

19

FIXED
INCOME
MARKET

ECONOMIC, MONETARY AND DEBT MARKET SCENARIO

Global, Eurozone and Spanish economies

- ✓ **The global economy in 2019, rather than meeting expectations** of a more sustained recovery in growth, actually slowed increasingly as the year progressed. **The IMF estimated global growth of 3% for 2019, six-tenths of a percent lower than in 2018 and the lowest rate in the decade since the financial crisis.**
- ✓ **The escalation of the trade war between China and the US, political risks, and economic and social unrest** in many emerging and developed countries **have created uncertainty in the world economy.**
- ✓ The slowdown and the absence of inflationary pressures have led to a return to expansionary monetary policies by the main central banks. **Global stock markets have responded with strong rises and debt market interest rates have fallen, becoming negative in many cases.**
- ✓ In the European economy, and the **Eurozone** in particular, **the slowdown, already noticeable at the end of 2018, worsened with the downturn in the German industrial sector and the uncertainty generated by Brexit.**
- ✓ **As for Spain, the economy confirmed its entry into a more mature phase of the cycle,** largely halted by global and European deceleration, the tensions and decline in international trade, and internal and external political uncertainty. However, according to the IMF's autumn forecast, **Spain outperformed the main European economies in 2019, with growth of 2% compared to the Eurozone average of 1.2%.**

Monetary policy

- ✓ **In 2019** there was a radical reversal in the **monetary policies of the major central banks compared to the previous year; becoming more expansionary in response to the slowdown in the global economy** recognised by various international organisations.
- ✓ **The US FED has lowered rates on three occasions.** In the presence of "prominent risks", it lowered its intervention interest rate on 31 July by 0.25 points down to 2.25%, the first reduction in 10 years. The Fed lowered rates for a second time (to 2%) on 18 September and on 30 October cut them again (down to 1.75%), after having also temporarily launched purchases of government debt securities to solve liquidity problems in repo markets; which once again increased the size of its balance sheet.
- ✓ **In July, the ECB announced that it would take measures to achieve its 2% inflation target and in September its new stimulus package was approved:** it kept its key interest rate at 0%; raised the penalty for banks depositing excess liquidity at the ECB to -0.5%, though with certain safeguards; launched a new 20.00 billion euros per month asset purchase programme in November; continued its policy of reinvesting funds from maturing bonds; and introduced new 2-year and 3-year funding rounds (TLTRO III) for banks on favourable terms.

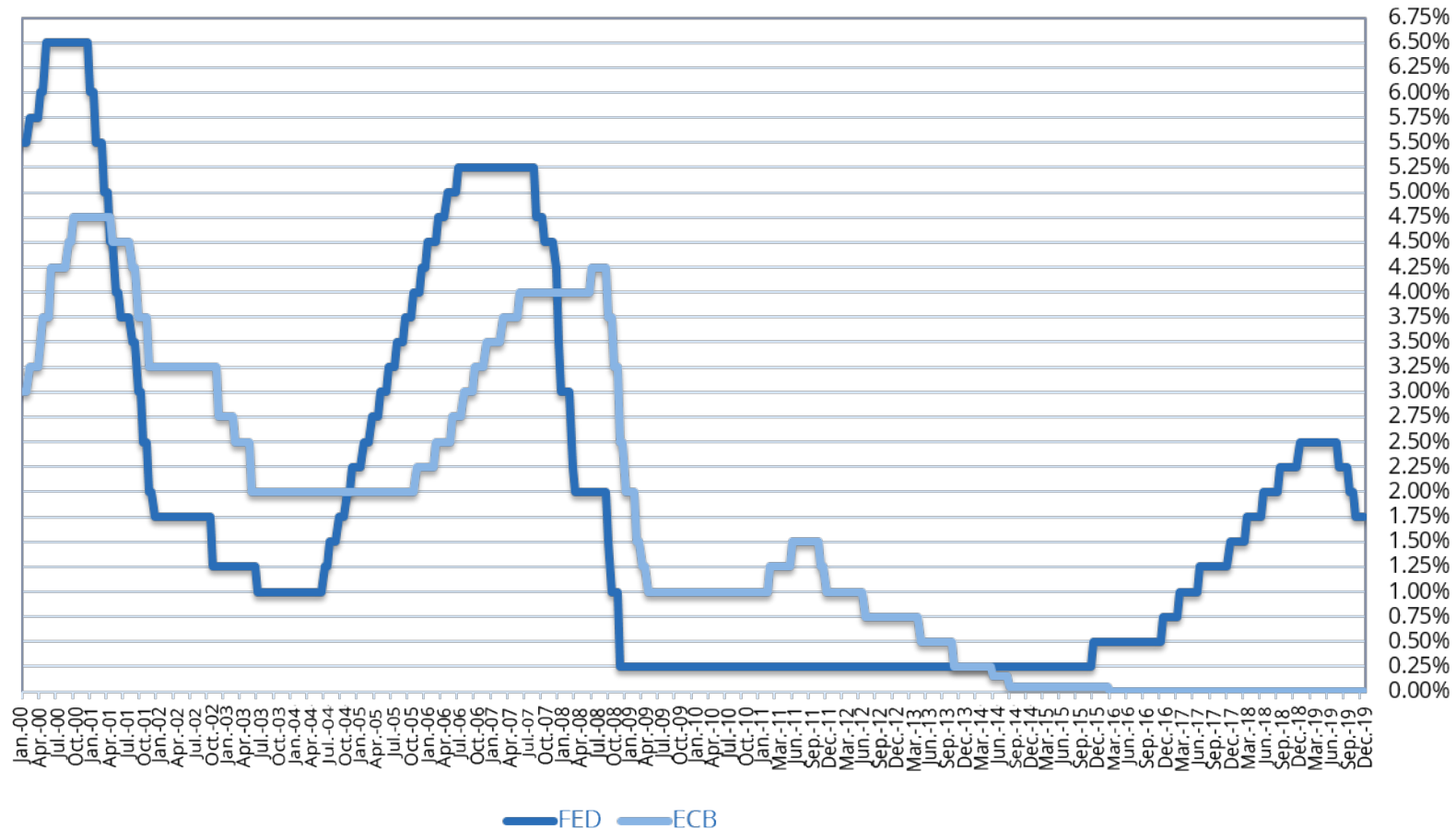
Debt markets

- ✓ In the **main government debt and private fixed-income markets** there has **been a sharp drop in yields.**
- ✓ **The US 10Y bond** began the year with a yield of 2.68% and ended it at 1.92%. **The German bond** started 2019 with a yield of 0.24%, then entered negative territory at the end of March, hitting a low of -0.72%, before finally closing the year at -0.19%.
- ✓ **At the beginning of the year, the Spanish 10Y bond had yields of 1.42%, which fell to a low of 0.04% in August.** It later recovered to 0.46% at the end of 2019. **The Spanish risk premium has also been considerably reduced: at the start of the year, it stood at 1.18 percentage points and by the end of December it was down to 0.65 points.**
- ✓ **Private fixed income also experienced a year characterised by yields falling** to historically low levels. Triple B rated European fixed income, depending on the term, reached levels below 1%.

SCENARIO INDICATORS

ECB and FED benchmark interest rates

(2000 - 2019)

