THE SPANISH ECONOMY:

MONTHLY REPORT

NOVEMBER 2004

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Research Department

"la Caixa"

Forecast

% change over same period year-before unless otherwise noted

	2003	2004	2005	2003 3rd Qtr.	2003 4th Qtr.	2004 1st Qtr.	2004 2nd Qtr.	2004 3rd Qtr.	2004 4th Qtr.
INTERNATIONAL ECONOMY		Forecast						Forecast	
Gross domestic product									
United States	3.0	4.3	3.2	3.5	4.4	5.0	4.8	3.9	3.5
Japan	2.5	4.2	1.8	1.8	3.5	5.1	4.3	4.0	3.2
United Kingdom	2.2	3.2	2.5	2.2	2.9	3.4	3.6	3.0	2.7
Euro area	0.5	1.9	2.0	0.4	0.7	1.4	2.0	1.9	2.2
Germany	*–0.1*	*1.7*	*1.5*	*–0.3*	*0.0*	*0.8*	*1.5*	*1.9*	*2.5*
France	*0.5*	*2.5*	*2.3*	*0.4*	*1.0*	*1.6*	*2.8*	*2.7*	*2.7*
Consumer prices									
United States	2.3	2.6	2.3	2.2	1.9	1.8	2.9	2.7	3.1
Japan	–0.3	–0.1	0.1	–0.2	–0.3	–0.1	–0.3	–0.1	0.1
United Kingdom	2.8	2.3	2.4	2.9	2.6	2.3	2.2	2.1	2.4
Euro area	2.1	2.2	2.0	2.0	2.0	1.7	2.3	2.2	2.3
Germany	*1.1*	*1.7*	*1.5*	*1.0*	*1.2*	*1.1*	*1.8*	*1.9*	*2.2*
France	*2.1*	*2.2*	*1.7*	*1.9*	*2.2*	*1.8*	*2.4*	*2.3*	*2.2*
SPANISH ECONOMY									
Macroeconomic figures									
Household consumption	2.9	3.2	2.7	3.0	2.9	3.3	3.2	3.1	3.0
Government consumption	3.9	4.3	4.1	3.8	4.2	4.3	4.3	4.2	4.3
Gross fixed capital formation	3.2	3.7	3.9	3.1	2.6	2.7	3.9	4.0	4.0
Capital goods and other	*1.7*	*2.9*	*3.0*	*1.7*	*0.7*	*0.8*	*3.6*	*3.7*	*3.5*
Construction	*4.3*	*4.1*	*3.7*	*4.1*	*4.2*	*4.3*	*4.2*	*4.1*	*4.0*
Domestic demand	3.2	3.5	3.0	4.1	3.5	3.5	3.8	3.5	3.4
Exports of goods and services	2.6	4.3	5.7	3.1	1.6	5.5	4.7	3.8	3.2
Imports of goods and services	4.8	7.1	7.0	7.9	3.7	7.8	8.1	6.6	5.9
Gross domestic product	2.5	2.6	2.5	2.6	2.8	2.7	2.6	2.5	2.5
Other variables									
Employment	1.8	2.0	1.8	2.0	2.1	2.1	2.0	2.1	1.9
Unemployment (% labour force)	11.3	10.8	10.5	11.2	11.2	11.4	10.9	10.5	10.5
Consumer price index	3.0	3.0	3.0	2.9	2.7	2.2	3.2	3.3	3.4
Unit labour costs	3.5	3.3	3.3	3.4	3.2	3.2	3.2		
Current account balance (% GDP)	–3.3	–4.0	–3.8	–3.5	–2.6	–5.0	–6.0		
Net lending or net borrowing rest of the world (% GDP)	–2.1	–2.8	–2.7	–2.6	–0.9	–4.4	–4.6		
Government balance (% GDP)	0.3	–0.8	–0.3						
FINANCIAL MARKETS									
Interest rates									
Federal Funds	1.1	1.3	3.1	1.0	1.0	1.0	1.0	1.4	1.9
ECB repo	2.3	2.0	2.3	2.0	2.0	2.0	2.0	2.0	2.0
10-year U.S. bonds	4.0	4.4	5.4	4.2	4.3	4.0	4.6	4.3	4.5
10-year German bonds	4.1	4.2	5.1	4.1	4.3	4.1	4.2	4.1	4.3
10-year Spanish bonds	4.1	4.2	5.2	4.1	4.3	4.1	4.2	4.2	4.3
Exchange rate									
$/Euro	1.13	1.23	1.20	1.12	1.19	1.25	1.20	1.22	1.25

”la Caixa” GROUP: KEY FIGURES
As of December 31, 2003

FINANCIAL ACTIVITY	Million euros
Total customer funds	126,281
Receivable from customers (including securitizations)	79,130
Group income	840

STAFF, BRANCHES AND MEANS OF PAYMENT	
Staff	24,338
Branches	4,735
Self-service terminals	6,939

”la Caixa” FOUNDATION	
Budget for 2004 (million euros)	183.5
Science Museum (number of visitors)	194,893
«CosmoCaixa» (number of visitors)	807,545
Exhibitions	295
Concerts and musical events	384
Recreation Clubs for elderly	544
Fellowships for study abroad (1982-2003)	1,688

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ECONOMIC OUTLOOK FOR 2005

The world economic situation would present an excellent appearance (apart from the imbalances shown by the U.S. economy) if it were not **for the continuing increase in oil prices** taking place all year. According to the IMF, **the world economy in 2004 has been showing its biggest growth in recent decades**. The United States is operating as the engine of world demand while China, Japan and a large part of the emerging Asian economies are going through one of the most brilliant periods in their history.

Maintenance of crude oil prices at current high levels could have negative effects on growth and inflation although with much less importance than in previous energy crises. In any case, there do not seem to be unresolvable problems in oil supply so that it is generally expected that oil prices will be adjusted in coming months. In this case, it is felt that, following growth of somewhat more than 4% in 2004, the U.S. **economy will continue to slacken in the course of the coming year** when it will reach a level of 3%-4%. Nor will 2005 bring a repetition of the extraordinary growth seen in 2004 in the Asian region where growth will be somewhat more moderate.

In the euro area, following **confirmation of recovery** in 2004, although at very modest growth levels, it is expected that 2005 will run along the same lines. Growth of 2% for this year is now taken as given while for the coming year forecasts are discounting any later increase due to the effect of the increased cost of energy. In the matter of prices, no pressures are to be expected but it is hard to see prices dropping below the rate of 2% in the harmonized consumer price index.

The central banks are indicating moderate increases in reference rates. It is expected that the Federal Reserve **will continue its moderate increases in coming months** putting its interest rates above those of the European Central Bank. The latter, in turn, will also slightly tighten monetary policy over the course of next year.

