senior bonds⁽¹⁾ issued on its creation



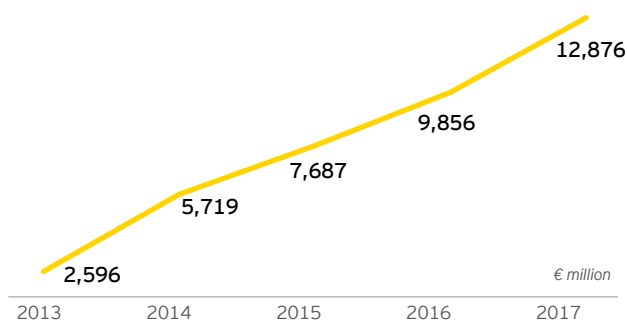
Financial contribution

Sareb issued bonds to acquire the assets from the participating banks, avoiding any impact on the public purse. The senior bonds were guaranteed by the State and exchangeable with the European Central Bank, providing immediate liquidity to the participating banks.

Redemption of bonds guaranteed by the State⁽²⁾

€12,876Mn
spent on the redemption of senior bonds (2013-2017)

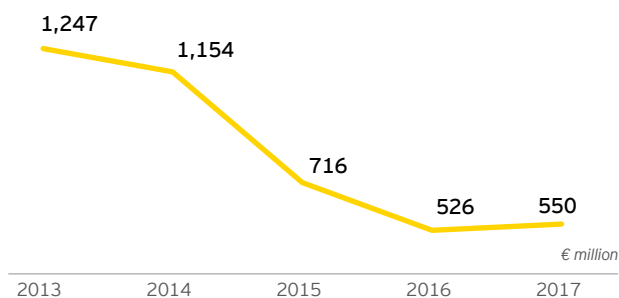
In its first five years of operation, Sareb has redeemed €12,876 million, 25.3% of the debt acquired upon its creation.



Payment of interest on bonds guaranteed by the State⁽²⁾

€4,193Mn
of interest paid on bonds guaranteed by the State

Sareb's finance costs include payment of interest on the senior bonds issued as consideration for the assets. By paying interest, the company avoids enforcement of the State's guarantees. Of total interest paid by Sareb, €2,779 million went to participating banks.



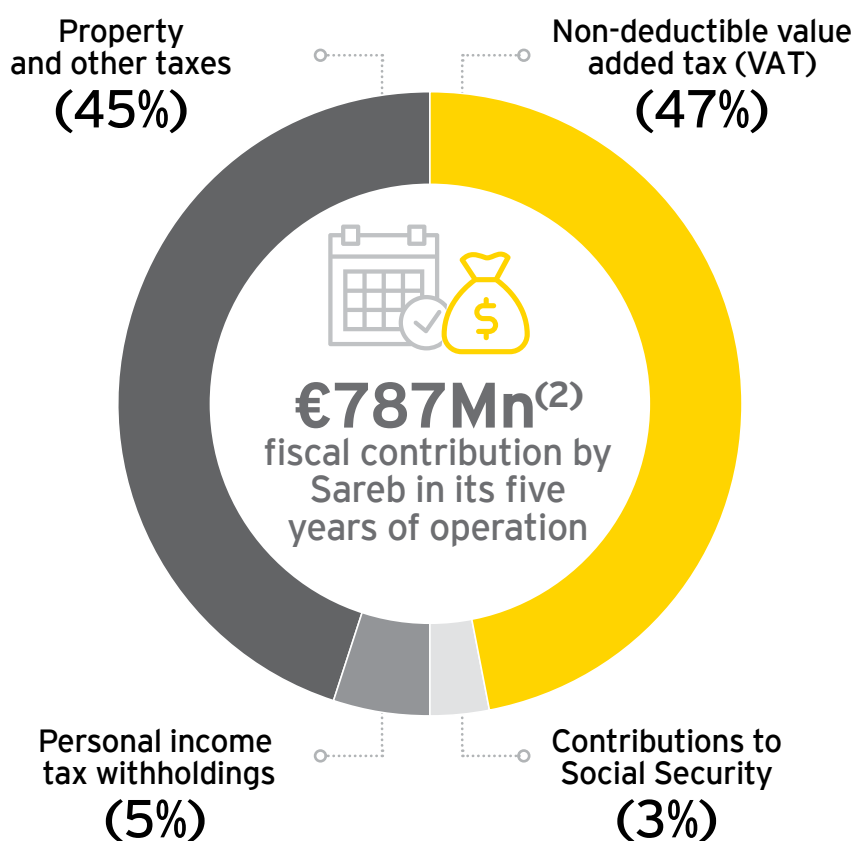
⁽¹⁾ Corresponds to the amount redeemed in 2013-2017 divided by the total debt acquired (€50,781Mn).