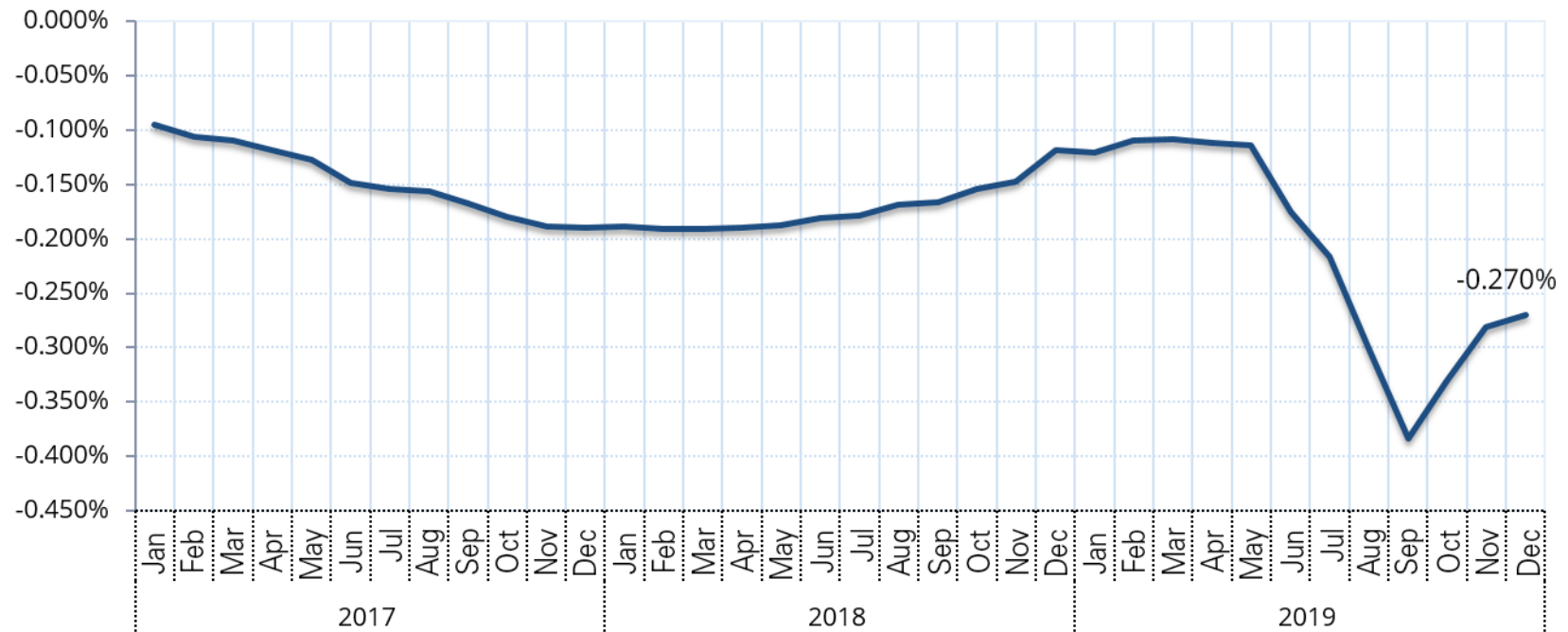


The US Federal Reserve has returned to an expansive monetary policy with three rate cuts in 2019.

Euribor at the end of each month (2017-2019)

Source: Bank of Spain

Euribor at the end of each month



Negative yields in the Euribor deepened in the middle-months of the year and rebounded slightly at the end of it.

Exchange rate

EUR vs USD in 2019

USD/EUR Daily data up to 31 December. Source: Factset



The EUR has continued to weaken against the USD. It lost around 7% between 2018 and 2019.

Government debt

Interest rates (%) of 10Y US and German debt (2017-2019)

Daily data up to 31 December. Source: Factset



The US 10Y bond began the year with a return of 2.68% and closed it at 1.92%, having dropped to a low of 1.46%. The German bond began 2019 with a return of 0.24% and entered into negative yield territory at the end of March. This trend accelerated until reaching lows of -0.72%, after which it recovered to -0.19% at the end of December. The gap between the US and European 10Y rates has been fairly stable throughout the year (between 2.05 and 2.50 percentage points).

Spanish Treasury debt

Interest rates (%) of Spanish government debt at 3, 5 and 10 years (2018-2019)

Daily data up to 31 December. Source: Factset



Spanish 10Y bond risk premium versus German Bund in 2019

Spread

Daily data until December 31, in basis points. Source: Factset



In 2019, the Spanish risk premium was once again regularly situated below the percentage point (100 basis points) from May onwards.

Oil

Oil price 2018-2019 (Brent crude in USD/barrel)

Daily data up to 31 December. Source: Factset



Oil prices have remained consistently above USD 55/barrel since the January 2019 rebound.

Gold

USD/ounce in 2019 (USD/ounce)

Gold London AM Fixing. Daily data in billions up to 31 December. Daily data. Source: Factset



The price of gold was driven up during 2019, with it acting as a safe-haven asset protecting against the uncertainties of the global economy.

ACTIVITY AND PERFORMANCE OF THE FIXED INCOME MARKETS MANAGED BY BME

Primary market Spanish government debt

Main figures 2019

- ✓ **Final deficit of the entire public sector in 2019 will be approaching 2.5% of GDP, higher than the Spanish Government had committed to** (Source: Bank of Spain and FUNCAS). The initial objective agreed with Europe was for a deficit of 1.3% of GDP, which was later increased to 1.8% and the Government subsequently set itself a target of 2%.
- ✓ **At the end of 2019, the government deficit stood at 1.19 trillion euros, equivalent to 95.5% of GDP, within the target set by the Government**, two points less than in 2018 and the lowest rate since 2012.
- ✓ **The gross issuance of Spanish Treasury debt was 196.64 billion euros in 2019**. This is the first time since 2011, that it has dipped below 200.00 billion euros.
- ✓ **Net issuance stood at 19.96 billion euros (the lowest figure since 2007) versus the budgeted 35.00 billion euros**. The cost of financing the new debt was reduced from 0.64% in 2018 to 0.23% in 2019, while the cost of outstanding debt also fell from 2.39% to 2.19%.

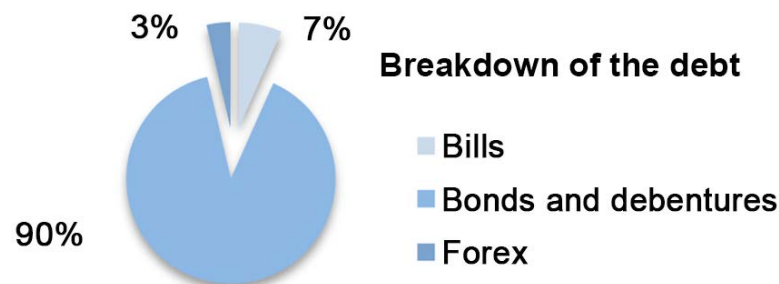
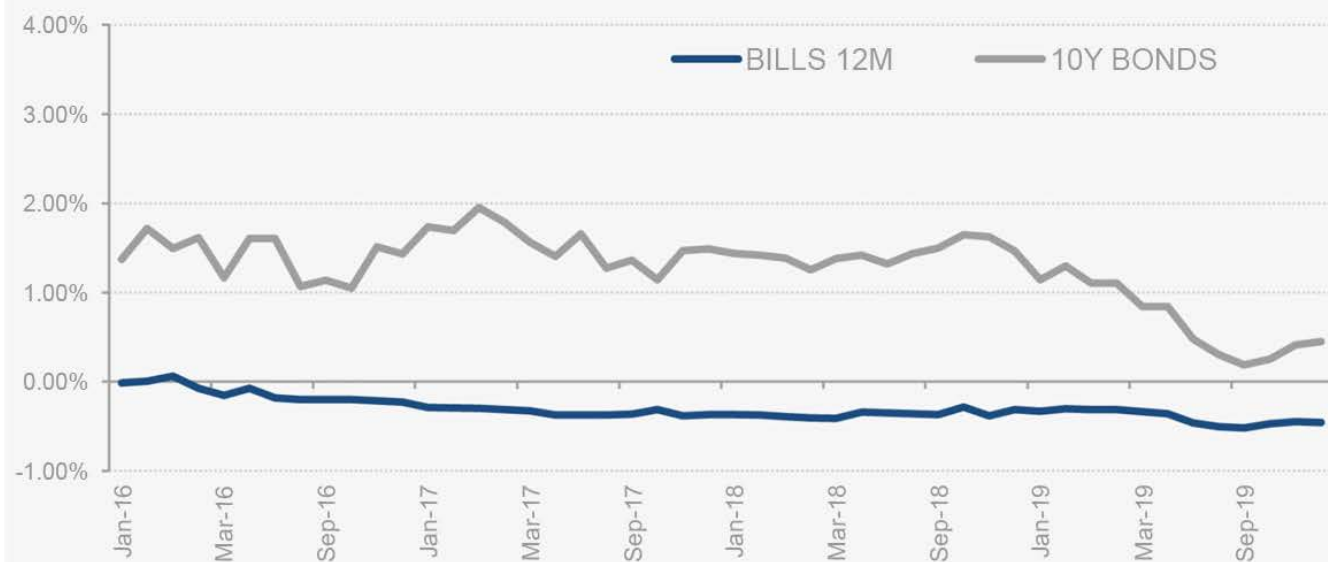
Primary market Spanish government debt

Treasury issuing activity in 2019 (I)

Sovereign debt ratings

Fitch: A-/stable
Moody's: Baal/stable
S&P: A/stable

Trend in marginal rates of interest on sovereign debt issuances



Source: Directorate General of the Treasury

Primary market Spanish government debt

Treasury issuing activity in 2019 (II)