With regard to Spain's economy, economic activity continues to grow at a fairly stable rate aided by the strength of consumption and construction. For the moment, the good state of the labour market (the Labour Force Survey showed the creation of 190,000 net jobs in the third quarter) and low interest rates continue to support the performance in consumption. Nevertheless, the rise in fuel prices may have a negative effect on consumer and corporate confidence, thus slightly lowering economic growth. In overall terms, **it is expected that the gross domestic product will grow by 2.6% in 2004 and around the same level in 2005**, due to a slight slackening of the current strong growth rate of domestic demand. **The increase in oil prices has significantly worsened inflation prospects** which, at the end of the year, could reach an annual rate of close to 3.5% to later gradually decrease during 2005 if, as expected, there is some lessening of current pressure on oil prices.

October 28, 2004

ECONOMIC SITUATION

Oil main risk for economy

Oil at more than 50 dollars a barrel remains threat to economic recovery.

The threat to the world economy from the current high level of oil prices grew worse in October. After going above the psychological barrier of 50 dollars a barrel for Brent quality oil at various sessions during the month, the possibility of any rapid change in the situation has lessened. In the current context of increasing world demand for crude oil and refined products as well as being at the beginning of the winter season, it is not expected that supply will increase to any appreciable extent given the low level of surplus production in the main producing countries.

While impact not comparable to Seventies and Eighties, IMF and European Commission foresee lower growth in 2005…

While in historical perspective current prices are not comparable to those during the shocks which took place in the Seventies and the Eighties of last century (oil would have to stand at 80 dollars a barrel to equal the high figures reached at the beginning of the Eighties in real terms), they do represent a tangible threat over the short term. In recently published forecasts, both the International Monetary Fund (IMF) and the European Commission recognized that oil prices may jeopardize growth forecast for 2005.

…so that world economy will grow by 4.3% with euro area up by approximately half that figure.

The IMF now expects that next year the world economy will grow by 4.3%, one decimal less than forecast last Spring, with special impact on the advanced economies and particularly in the United States (annual increase of 3.5% forecast for 2005). The prospect for Europe is rather similar. The European Commission has lowered its growth forecast for the euro area by three decimals indicating that the gross domestic product (GDP) would reach an annual growth of only 2.0% next year.

On other hand, 2004 will end with economic level better than expected a few months ago…

On the other hand, the international bodies are confident that 2004 will end with better figures than those anticipated only a few months ago. The United States and Japan will go above 4%, twice the growth rate in the euro area, with no excessive rise in prices. Latest available indicators certainly support this impression when we see the impact on inflation and economic growth being so low. In the United States and Japan economic activity in the third quarter held at an acceptable rate while in the euro area we note some economic improvement although starting out from very low levels.

…and consumer prices have managed to take up part of the increased price of oil.

Consumer prices, in turn, in the three large world economic areas are showing a notable capacity to absorb pressure from oil prices. The year-to-year inflation rate in the United States and the euro area dropped by two decimals in September going to 2.5% and 2.1% respectively. In Japan, consumer prices even sharpened their rate of decrease in August putting the drop at 0.2% year-to-year.

Fed and European Central Bank maintaining course on monetary policy…

In the current situation, which combines the current impact of oil, moderated in terms of growth and prices, with less positive prospects for the coming year, the central banks have opted to maintain their general directives on monetary policy unchanged. In October, with no meeting of the Federal Open Market Committee of the Federal Reserve Board taking place, attention was centred on the Governing Council of the European Central Bank on October 7 which, as expected, maintained its reference interest rates unchanged.

…but prospects of lower growth and relative containment of inflation put long-term interest rates at low levels.

In this situation, long-term interest rates have sharpened the downward trend begun last June, thus reflecting the perception in the markets that costly oil would have a more appreciable effect on growth than on inflation. Specifically, the yield on U.S. Treasury bonds held below 4% at the end of October while German government bonds stood somewhat lower. The stock markets, in turn, took advantage of the first half of October to mark up notable increases to later on partly correct that upward move. Some European markets, such as Milan and London, even recorded annual highs in October.

Spain: moderate slowdown in economic activity

Spain's economy enjoying good level of activity thanks to strength of domestic demand although third quarter somewhat less expansionist.

Spain's economy did not manage to avoid the above trends although it maintained a positive differential in economic activity compared with its immediate neighbours in the euro area. In the third quarter, indicators pointed to a moderate slowdown in economic activity which, in any case, will not likely be very extensive given that strong support from buoyant domestic demand is continuing. This performance basically arises from maintenance of the drive in consumption and investment.

Current account deficit doubles in one year.

In contrast to the strength of domestic activity stands the increasing imbalance with abroad. The current account balance in July recorded a deficit of 3.7 billion euros, putting the cumulative balance for the past twelve months at 30 billion euros, a figure twice that for one year earlier. This worse position is spread over all headings of the balance of payments but especially notable is the increase in the trade deficit and the lower surplus in services.

Industrial activity slowing down, construction maintaining strength, foreign tourism slackening but domestic tourism increasing.

On the supply side, the main new factor shows up in industrial activity which has confirmed stabilization of growth. In spite of this, the strength seen in construction, especially with regard to current indicators, continues to act as a key support for Spain's growth. The situation in the tourist sector is more qualified, combining as it does a good situation in domestic tourism with a weaker picture in foreign tourism, a segment which recorded an increase in the total number of foreign tourists while, at the same time, showing a decrease in revenue inflows. Finally, if we look at the indicators for supply and demand we find that the impact of higher priced oil so far is restricted to a worsening of consumer confidence, which in September showed its lowest level in the past twelve months, along with the increase in fuel prices.

Inflation drops to 3.2% thanks to moderating effect of fresh food prices, but in view of high-cost oil immediate prospects not bright.

In fact, among key aspects of the present national economic picture emphasis may be placed on the relative containment of inflation in spite of the notable pressure on prices of oil products. The decisive factor making it possible to contain the consumer price index at 3.2% in September was the positive contribution coming from fresh foods. In any case, the increase in the consumer price differential with the euro area as of September and the prospect of further pressure from oil prices somewhat darken any evaluation made about inflation.

Job creation increasing although job quality not improving.

At the same time, the trend in employment presents a number of ups and downs. With 190,000 new jobs created in the third quarter, a figure 2.5% higher than one year ago, the rate of job creation remains healthy. Nevertheless, the notable increase in part-time hiring and the rise in temporary jobs, along with the increase in employment among those under 20 years of age linked to hiring specifically for the holiday period, is a reminder of the continuation of certain deficiencies in the matter of quality in the jobs created.

Budget stability, support for productivity and more attention to social policy are three key aspects of 2005 central government budget.