⁽²⁾ Source: Sareb



Fiscal contribution

Sareb contributes to Spain's public sector by paying taxes. Some taxes are paid directly, while others are collected from its business thanks to dealings with customers and employees.



The amount of taxes paid by Sareb in its five years of operation is similar to the budgets of town councils such as Seville or Valencia⁽¹⁾

⁽¹⁾ Source: Ministry of Finance and Civil Service (Valencia: €787 million in 2017; Seville: €821 million in 2017)

⁽²⁾ Source: Sareb

Sector impact



Sareb has divested 27.2% of its assets in its five years of operation



Contribution to the financial and real estate sectors

Sareb was created to operate for a period of 15 years. Divestment of its portfolio of financial and real estate assets is an indicator of the company's impact on the economy, since it enables these sectors, with a combined weight of 16% on the Spanish economy⁽¹⁾, to recover and grow. Sareb mainly engages in the management of loans and properties, with the following characteristics:

Loan management

Management revenues include revenue from the cancellation and sale of loans, sales growth plans (PDVs in Spanish) and the sale of collateral. PDVs are agreements that allow Sareb's borrowers and debtors to cancel their debts by selling the properties used as loan collateral. Sareb has reduced its number of debtors from 17,345 when it was created to 14,875 by the end of the first half of 2017.

20% of revenue from trade agreements with sector companies, mainly SMEs ⁽²⁾

2,470 fewer debtors since its creation (14% decrease) ⁽²⁾

Property management (sale and lease)

The sale of real estate assets is one of Sareb's core activities, along with loan management. In addition, the incentive to lease is an alternative to divestment for Sareb, which also lowers the costs of the properties.

65,000 properties sold ⁽³⁾

4,603 properties leased ⁽³⁾

11,507⁽⁴⁾ beneficiaries of the lease of residential property

818 tertiary assets

Sareb has spent €1,115 million on the management and sale of assets, divesting €13,817 million (27.2% of the portfolio). The participating banks oversaw the management and sale of the assets in 2013 and 2014, while this was assigned to servicers (Altamira, Haya, Servihabitad and Solvia) in 2015. Servicers share the company's interests and offer comprehensive management of the asset portfolio, enhancing the professionalization of the real estate sector.

€1,115Mn spent on the management and sale of assets ⁽³⁾

€13,817Mn divested ⁽³⁾ since Sareb was created

⁽¹⁾ The percentage weight of the financial (excluding insurance) and real estate sectors on total GDP in Spain (2013-2017 period)

⁽²⁾ Source: Sareb. Average for 2013 - 2016

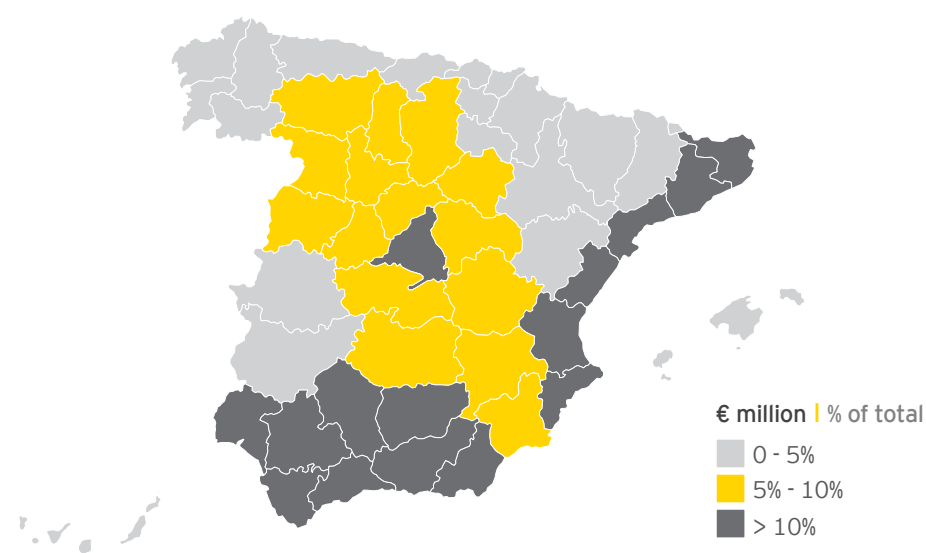
⁽³⁾ Source: Sareb

⁽⁴⁾ Estimate based on the calculation of the average size of households by INE (2.5 people in 2016)



Breakdown of expenditure on management of the real estate asset portfolio by region