Government debt

Figures in billions of euros. Source: BME

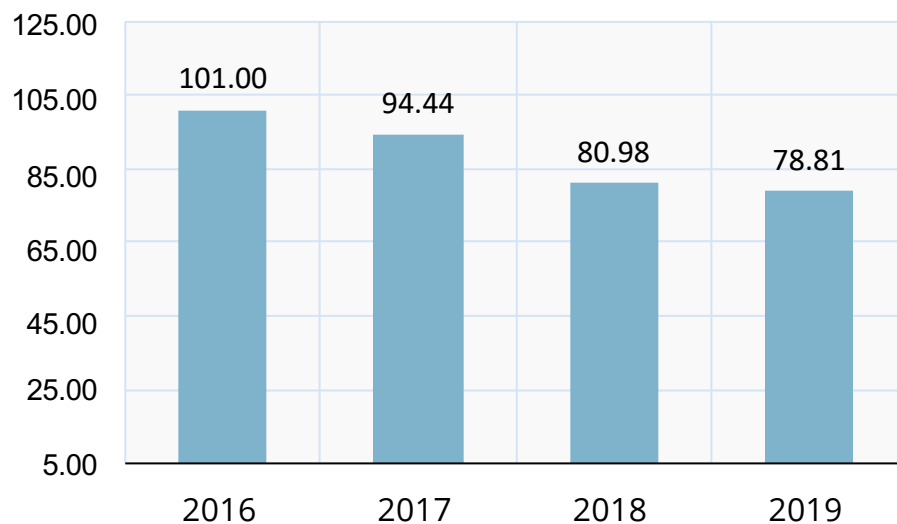
	Maturities	Auctions
January	24.26	25.62
February	5.57	15.46
March	7.17	19.66
April	30.09	14.14
May	6.54	15.14
June	6.53	20.41
July	28.27	15.36
August	7.97	11.33
September	4.92	15.37
October	25.92	13.54
November	14.78	16.40
December	4.29	14.22
TOTAL	166.33	196.64

Primary market Spanish government debt

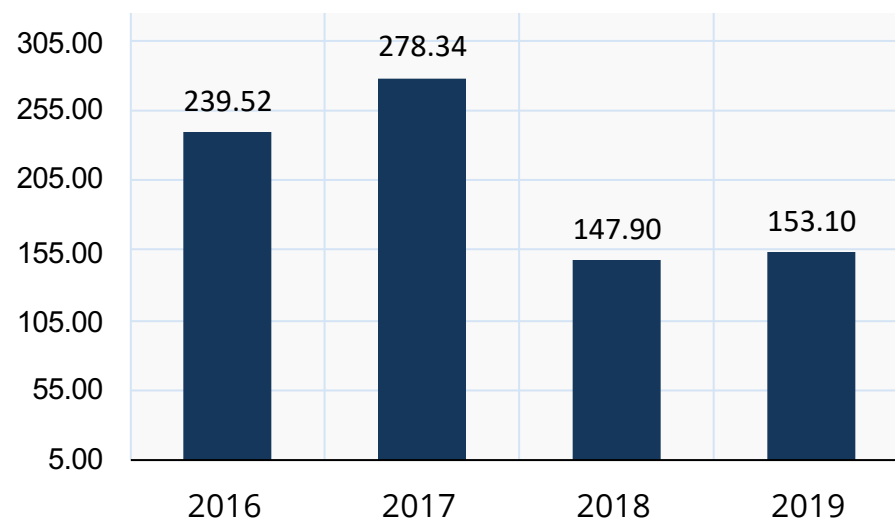
AIAF market. Admissions to trading

Figures in billions of euros. Source: BME

Short-term government debt



Medium- and long-term government debt



Primary market Spanish private debt

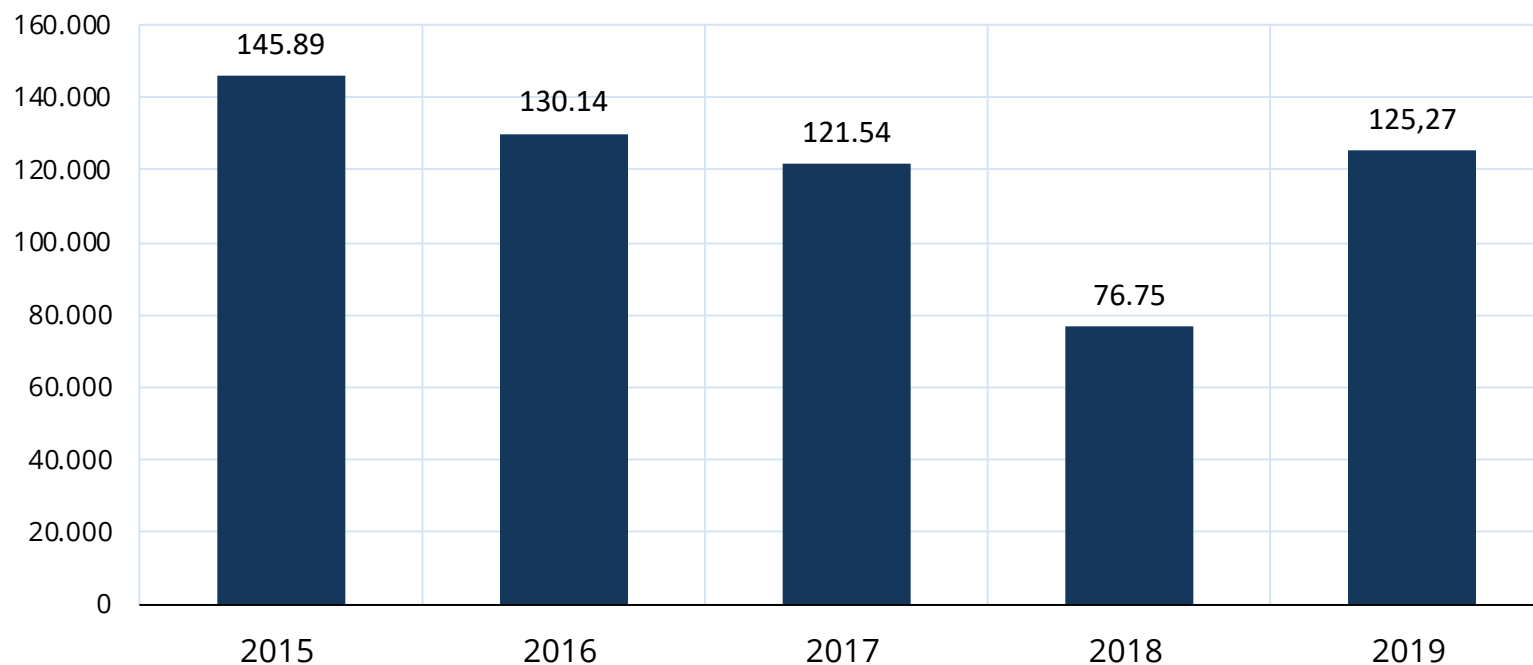
2019 summary

- ✓ **Low rates and good liquidity conditions have boosted the issuing activity of non-financial companies.**
- ✓ **Recovery of issuances from financial institutions**, with a special **role played by mortgage-backed and regional bonds**, which recovered to once again see major levels of activity, **and hybrid fixed-income issues (CoCos, AT1s, subordinated debt, senior-non-preferred debt)**, made by credit institutions to cover their liquidity ratios.
- ✓ **Recovery of securitisation fund issuances**, which have begun to see trading activity once again with the regulatory measures of standardisation and improvements in reporting.
- ✓ **Issuances made and registered by Spanish companies and business groups in other markets reached 69.48 billion euros up to September 2019 (Source: CNMV), exceeding the 55.13 billion euros issued and registered in Spain in that period.** Both the CNMV and the Spanish fixed-income markets managed by BME are trying to introduce measures that simplify issuance and admission in the Spanish markets and this has already seen the return to Spain of some issuers, including Endesa, Colonial, Aena and various financial institutions.