In the face of this economic situation, the Spanish government has presented its 2005 budget which combines greater emphasis on social matters and an effort to deal with those factors affecting competitiveness, while at the same time staying within the framework of fiscal discipline established by the General Law on Budgetary Stability. Specifically, forecast consolidated spending will increase by 7.8% compared with the 2004 budget, that is to say, 1.5 points above nominal growth of the GDP, while revenues will go up by 6.5% compared with the previous budget. The consolidated budgetary balance forecast for 2005 (the sum of balances of the central government, Social Security and other public entities and bodies), if accrual criteria are applied, will be positive amounting to 0.2% of the GDP. Debt of the central government and government bodies as a whole will stand at 47% of the GDP.

CHRONOLOGY

2003

March	**20**	*United States and its allies begin* ***war against Iraq*** *to depose Saddam Hussein regime.*
April	**27**	*Coming into force of group of* ***economic reform measures*** *aimed at reducing cost of mortgage loans, fostering female employment, improving scheme for self-employed persons under Social Security and access of young people to rental housing, as well as improving tax treatment of small and medium-size companies (BOE 26-4-03).*
May	**25**	***Elections*** *for local government and autonomous communities.*
June	**5**	***European Central Bank*** *cuts official interest rate by 50 basis points to 2.00%, the second reduction this year.*
September	**14**	*Sweden rejects adoption of* ***euro*** *in referendum.*
		World Trade Organization *summit in Cancun (Mexico) ends without agreement.*
November	**1**	*Jean-Claude Trichet, former governor of French central bank, takes over from Willem F. Duisenberg as* ***chairman of European Central Bank****.*

2004

January	**1**	***Central government budget for 2004*** *comes into force (BOE 31-12-03).*
February	**11**	*Dow Jones index for* ***New York stock exchange*** *records annual high (10,737.7), rise of 2.7% compared with end of 2003.*
	17	***Euro*** *running at 1,286 dollars, highest figure since launching of single currency at beginning of 1999.*
March	**11**	*Tragic* ***terrorist attacks*** *on commuter trains in Madrid.*
	14	*Victory of Spanish Socialist Workers Party (PSOE) in Spanish* ***general elections****.*
April	**13**	*IBEX 35 index for* ***Spanish stock market*** *records annual high (8,444.3), a cumulative gain of 9.1% over end of December 2003.*
May	**1**	*Enlargement of the* ***European Union*** *by ten new member states making a total of 25.*
June	**18**	*Summit meeting of European Council in Brussels approves* ***European Constitution*** *which must be ratified by member states of European Union.*
September	**21**	***Federal Reserve Board*** *raises target level for third time this year putting it up a quarter-point to 1.75%.*
October	**25**	*One-month forward price of Brent quality* ***oil*** *reaches record level of 51.51 dollars a barrel.*

AGENDA

November

2 *Presidential elections in United States.*

4 *Meeting of Governing Council of European Central Bank.*

5 *Industrial production index (September).*

10 *Meeting of Open Market Committee of Federal Reserve Board.*

12 *Consumer price index (October).*

17 *Harmonized consumer price index for European Union (October).*

24 *Quarterly National Accounts (3rd Quarter).*

25 *Producer price index (October).*

29 *Early HCPI index (November).*

December

2 *Meeting of Governing Council of European Central Bank.*

3 *Industrial production index (October).*

14 *Meeting of Open Market Committee of Federal Reserve Board.*

15 *Consumer price index (November).*

16 *Harmonized consumer price index for European Union (November).*

17 *Quarterly Labour Cost Survey (3rd Quarter).*

22 *Ongoing survey of household budgets (3rd Quarter).*

27 *Producer price index (November).*

30 *Early HCPI index (December).*

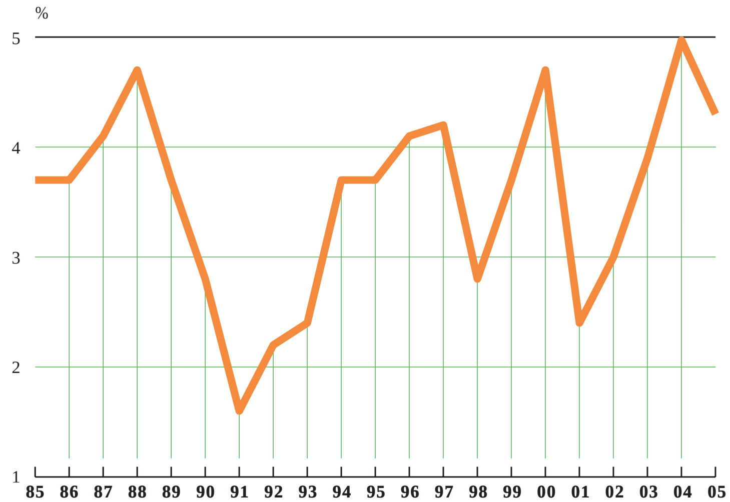
World economy undergoes biggest growth in decades

IMF expects growth of 5% in 2004 and 4.3% in 2005.

The International Monetary Fund (IMF) has made an upward revision of its previous quite optimistic forecasts for 2004 putting world growth at 5.0%. It has also slightly reduced growth in 2005 to 4.3%. Within this framework of strong growth, there was some loss of strength in the United States, Japan and China in the second quarter. As a result, while remaining strong, overall growth will be somewhat less than initially expected for 2005. The greatest risk will come from possibly lower growth with special concern about the volatility of oil prices.

WORLD ECONOMY GROWING AT STRONG RATE

Real annual change in world product



NOTES: 2004 and 2005 are forecasts.
SOURCE: International Monetary Fund.

Interest rates will move up but with notable differences between countries.

Interest rates will likely move up as recovery consolidates, although there will be notable differences between countries depending on their respective positions in the economic cycle. Nevertheless, the biggest challenge will be how to take advantage of the current economic drive in order to resolve problems of a more structural nature, improve fiscal balances and eliminate imbalances in current account, as in the case of the United States.

Asia and United States acting as bases of growth.

In spite of the weaknesses noted in the second quarter, the world economy continues to base its strength on the U.S. economy along with support from Asia. Economic activity in Latin America has moved up considerably while recovery in the euro area, although more and more established, still remains weak.