Sareb generates a direct impact from its real estate asset management business in the regions where the properties in its portfolio are located. Payments to homeowners' associations and property tax, in addition to maintenance costs and payments to the servicers overseeing local management, since 2013 amount to €1,687 million⁽¹⁾, broken down as follows:



Andalusia 200.3 11.9%	Castile and Leon 126.5 7.5%	Extremadura 24.8 1.5%	Basque Country 5.1 0.3%
Aragon 40.5 2.4%	Catalonia 336.6 19.9%	Galicia 57.9 3.4%	Asturias 35.4 2.1%
Canary Islands 54.6 3.2%	Ceuta and Melilla 11.4 0.7%	Balearic Islands 33 2%	Murcia 91.6 5.4%
Cantabria 32.1 1.9%	Madrid 204.2 12.1%	La Rioja 17 1%	
Castile - La Mancha 126.1 7.5%	Valencia 277.6 16.5%	Navarre 12.3 0.7%	



Real estate asset management has contributed €1,687 million⁽¹⁾, spread out across Spain

Sareb has spent a total of €414 million⁽²⁾ in payments to homeowners' associations and maintenance costs for its portfolio of real estate assets

⁽¹⁾⁽²⁾ Source: Sareb

Sector impact (cont.)

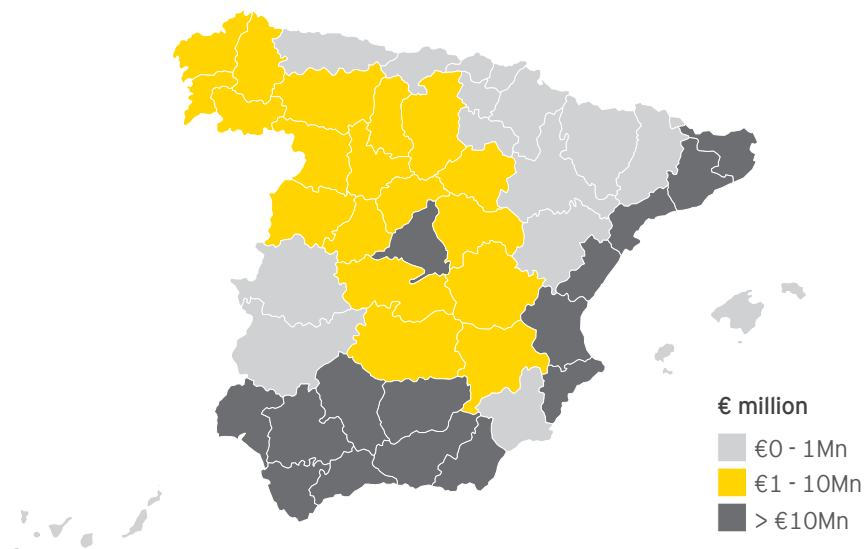


Sareb has invested nearly €64 million⁽²⁾ to complete construction and develop land



Revitalization of local economies and the construction and real estate sector

Sareb has invested nearly €64 million⁽¹⁾ to complete construction and build homes on its land. Real estate development has been one of the company's pillars, with Sareb resuming projects that were halted and starting new ones on undeveloped land.



Andalusia 13	Catalonia 17	Galicia 2.5
Canary Islands 0.8	Madrid 13	La Rioja 0.04
Cantabria 2	Valencia 11	Asturias 1.3
Castile - La Mancha 0.8	Extremadura 1.2	Murcia 0.06
Castile and Leon 1.3		

⁽¹⁾Source: Sareb (at September, 2017)