Primary market Spanish private debt AIAF market. Admissions to trading (2015-2019)

Volume of admissions to trading

Figures billions of euros. Source: BME

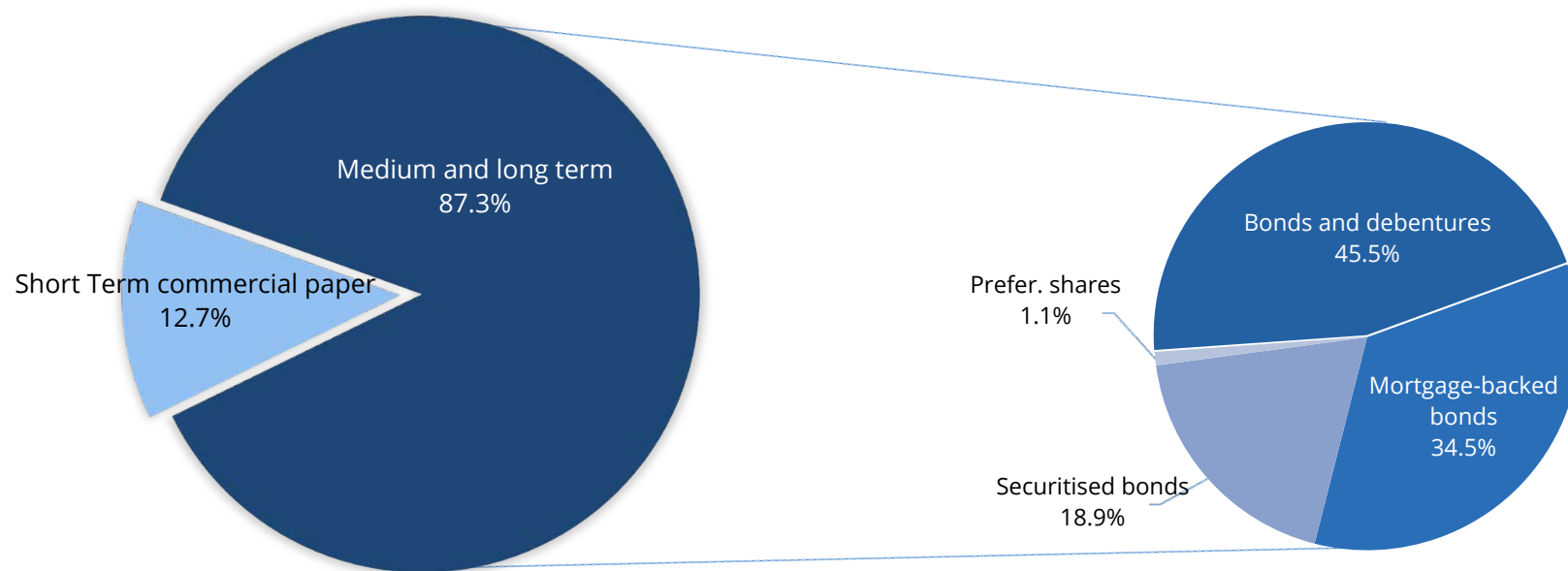


The total volume admitted to trading in 2019 reached EUR 125.27 billion, representing an increase of 63% on the previous year.

Primary market Spanish private debt AIAF market. Admissions to trading

Admissions to trading by terms and type in 2019

Source: BME

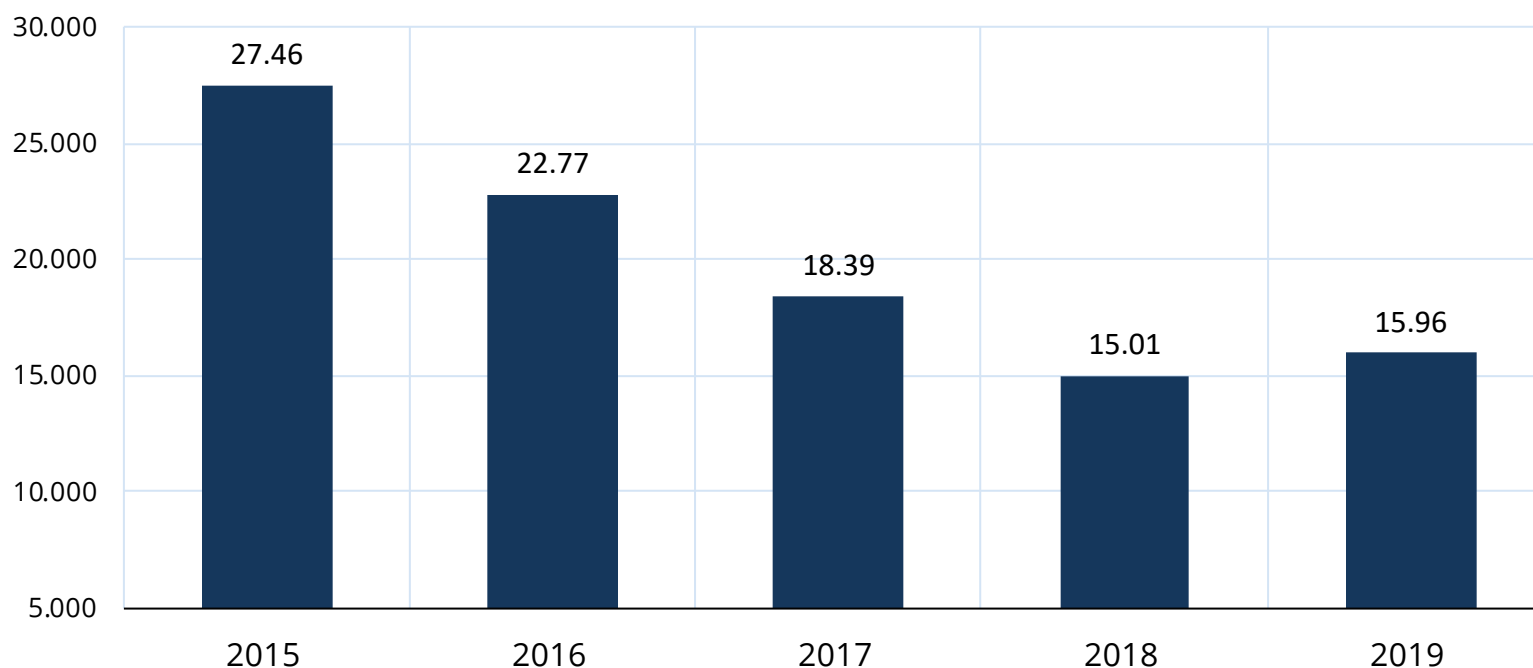


In a very favourable interest rate environment, medium- and long-term issuances gain weight

Primary market Spanish private debt AIAF market. Short term commercial paper

Volume of admission to trading of commercial paper (2015-2019)

Figures in billions of euros. Source: BME



After the sharp decline in previous years, 2019 saw a slight rebound in commercial paper issuances.

AIAF market

Total outstanding balances. Summary 2019

- ✓ **In 2019, the outstanding balance of Spanish government debt securities in the BME AIAF fixed income market grew at an annual rate of 2.1%, to 1.02 trillion euros.** Treasury issuances account for the heaviest weighting, with 68.34 million euros in bills and 915.58 billion in bonds and debentures.
- ✓ The outstanding balance of Autonomous Communities debt stands at 35.25 million euros. Of particular note, was **the return of the Balearic Islands, Castilla y León, Andalusia and the Principality of Asturias to the issuance markets** during 2019, after having no fixed income activity in recent years.
- ✓ **The outstanding balance of private fixed-income issuances in the AIAF market reached 463.80 billion euros at the end of the year.** The 31% growth in the balance of straight bonds and debentures issuances stands out.

AIAF market. Secondary market

Outstanding balances of government debt and private debt

Data at the end of 2019 in billions of euros and number. Source: BME

OUTSTANDING BALANCE

	SHORT TERM	MEDIUM AND LONG TERM
Private fixed income	6.38	457.36
Government fixed income	68.34	979.56
Foreign government fixed income	--	4,914.79
TOTAL	74.71	6,351.70

NUMBER OF ISSUANCES (ISIN) OUTSTANDING

	MEDIUM AND LONG TERM
Private fixed income	1,848
Spanish government fixed income	442
Foreign government fixed income	508
TOTAL	2,798

AIAF market

Secondary market

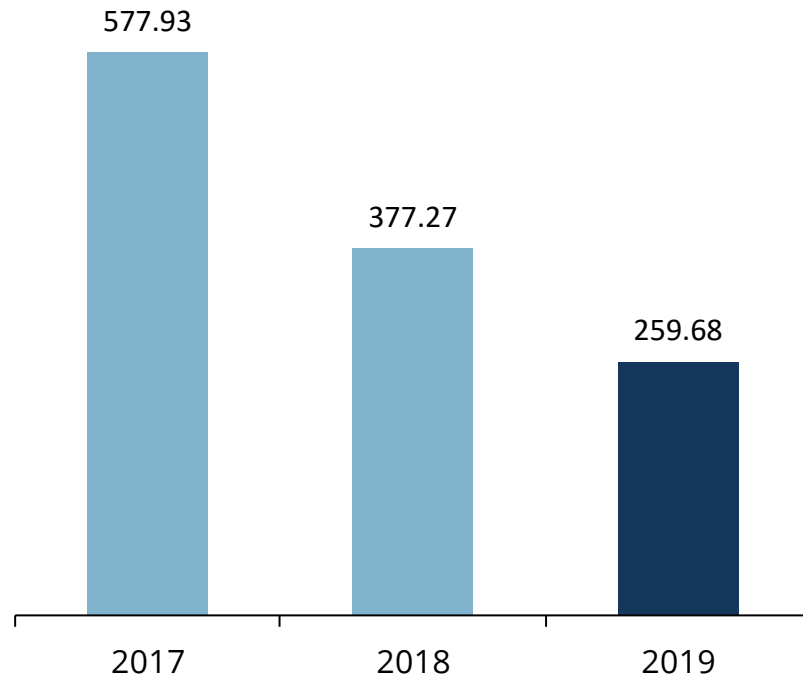
- ✓ This was the second year that the **MiFID II regulation was applied to fixed income**. It brings more rigorous market and transparency rules, similar to those governing equity markets.
- ✓ There has been an intensification in the global and, in particular, European trend towards **increased fixed-income trading via electronic platforms** with the introduction of the new regulation.
- ✓ **Members** are also turning to the electronic markets and fixed income trading systems managed by BME **to meet their transparency and reporting obligations resulting from the application of the regulation**.
- ✓ **Treasury issuances from Germany, France, the Netherlands, Belgium, Italy, Austria, Portugal, Ireland, Greece and the European Stability Mechanism (ESM) have been admitted to the platform** and have already attained an outstanding balance of 4.9 trillion euros.