IMF FORECASTS

Annual change as percentage

	2002	2003	2004 (1)	2005 (1)
GDP				
United States	1.9	3.0	4.3	3.5
Japan	–0.3	2.5	4.4	2.3
Germany	0.1	–0.1	2.0	1.8
France	1.1	0.5	2.6	2.3
Italy	0.4	0.3	1.4	1.9
United Kingdom	1.8	2.2	3.4	2.5
Spain	2.2	2.5	2.6	2.9
Euro area	**0.8**	**0.5**	**2.2**	**2.2**
Advanced economies	**1.6**	**2.1**	**3.6**	**2.9**
World total	**3.0**	**3.9**	**5.0**	**4.3**
Developing countries	*4.8*	*6.1*	*6.6*	*5.9*
Latin America	*–0.1*	*1.8*	*4.6*	*3.6*
Eastern and Central Europe	*4.4*	*4.5*	*5.5*	*4.8*
Russia	*4.7*	*7.3*	*7.3*	*6.6*
China	*8.3*	*9.1*	*9.0*	*7.5*
Consumer prices				
United States	1.6	2.3	3.0	3.0
Japan	–0.9	–0.2	–0.2	–0.1
Germany (2)	1.3	1.0	1.8	1.3
France (2)	1.9	2.2	2.4	2.1
Italy (2)	2.6	2.8	2.1	2.0
United Kingdom (2)	1.3	1.4	1.6	1.9
Spain (2)	3.9	3.0	2.8	2.7
Euro area (2)	**2.3**	**2.1**	**2.1**	**1.9**
Advanced economies	**1.5**	**1.8**	**2.1**	**2.1**
Developing countries	*6.0*	*6.1*	*6.0*	*5.5*
Unemployment rate (3)				
United States	5.8	6.0	5.5	5.4
Japan	5.4	5.3	4.7	4.5
Germany	8.7	9.6	9.7	9.5
France	8.9	9.4	9.4	9.0
Italy	9.0	8.7	8.3	8.2
United Kingdom	5.2	5.0	4.8	4.8
Spain	11.4	11.3	11.1	10.3
World trade by volume (4)	**3.3**	**5.1**	**8.8**	**7.2**
Oil price ($ per barrel) (5)	**2.5**	**15.8**	**28.9**	**–**

NOTES: (1) Forecasts in September 2004.
(2) Harmonized consumer price index.
(3) Percentage of labour force.
(4) Goods and services.
(5) Average spot prices for Brent, Dubai and West Texas Intermediate oil. Average oil price in dollars per barrel in 2003 was $28.89, price forecast for 2004 is $37.25 and $37.25 in 2005.

U.S. current account balance continues to worsen.

In spite of this increased growth, the current account balance in the United States continued to worsen this year. This imbalance was compensated by bigger surpluses in the euro area and Japan along with continuity in other Asian economies. It is these economies especially which have made financing of the U.S. deficit possible.

Raw materials moderate increase but oil on rise and remains volatile.

Raw materials reported a rise in prices due to heavy demand combined with certain supply factors. While oil has continued to rise, showing high volatility, other raw materials seem to have eased their price increases in the first half of 2004, partly thanks to some moderation in economic activity in China. In this context, inflation has risen slightly after reaching exceptionally low levels.

United States: gradual slowdown in economic activity

Retail sales recovering in United States.

Within a tendency to slow down, the U.S. economy is maintaining a certain strength. Retail sales, which in recent months had shown some moderation, recovered their strength and grew by 7.7% year-to-year in September. Along the same lines, industrial production of consumer goods grew by 3.0% year-to-year, slightly going above the figures for previous months. On the other hand, consumer confidence held to a lower trend going to 92.8 in October, a level close to the end of 2003 although less than the 98.7 figure for August and far from the 106.4 level in June. The expectations component stood at 92.0, which was below the 97.7 figure for September. As a result, the expectations component again stood below the current situation which was 94.2 in October. This reflects some lack of consumer confidence in the face of the uncertainties of recent months.

Car sales showing irregular performance.

Car sales in September grew by 1.6% year-to-year, a notable improvement over the drop of 13.8% in August. We should point out the importance of seasonal factors in this case, although the more plausible conclusion is that at this moment this indicator does not seem to be showing a clearly upward drive.

UNITED STATES: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
GDP	1.9	3.0	3.5	4.4	5.0	4.8	–	...	–
Retail sales	2.5	5.4	6.3	6.7	7.8	7.8	6.9	4.8	7.7
Consumer confidence (*)	96.6	79.8	78.6	89.7	91.6	96.3	105.7	98.7	96.7
Industrial production	–0.6	0.3	–0.4	1.5	2.9	5.2	5.3	5.1	4.6
Sales of single-family homes	7.6	11.6	15.2	8.7	22.2	8.2	–6.4	–0.4	...
Industrial activity index (ISM) (*)	52.4	53.3	54.1	60.6	62.5	62.1	62.0	59.0	58.5
Unemployment rate (**)	5.8	6.0	6.1	5.9	5.6	5.6	5.5	5.4	5.4
Consumer prices	1.6	2.3	2.2	1.9	1.8	2.9	3.0	2.7	2.5
Trade balance (***)	–39.0	–44.4	–43.8	–44.4	–45.4	–47.8	–48.6	–49.7	...

NOTES: (*) Value.
(**) Percentage of labour force.
(***) Cumulative balance for 12 months. Billion dollars as monthly average.
SOURCE: OECD, national statistical bodies and internal figures.

Industrial production stabilizes growth.

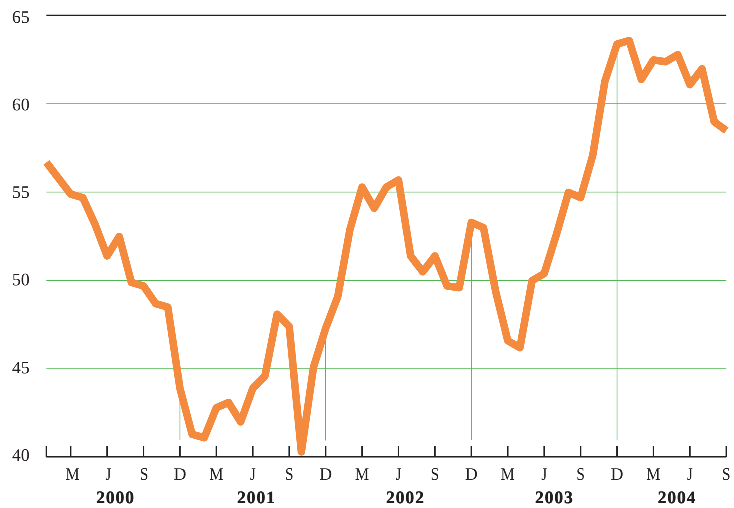
Industrial production grew by 4.6% year-to-year in September which meant a slight drop compared with growth of close to 5% in recent months. Nevertheless, levels for this index in June and July were revised upward while, in August, they were revised downward. As a result, the year-to-year growth in July, which originally had been 4.9%, stood at 5.3% while the figure for August went from 5.2% to 5.1%. Overall, rather than there being a slowdown it may be said that growth in recent months shows some stability.

Manufactures continue to show notable strength.