⁽²⁾Source: Sareb

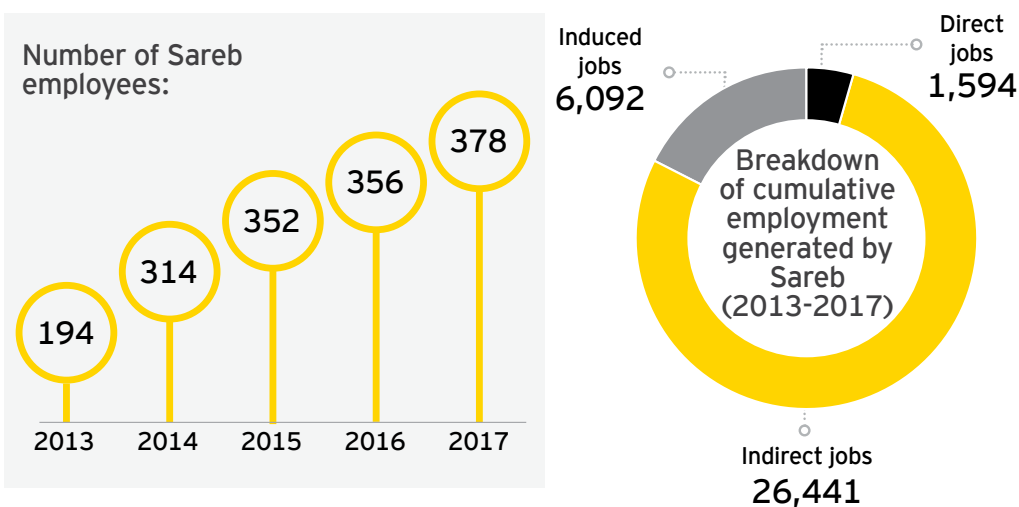
Social impact



Job creation

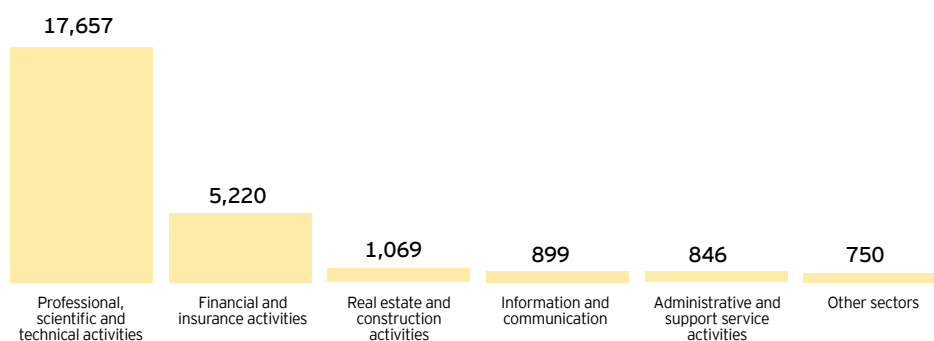
Sareb makes a direct, indirect (through purchases from suppliers) and induced (spending by company and suppliers' employees) contribution to the creation and maintenance of employment in Spain.

34,127 direct, indirect and induced jobs created in Sareb's five years of operation



For every direct employee, Sareb generates 20 indirect and induced jobs ⁽¹⁾

Sector breakdown of cumulative indirect jobs created:



⁽¹⁾ Cumulative indirect and induced jobs divided by cumulative direct jobs

Social impact (cont.)



Sareb has earmarked 4,000 homes⁽²⁾ for social purposes (2,360⁽²⁾ of which are already committed)

5,900 people⁽¹⁾ have benefited from these public housing programs

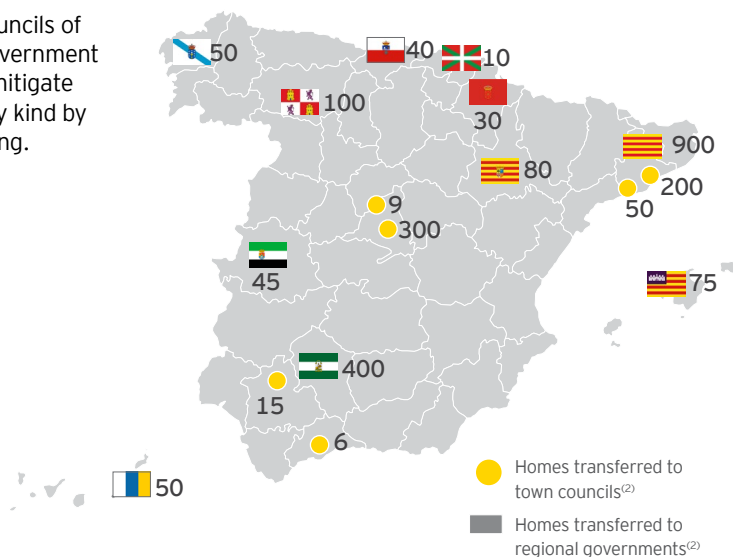


Public housing assistance program

In conjunction with a number of regional governments, Sareb provides homes to mitigate the situation of groups at risk of exclusion.

Aid program for people in social emergency situations

In conjunction with town councils of major cities and regional government bodies, the initiative helps mitigate exceptional situations of any kind by temporarily providing housing.



Alternative affordable rental program

In cooperation with Social Services of regional governments and town councils, the purpose of this program is to provide an alternative housing solution to vulnerable families by triggering a mediation procedure with occupants of the asset.



107 subsidized housing agreements⁽²⁾

⁽¹⁾ Estimated based on average household size according to INE (2.5 people in 2016) (considering committed homes)

⁽²⁾ Source: Sareb

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