AIAF market

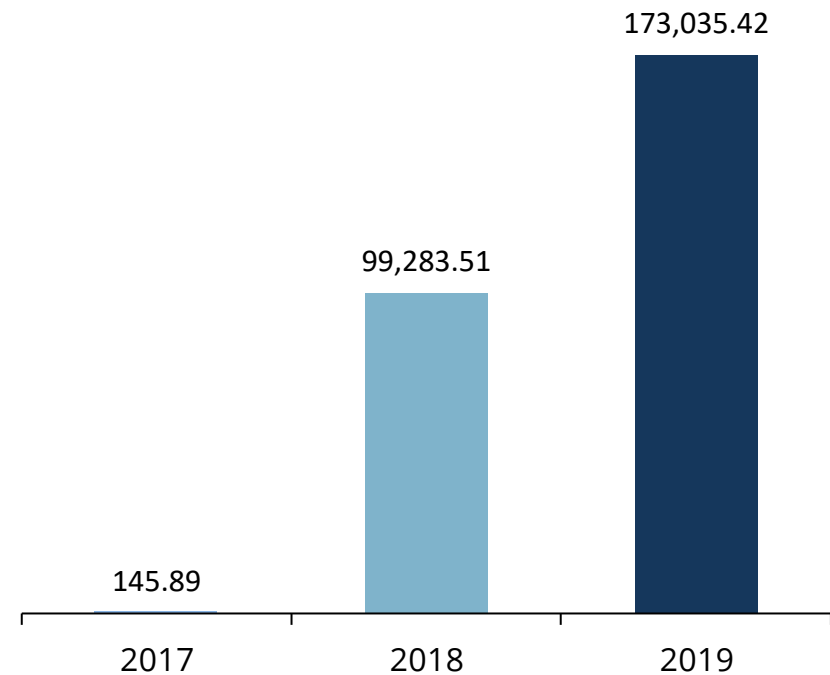
SEND platform. Volume traded

Figures in millions of euros. Source: BME

SEND. Private debt trading



SEND. Government debt trading

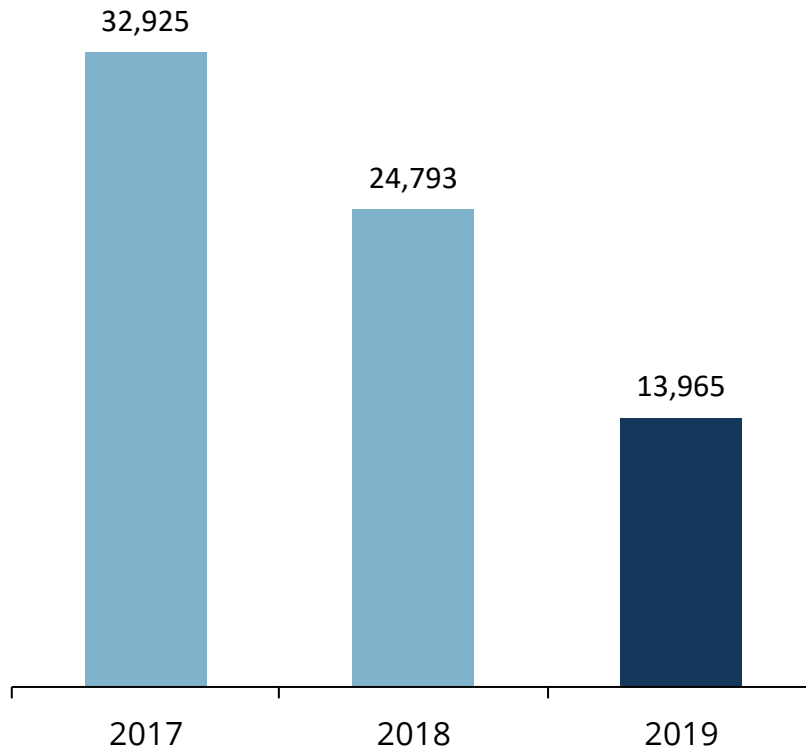


AIAF market

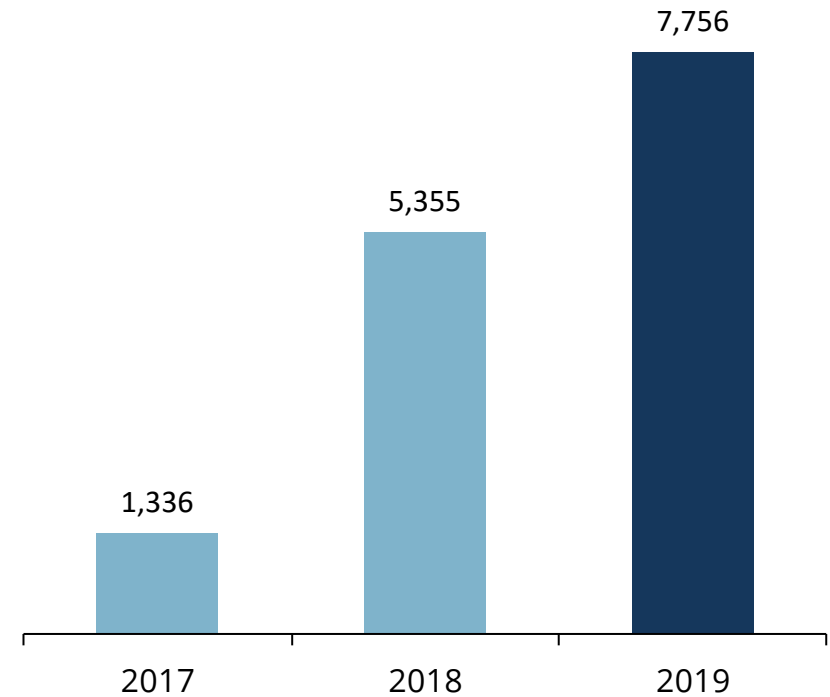
SEND platform. Trades

In number of trades. Source: BME

SEND. Private debt trades



SEND. Government debt trades

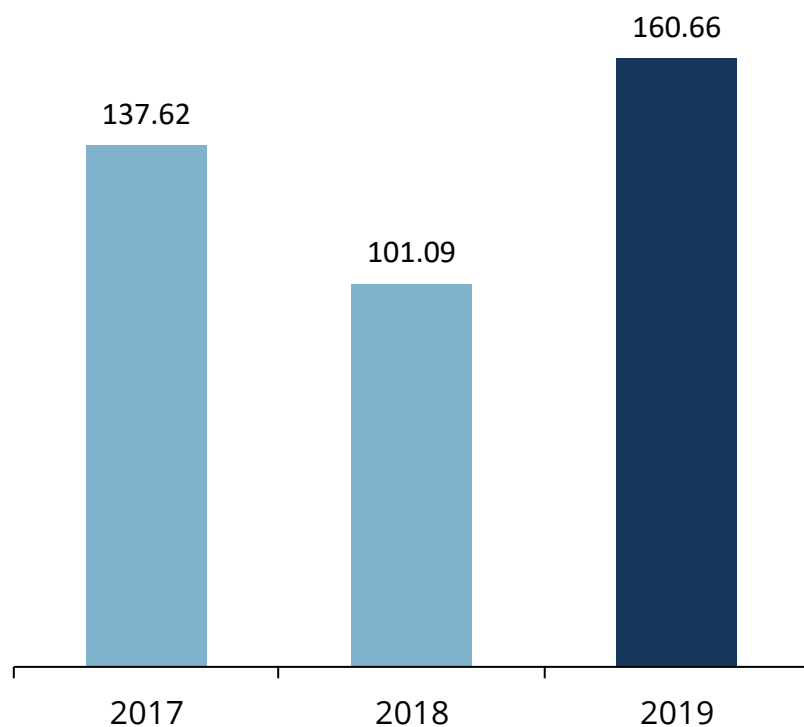


SENAF platform

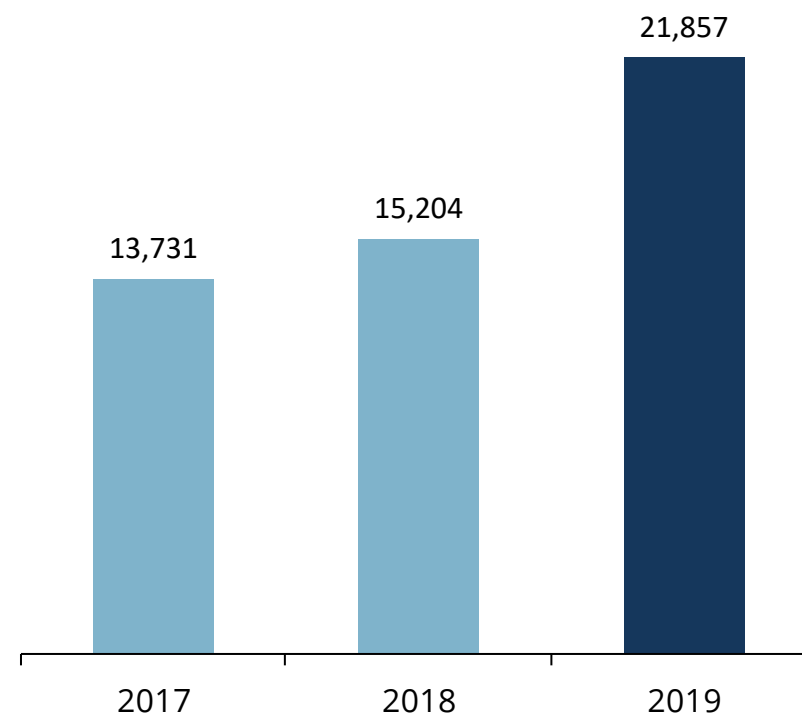
Volume and trades

Data in billions of euros and number of trades. Source: BME

SENAF. Cash volume



SENAF. Number of trades

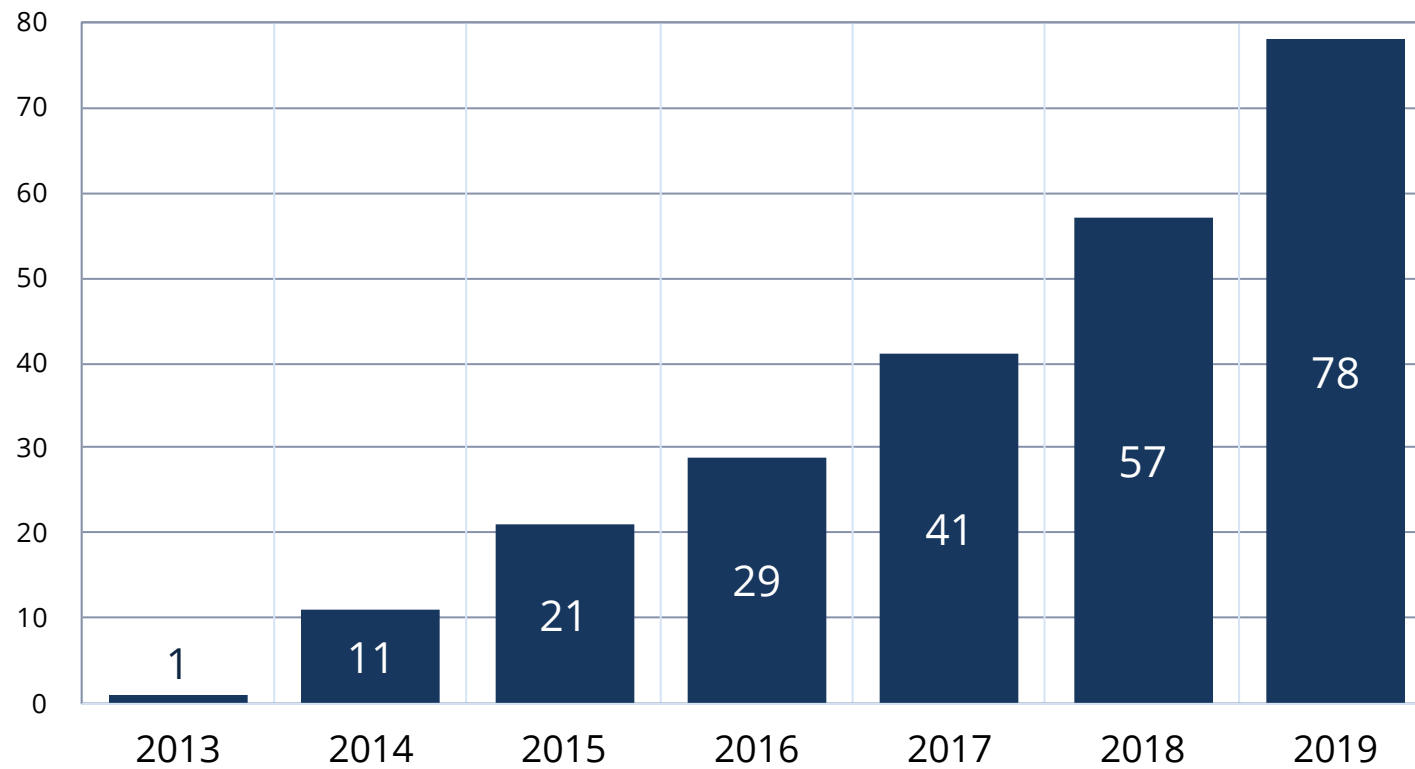


MARF

- ✓ **The Alternative Fixed Income Market (MARF) has grown steadily in its six years of operation** and it has acquired a major role among the various alternatives available which are helping to increase diversification in sources of business financing in Spain.