On the corporate side, the manufacturing activity indicator, prepared by the Institute of Supply Management (ISM) for September stood at 58.5, somewhat lower than the 59.0 in August, while still holding above the 50 level, which indicates a continuation of the expansionist stage. The production component in September moved up from 59.5 to 61.6 while new orders dropped from 61.2 to 58.1, a fact in keeping with the current situation of strong investment side by side with consumer doubt. The non-manufacturing index showed a lower level going down to 56.7. In any case, it should not be forgotten that these levels continue to be quite high compared with past periods, thus indicating a situation of some optimism which is in keeping with the current level shown by corporate profits in the gross domestic product (GDP) as a whole.

GRADUAL SLOWDOWN IN MANUFACTURING INDUSTRY IN UNITED STATES

Value of ISM business activity index



SOURCE: Institute of Supply Management.

Construction sector recovering strength but prospects of moderation continue.

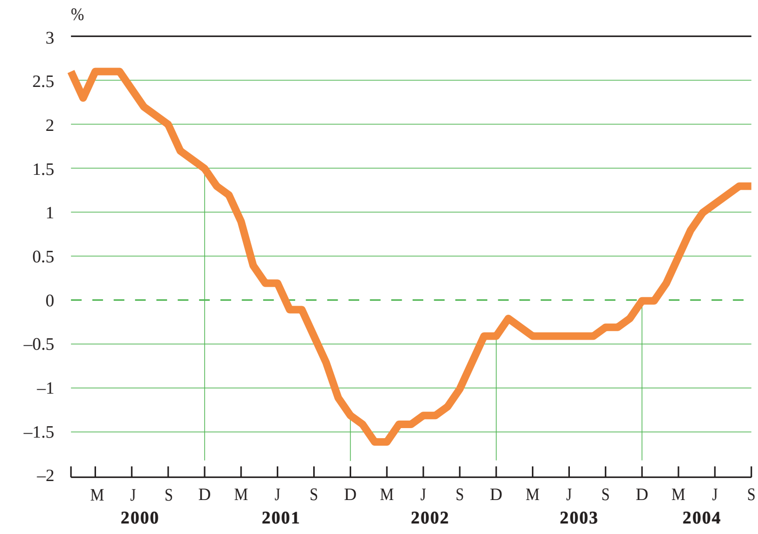
The construction sector, as in the case of demand indicators, recovered part of the strength seen in previous months. Construction permits continued to show moderation with a drop in August with resulting growth of 3.9% year-to-year, lower than the 5.0% in July and far from the 11.4% in April. Nevertheless, housing starts in August were up by a strong 12.3% compared with the same period last year going well above the increase in July moving up from 3.5% to 3.9%. Compared with the previous month, August brought a continuation of prospects of moderation which, in any case, seem to be somewhat late in coming.

Labour market continues gradual recovery...

The labour market is gradually confirming its recovery in spite of some ups and downs. September brought the creation of 96,000 jobs, somewhat less than expected, with growth of 1.3% year-to-year, a repetition of the figure for August.

EMPLOYMENT IN UNITED STATES GROWING SLOWLY

Year-to-year change in non-farm employment



SOURCE: Department of Commerce.

...while producer prices moderate.

In the area of prices, the increase in the consumer price index for September was 2.5% year-to-year, continuing its gradual drop. While the month-to-month increase rose from 0.1% to 0.2%, a comparison with previous months and the background trend suggest contained prices. Also in September there was a continuation of the positive trend to moderation in producer prices of finished products which grew by 3.3% year-to-year compared with 3.4% in August and 4.0% in June and July. As a result, there was a recovery of half the rise which took place between March and May this year when prices went up to growth of 4.7% year-to-year down from the previous 4.9%. This fact, linked to inflation, gives a note of general stability to U.S. prices.

Trade deficit grows sharply worse.

The foreign sector continued to provide the most negative note. The trade deficit continued to grow and, in the past twelve months as of August, it reached 596.6 billion dollars. Following the pattern of recent months, the stagnation in exports with regard to August went side by side with imports which reached a record figure of 150 billion dollars in September, presenting year-to-year growth of 20.7% as against 14.2% for exports. The most troublesome factor is the increasing deterioration of this figure which has taken place over the last three months. It is clear at this moment that this worsening of the figure is far from hitting bottom which means that this imbalance will in the future continue to be a sword of Damocles hanging over the U.S. economy.

Japan’s economy growing but fails to dispel doubts

Japanese demand fails to boost economic activity.

In the absence of early estimates for the GDP in the third quarter, demand indicators in Japan still fail to provide any clear prospect of growth. Retail sales in August were down 1.6% year-to-year following growth of 1.0% in July. It is possible that the typhoon had an effect on this indicator but the fact is that no strong growth is to be seen in retail consumption. Car sales continued to show a good level growing by 9.1% year-to-year in September.

JAPAN: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
GDP	–0.3	2.5	1.8	3.5	5.1	4.3	–	...	–
Retail sales	–3.9	–1.9	–2.2	–1.2	0.2	–1.9	1.0	–1.6	...
Industrial production	–1.3	3.3	1.1	4.7	5.0	8.3	7.1	8.4	...
Tankan company index (*)	–32.8	–21.0	–21.0	–11.0	–5.0	0.0	–	2.0	–
Housing construction	–1.8	0.6	–0.5	3.3	5.3	–3.6	7.7	10.4	...
Unemployment rate (**)	5.4	5.3	5.2	5.1	4.9	4.6	4.9	4.8	...
Consumer prices	–0.9	–0.3	–0.2	–0.3	–0.1	–0.3	–0.1	–0.2	...
Trade balance (***)	11.8	12.4	11.9	12.4	13.2	14.2	14.3	14.6	...

NOTES: (*) Value.
(**) Percentage of labour force.
(***) Cumulative balance for 12 months. Trillion yen.
SOURCE: OECD, national statistical bodies and internal figures.

Drop in company bankruptcies and corporate debt lower.

On the supply side, industrial production in August grew by 8.4% year-to-year. While this figure may give the impression of increasing strength in the industrial sector, there exist certain doubts about making a favourable verdict, given that the month of August 2003 was quite weak, which meant there was a substantial base effect. Company bankruptcies continued on a good trend recording a figure of 1,090 in September, a figure which meant an improvement over the same period last year when 1,212 companies went into bankruptcy.

Housing starts and machinery orders continue to show strong level.

While real estate demand showed slight signs of improvement, supply continued to show recovery with the result that housing starts in August were up by 10.4% year-to-year, thus improving on the figure of 7.7% in July. Machinery orders also continued upward with an increase of 14.1% year-to-year in August. As in the month before, both indicators are a strong sign of the strength of investment in Japan’s economy and would indicate a healthy third quarter so far as capital formation is concerned.

Employment positive in August while deflation continues.