- ✓ **From its launch up to 2019, 78 companies have used it for funding.** Six of these are Portuguese.
- ✓ **MARF closed 2019 with an outstanding balance of corporate debt issuances of 5,115.3 million euros, with growth of 54%** compared to the end of the previous year.
- ✓ **A total of 52 companies used the MARF** to cover their financing needs in 2019, either through the registration of commercial paper programmes or the launch of bond issuances. Of these, **18 were using it for the first time.**
- ✓ The volume of **issuances and admissions** to trading in the MARF in the whole of 2019 **amounts to 10,357.3 million euros, 63% more than the previous year.**

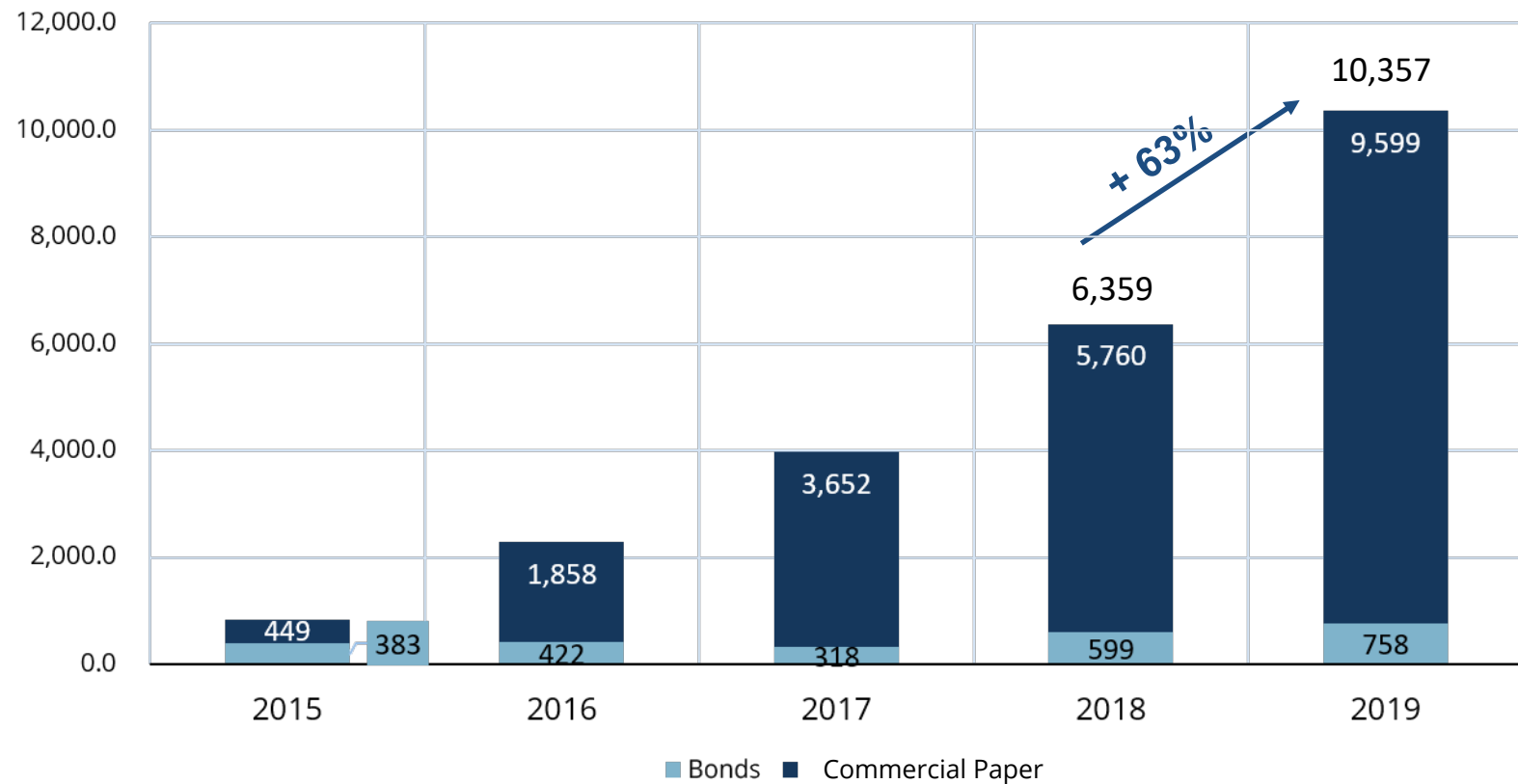
Companies financed since its launch (2013-2019)

Accumulated data from 2013 until the end of each year. Source: BME



Volume of issuances and admissions to trading (2015-2019)

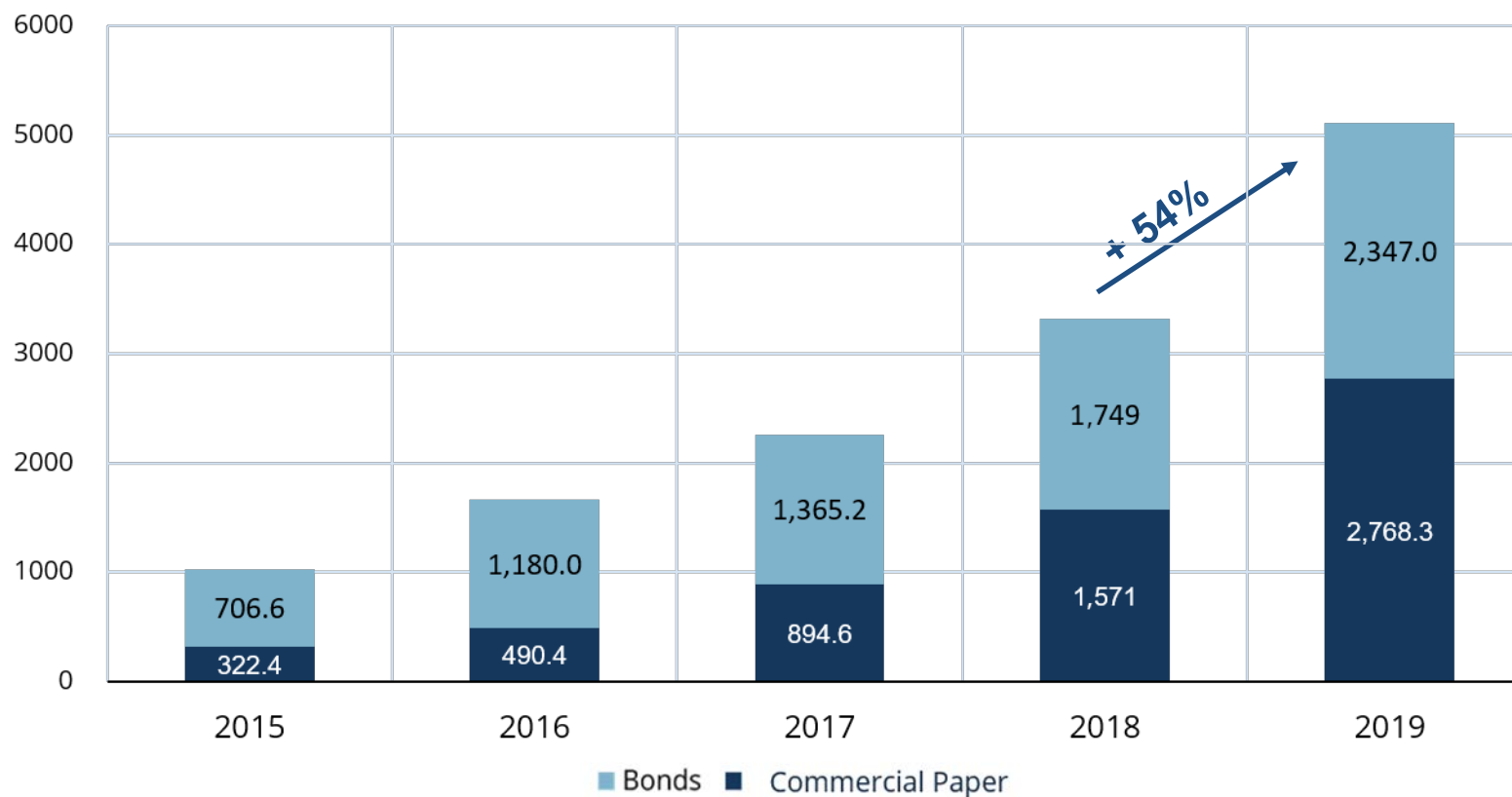
Figures in millions of euros. Source: BME



In 2019, the volume of issuances and admissions to trading in the MARF amounted to 10.36 billion euros, 63% higher than in 2018.

Outstanding balance at the end of the period (2015-2019)

Figures in millions of euros. Source: BME



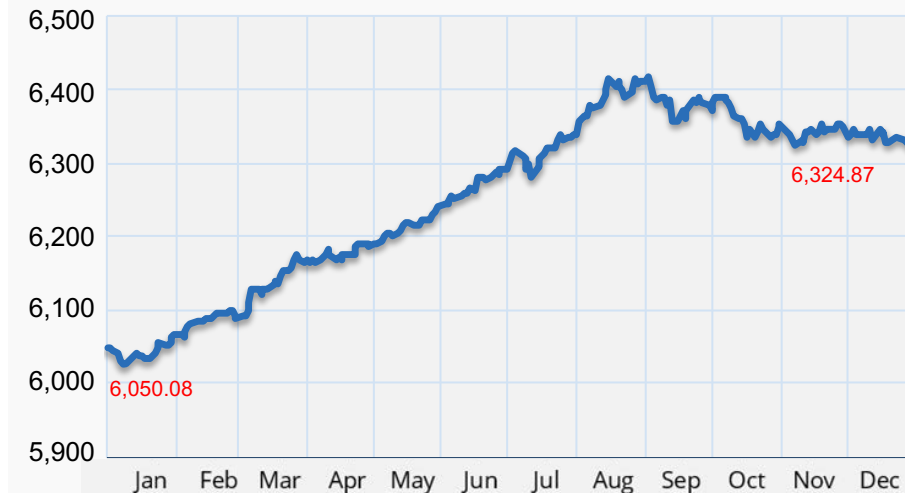
The MARF had an outstanding balance of corporate debt issuances of 5,115.3 million euros at year-end 2019, comprising just over 2,768 million euros in commercial papers and 2,347 million euros in various types of bond issues. The outstanding balance grew 54% compared to the end of 2018.