In August, the labour market showed a more positive picture than in July. The unemployment rate partly corrected the July increase with a drop to 4.8% in August. Consumer prices continued a gradual decrease going down by 0.2% in August compared with the same period last year, worse than the 0.1% figure in July. If we exclude food, the decrease was 0.2%. We should keep in mind the heavy downward pressure from consumer durables which dropped by 4.3% year-to-year.

Trade balance positive but exports to China show small drop.

The trade balance continues to increase and, for the last twelve months ending in August, showed a surplus of 14,600 billion yen. This good performance, based on Japanese productivity, presented a slight reverse in August due to a modest decrease in exports to China. Net direct investment in the past twelve months ending in August was negative going to 2,200 billion yen.

Brazil: good results in growth and investment

Brazil grows by 5.4% in second quarter.

Growth of Brazil's economy continued to take on strength in the second quarter with the GDP growing by 5.4% year-to-year. This meant a decided advance in the upward cycle already indicated by 2.7% recorded in the first quarter. Private consumption continued on a clear growth trend rising by 4.5% over the same period last year. In contrast, public consumption continued along the moderate line followed in recent times with a figure of 1.2%, once more confirming the present government's commitment to stability.

BRAZIL: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
GDP	1.9	–0.2	–1.3	–0.1	2.7	5.4	–	...	–
Industrial production	2.7	0.0	–0.5	1.9	5.9	9.1	9.6	13.1	...
Unemployment rate São Paulo (*)	19.0	19.9	20.1	19.8	19.8	19.8	18.5	18.3	...
Consumer prices	10.2	17.0	17.8	13.0	7.6	5.4	6.3	6.6	6.0
Trade balance (**)	13.1	24.8	23.1	24.8	27.1	29.4	30.9	31.6	32.1

NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion dollars.
SOURCE: Brazilian Institute of Geography and Statistics and Central Bank of Brazil.

Investment up by 12%.

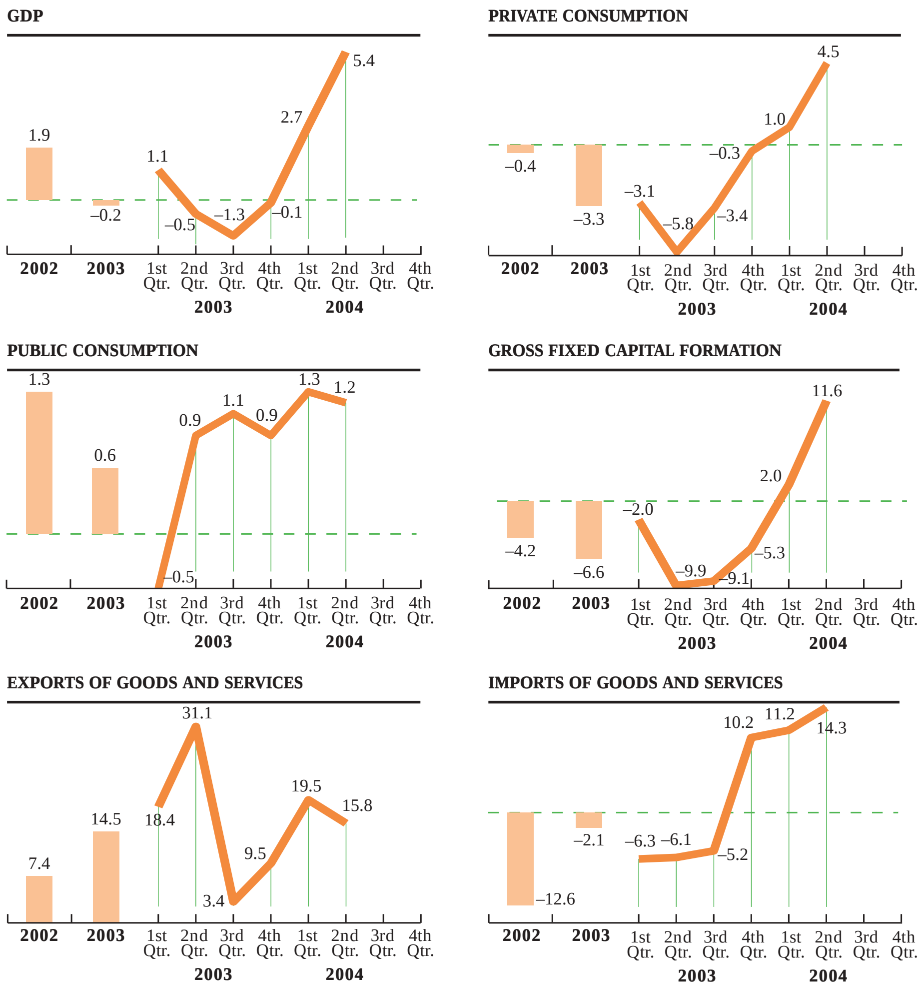
The most positive note in the second quarter was undoubtedly the healthy increase in gross fixed capital formation which rose by 11.6% year-to-year. This strength in investment is positive in two respects. On the one hand, it confirms the sustainability of growth and, on the other, provides relief for a region noted for its lack of investment. We must go back to 1997 to find such a positive quarter for investment but at that time public consumption was growing well above current levels.

Foreign sector continues to demonstrate Brazil's competitiveness.

The foreign sector also showed a positive performance in the second quarter following the good trend in previous months. Exports were up by 15.8% year-to-year. Imports, which reflected the strength of domestic demand, increased growth to 14.3%.

TREND IN BRAZIL'S GDP BY COMPONENT

Percentage year-to-year change rate



SOURCE: Brazilian Institute of Geography and Statistics and Central Bank of Brazil.

Industrial production up 13%...

Monthly supply indicators continue to confirm this growth. Industrial production in August rose by 13.1% year-to-year, this being the third consecutive month in which growth has continued at these levels. Industrial production of capital goods, a more volatile indicator, grew by 32.5% in the same period.

...giving support to retail sales and car sales.

Having found support in the strength of supply, demand continued to maintain growth. Retail sales in July were up by 12% year-to-year. Car sales grew by 25.8% in August, a logical decrease in terms of previous months when they had reached growth rates of 30%. This situation found support in industrial production of consumer goods which moved ahead in August to a growth rate of 11.7% year-to-year.

September inflation puts positive end to slight rise in summer while unemployment remains high although improving.

Consumer prices rose by 6.0% in September which reduced the slight rise in July and August. If we take into consideration the overall prices of raw materials and the trend in Brazil's CPI, the figure is positive. Taking into account income level and the painful measures taken in fiscal austerity, the risks for stability lie more in the high level of unemployment. In August, the unemployment rate in São Paulo went down to 18.3%. This level is still high but since April the number of unemployed has dropped by 2.4% in terms of the labour force.