AIAF 2000 indices in 2019

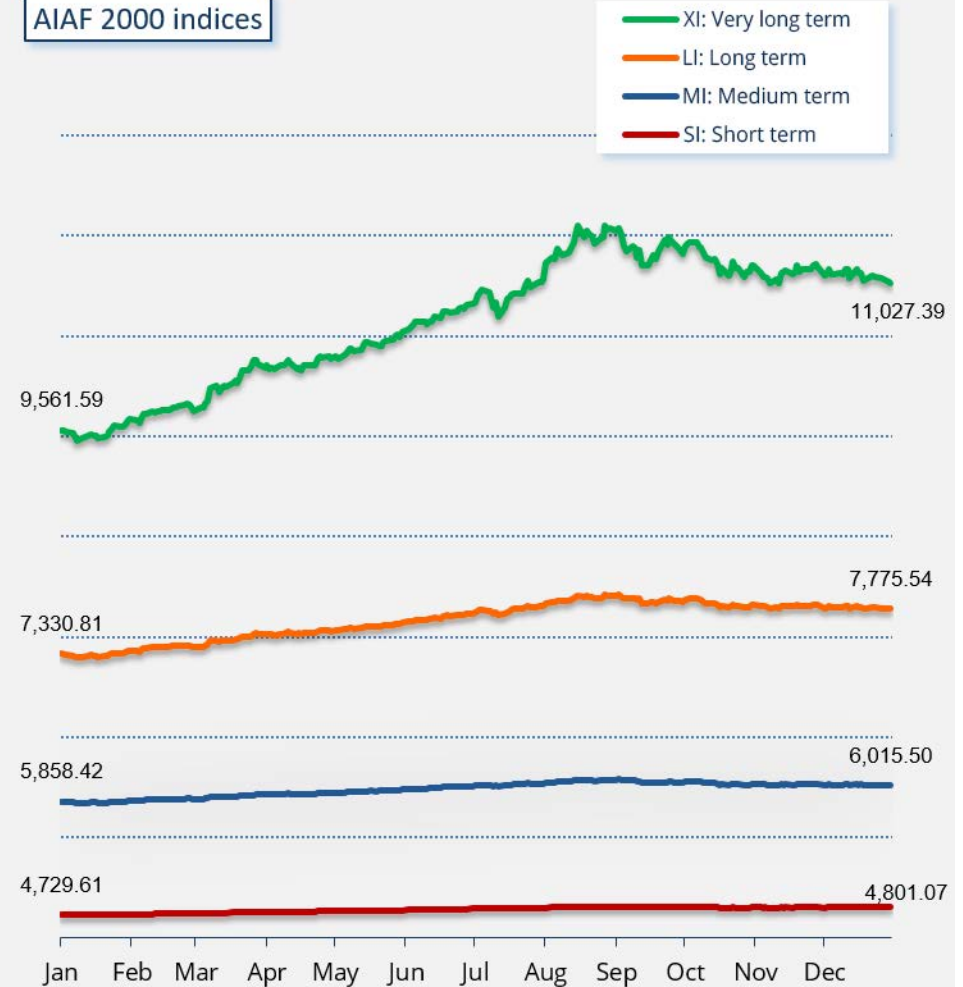
Source: BME

Performance of AIAF 2000 indices					Duration			
	Index	High	Low	Last	Average	High	Low	Last
GI	General	6,417.29	6,026.61	6,324.87	4.61	4.68	4.49	4.49
SI	Short	4,812.67	4,725.38	4,801.07	1.92	1.99	1.83	1.83
MI	Medium	6,080.55	5,839.41	6,015.50	3.67	3.79	3.57	3.76
LI	Long	7,922.65	7,291.22	7,775.54	5.84	6.12	5.49	5.49
XI	Very long	11,605.44	9,459.74	11,027.39	11.98	12.19	11.65	11.65

AIAF 2000 General Index



AIAF 2000 indices



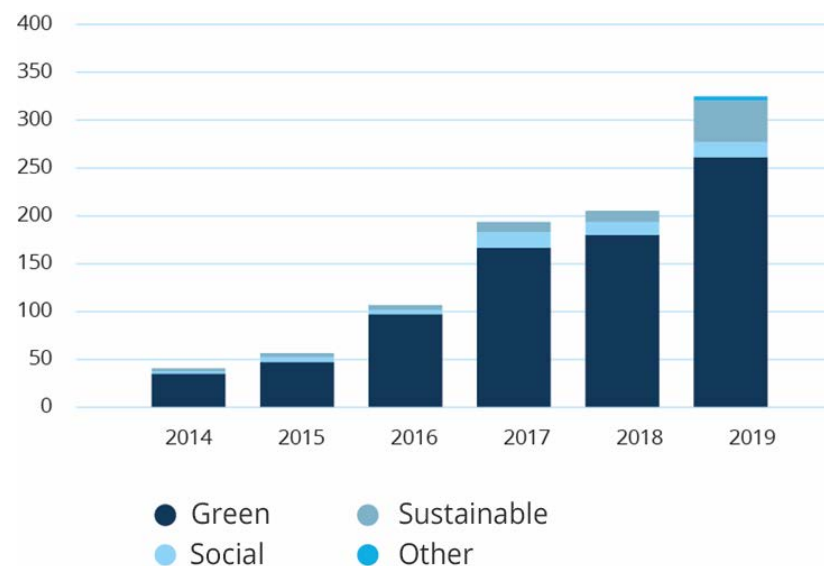
SUSTAINABLE FINANCING: Green, social and sustainable bonds

Global sustainable financing

- ✓ There has been a **huge global expansion** in **sustainable financing** in recent years, particularly in Europe.
- ✓ This results from a **change in the regulatory architecture**. The market was developed in Europe following mainly private standards: Green Bonds Principles from organisations like ICMA or the Climate Bonds Initiative.
- ✓ Further to its Action Plan on Sustainable Finance, the **European Commission has published a new green bond taxonomy**, definition of standards and approved metrics, etc.

Global development of sustainable financing

Figures in billions of USD. Source: Ofiso



Sustainable financing in Spain

- ✓ In Spain, **public and private companies, banks, the autonomous communities and public agencies issued green, social and sustainable bonds amounting to 9,756 million euros in 2019**. This figure is an increase of over 9 times the volume of 2014 and of 2015.
- ✓ **Spain was among the top-ten countries in the world** for sustainable bonds in 2018 and 2019, above other bigger economies (Source: Climate Bonds Initiative and IMF)

Sustainable financing in Spain. Volume of bond issues by type

Figures in billions of euros.
Source: Ofiso



Sustainable issuances market

- ✓ **Debt issuances linked to sustainability already form a market segment that has its own specialised participants, issuers and investors**, and its own dynamics. The type of issuances that are made, combine their financial function with an environmental and social purpose, within the framework of the United Nations' Sustainable Development Goals (SDGs).
- ✓ Not only have large companies and public sector institutions, which are usually the focus of these types of transactions, made bond issues with sustainable criteria, but **smaller companies have too. In October 2019, the MARF registered its first green bond issuance**, which was made by **Greenergy**. This 50 million euro programme will allow the company to diversify its sources of long-term financing and **to gain access to investors who support ESG criteria**.
- ✓ **BME actively participates in the United Nations' Sustainable Stock Exchanges initiative**, promoting sustainable financing in its markets and transparency through the development of sustainability indices or metrics (such as the FTSE4Good Ibex® index), financial education and the promotion of events related to sustainability.

ECONOMIC AND MARKET OUTLOOK

Economy

- ✓ **International.** The exponential spread of **Covid-19** has decimated forecasts for both the global and, in particular, the European economies. At the end of the first quarter of 2020, forecasts suggest that it is **possible that the entire global economy could go into recession, something which is already taken for granted for the European Union**. This would involve the loss of at least 2.5 points of GDP, which would lead to a drop in output of at least 1.1% according to the European Commission.
- ✓ **Markets.** In March, the expected global economic slowdown triggered **falls of over 30% in many world stock markets**, and has taken **yields on those bonds considered as safe haven assets to all-time lows**. The price of **oil**, in the middle of a price war, **has fallen by more than 50%**.
- ✓ **Spain.** The **likelihood of the economy going into recession in this first quarter and in the whole of 2020 are increasing**, although the final impact will depend on the tourist season. The Government has introduced **measures to protect businesses and jobs**.

Interest rates and government debt in Europe and Spain (I)

- ✓ **Central bank action is crucial in countering the public health crisis** alongside fiscal measures. Both individual and concerted measures are being put in place to guarantee liquidity and credit.
- ✓ **The Fed has already made two rates cuts**, on 3 March and 15 March (unscheduled and on a Sunday), **to take its intervention rates from 1.5% to a range between 0% to 0.25%**. Additionally, they announced **USD 700,000 million in asset purchases** (USD 500,000 million in Treasury Bonds and USD 200,000 million in mortgage-backed assets, which can subsequently be extended without limit of amount and time). It also announced **USD 1.5 billion of liquidity injections at one and three months, intervention in the repo market of USD 1 billion a day and daily liquidity provision in USD.**

Interest rates and government debt in Europe and Spain (II)

- ✓ The ECB's package of **measures, launched on 12 March and 18 March**. An easing of the applicable costs and conditions in order to be able to **provide almost unlimited liquidity to the TLTRO-III programme** for bank financing; and the launch of two new **purchase programmes of 120,000 million and 750,000 million euros in more flexible public and private assets**, to avoid the financial fragmentation of the euro area.
- ✓ **German and US government debt** have become **safe-haven assets**, and their yields have returned to historical lows. **There was a rise in the risk premiums of those European countries initially most affected by the pandemic, which has been corrected by the ECB's intervention.**

European fixed-income markets and BME

- ✓ **The process of adaption to MiFID II will continue for European fixed-income markets** and the redistribution of activity between various trading platforms and systems will continue.
- ✓ In line with the regulation's objectives, **trading in OTC fixed-income markets will gradually decrease in the European Union.**
- ✓ **BME's fixed-income markets and platforms aim to enhance their usefulness for issuers and investors**, by optimising their admission to trading procedures for various types of fixed-income issuances, and also their fee structures.



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