Trade balance increases surplus.

The trade balance continued to offer reasons for confidence in the Brazilian economy going to 32.1 billion dollars in the past 12 months as of September. The coming together of such a positive foreign sector along with robust industrial production has not been frequently seen in this Latin American giant.

Raw materials: oil price goes above 50 dollars a barrel

Oil price up 70% in one year...

In the month of October, oil hit new all-time highs. On October 25 the one month forward per barrel price of Brent quality oil closed at 51.51 dollars, the highest level since this quality was first quoted in 1985. The average price in October stood at 49 dollars a barrel. This level is more than 70% higher than that recorded one year earlier. The factors pushing up crude oil prices are by no means new. In view of a situation of rising world demand, any perceived risk to supply pushes up prices to a notable extent.

RAW MATERIALS PRICES

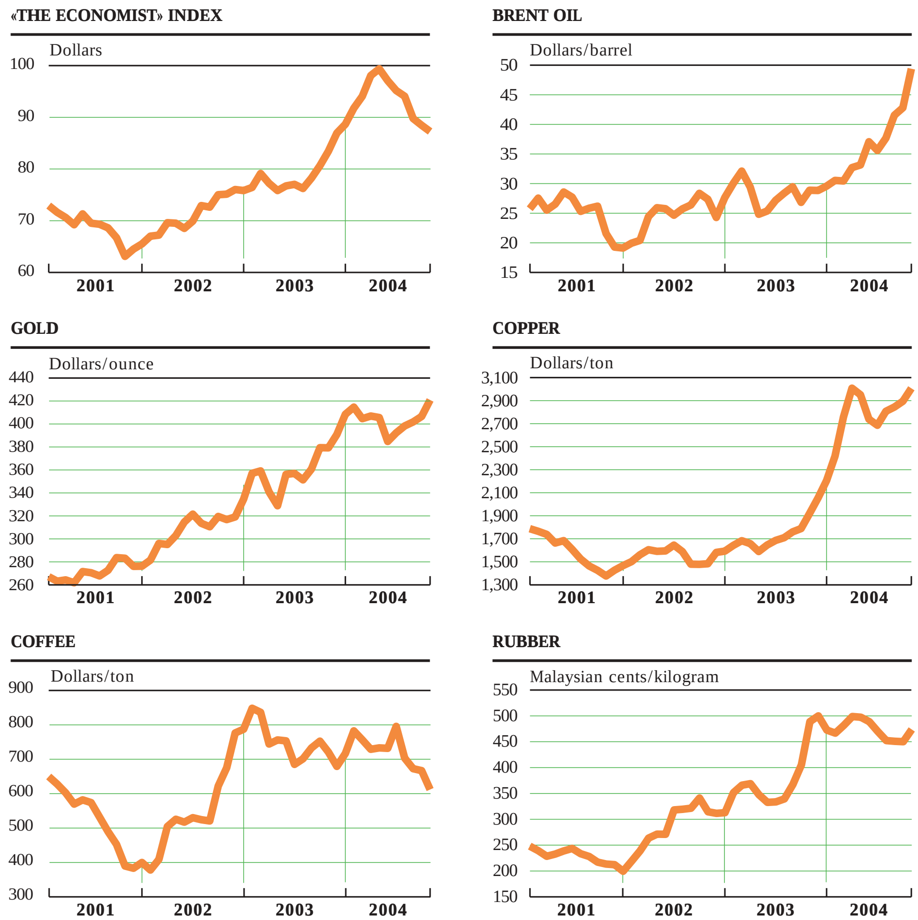
	2002	2003	2003		2004					
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September	October
«The Economist» index in dollars (*)										
General	4.4	11.3	6.5	14.2	21.9	27.0	23.4	14.7	9.7	4.6
Food	7.4	8.8	0.8	7.7	15.7	22.5	19.3	8.0	1.7	–4.3
Industrials	0.3	14.8	15.1	24.1	31.0	33.8	29.1	23.5	20.3	16.2
Non-food agricultural	*6.1*	*17.8*	*17.3*	*22.6*	*21.2*	*24.4*	*15.3*	*10.8*	*3.9*	*–6.6*
Metals	*–4.2*	*12.4*	*14.2*	*25.2*	*40.1*	*42.4*	*40.3*	*34.9*	*36.2*	*37.4*
«The Economist» index in euros (*)	**–0.8**	**–7.2**	**–6.9**	**–4.3**	**4.3**	**19.6**	**14.9**	**5.3**	**0.4**	**–1.5**
Oil (**)										
Dollars/barrel	25.1	28.4	28.2	29.1	31.2	35.3	37.7	41.6	42.8	49.4
Change rate	0.8	13.1	5.5	10.4	2.6	36.9	32.8	41.0	59.5	71.1
Gold										
Dollars/ounce	310.4	364.0	363.5	392.7	408.4	394.0	398.0	401.5	406.3	420.6
Change rate	14.5	17.3	15.6	21.4	16.0	13.7	13.3	11.4	7.1	11.0

NOTES: (*) Year-to-year change rate.
(**) Brent quality: one-month forward price.
SOURCE: «The Economist», Thomson Financial Datastream and internal figures.

...due to existing uncertainty on guaranteed future supply in an environment of growing demand.

In October, key negative factors were the conflicts in Iraq and Nigeria and uncertainty about the Russian oil company Yukos, to which must be added the effects of the hurricane Ivan in the Gulf of Mexico in September and the continuing activity of speculative money. In September, the International Energy Agency pointed out that the surplus oil extraction capacity of the Organization of Petroleum Exporting Countries continued to be quite limited and that the level of reserves was still less than normal, especially with regard to refined products.

TREND IN SELECTED RAW MATERIALS



SOURCE: «The Economist», Thomson Financial Datastream and internal figures.

Other raw materials moderate because of price decreases in food and non-food agricultural products.

The increase in crude oil prices is not being followed by other raw materials. In October, The Economist index for raw materials in dollars stood at levels of 4.6% higher than one year earlier. Expressed in euros, the impact was much more contained with a decrease of 1.5% year-to-year. Both figures were far from the notable growth occurring in the second quarter reaching 27% year-to-year in dollars and 20% year-to-year in euros, which represented an annual high. We should point out, however, that the trend in raw materials prices varies substantially according to type while the metals group showed a cumulative increase of 37% year-to-year in October, that same month food raw materials and non-food agricultural raw materials went to levels lower than those recorded one year earlier.

EUROPEAN UNION

European Commission foresees gradual slowdown in 2005

In 2005, EU to grow by 2.3% and euro area by 2.0%, figures lower than rate recorded in 2004.

In its autumn forecasts, the European Commission stated that, following a better than expected 2004, the year 2005 would show a gradual slowdown in economic activity. After reporting growth of 2.5% year-to-year this year, the 25 member states of the European Union (EU) as a whole will barely reach an increase of 2.3% in gross domestic product (GDP). A similar performance is expected in the euro area which will grow by 2.1% in 2004 and 2% in 2005. The European Commission believes that in 2006 the EU will reach growth of 2.4% with 2.2% in the euro area. Current forecasts for growth in the EU put out by the Commission show an upward revision of the figures for 2004 to the extent of four decimals with a decrease of two decimals for 2005 compared with forecasts published in the Spring.

MACROECONOMIC FORECASTS FOR EURO AREA (1)

	2002	2003	Current forecasts autumn 2004			Difference from Spring 2004 (2)	
			2004	2005	2006	2004	2005
Gross domestic product	**0.9**	**0.6**	**2.1**	**2.0**	**2.2**	**0.4**	**–0.3**
Consumption	0.7	1.1	1.5	1.7	2.0	–0.1	–0.6
Investment	–2.4	–0.5	2.2	3.2	3.6	–0.2	–0.4
Employment	0.6	0.2	0.5	0.9	0.9	0.2	0.0
Unemployment rate (3)	8.4	8.9	8.9	8.9	8.6	0.1	0.3
Inflation (4)	2.3	2.1	2.1	1.9	1.7	0.3	0.3
Government balance (% of GDP) (5)	–2.4	–2.7	–2.9	–2.5	–2.5	–0.2	0.1
Government debt (% of GDP)	69.4	70.7	71.1	71.1	70.9	0.2	0.2
Current account balance (% of GDP)	1.2	0.6	0.8	0.8	0.8	0.1	0.2
Growth of GDP in EU-25	*1.1*	*1.0*	*2.5*	*2.3*	*2.4*	*0.4*	*–0.2*

NOTES: (1) Annual change as percentage unless otherwise indicated.
(2) «+» («–») sign indicates a higher (lower) positive figure or a lower (higher) negative figure compared with Spring 2004.
(3) Percentage of labour force.
(4) Harmonized consumer price index.
(5) Includes revenue from UMTS licences in 2002.
SOURCE: European Commission.

Exports save growth in 2004...

The partial recovery in 2004 may be explained by the limited contribution from domestic demand. During the year the main drive in economic activity has come from the foreign sector which has compensated for the lower strength in consumption and investment. While various factors may have made it possible for European exporters to overcome the barrier to competitiveness represented by an appreciated euro, the European Commission places emphasis on the fact that the EU has benefited from the sharp increase in investment taking place in China, United States and Japan given that capital goods represent a significant part of European exports.

MACROECONOMIC FORECASTS OF EURO AREA COUNTRIES

Autumn 2004

	GDP (*)			Inflation (**)			Unemployment (***)		
	2004	2005	2006	2004	2005	2006	2004	2005	2006
Belgium	2.5	2.5	2.6	2.0	1.9	1.8	8.2	8.1	7.9
Germany	1.9	1.5	1.7	1.7	1.3	1.1	9.7	10.0	9.6
Greece	3.8	3.3	3.3	3.0	2.9	2.9	8.5	9.0	9.0
Spain	2.6	2.6	2.7	3.1	2.9	2.5	11.1	10.8	10.6
France	2.4	2.2	2.2	2.3	2.0	1.8	9.6	9.5	9.3
Ireland	5.2	4.8	5.0	2.3	2.4	2.4	4.4	4.4	4.3
Italy	1.3	1.8	1.8	2.3	2.3	2.0	8.3	8.1	8.0
Luxembourg	4.0	3.5	3.6	3.0	2.3	1.6	4.3	4.6	4.4
Netherlands	1.4	1.7	2.4	1.2	1.3	1.4	4.6	5.0	4.4
Austria	1.9	2.4	2.4	2.1	1.8	1.4	4.2	3.9	3.4
Portugal	1.3	2.2	2.4	2.4	2.4	2.3	6.3	6.2	6.1
Finland	3.0	3.1	2.7	0.2	1.5	1.7	8.8	8.6	8.3
Euro area	**2.1**	**2.0**	**2.2**	**2.1**	**1.9**	**1.7**	**8.9**	**8.9**	**8.6**

NOTES: (*) Percentage real change.
(**) Percentage change in harmonized consumer price index.
(***) Percentage of labour force.
SOURCE: European Commission.

…nevertheless sharp increase in oil in 2005 could bring about some slackening in economic activity.

On the other hand, in 2005, economic activity will likely be affected negatively by high oil prices. The European Commission forecasts that, after increasing by 40% in 2004, crude oil prices will add a further increase in 2005 amounting to 15%. Apart from the direct impact on economic activity, the European Commission is troubled by the uncertainty being brought about by the oil situation.

Upward revision of price forecasts because of impact of oil.

At the same time, pressures on oil prices have resulted in an upward deviation from previous forecasts for consumer prices. The European Commission now foresees maintenance of inflation above 2% annual in the period 2004-2005 for the EU-25 whereas its Spring forecasts put the growth rate for consumer prices at values of the order of 1.8%. In the case of the euro area, inflation will be 2.1% in 2004 and 1.9% in 2005, both figures being three decimals above what was expected last May. With regard to unemployment, the slowdown in growth will prevent any improvement in the unemployment rate in 2004-2005 (9.1% in the EU-25). On the other hand, the government deficit will go down by 0.4% of the GDP both in the euro area and the EU as a whole.

As a whole, countries sharing single currency to grow less than non-euro group.

There will continue to be notable differences in economic activity among members of the EU. The countries in the euro area as a whole will grow less than their partners outside the single currency area. What is noticeable is the poor growth to be recorded in 2005 in Germany, the Netherlands and Italy, all below 2%. On the other hand, the three Baltic countries (Estonia, Latvia and Lithuania) will show above 6%, while Poland, the biggest economy among those in the recent enlargement, will come close to 5%.

MACROECONOMIC FORECASTS FOR EUROPEAN UNION COUNTRIES OUTSIDE EURO AREA

Autumn 2004

	GDP (*)			Inflation (**)			Unemployment (***)		
	2004	2005	2006	2004	2005	2006	2004	2005	2006
Czech Republic	3.8	3.8	4.0	2.8	3.1	2.9	8.3	8.2	8.0
Denmark	2.3	2.4	2.0	1.1	1.9	1.6	5.8	5.3	4.9
Estonia	5.9	6.0	6.2	3.4	3.5	2.8	9.7	9.4	9.1
Cyprus	3.5	3.9	4.2	2.4	2.4	2.1	4.2	4.0	3.7
Latvia	7.5	6.7	6.7	6.8	4.7	3.5	9.9	9.7	9.4
Lithuania	7.1	6.4	5.9	1.2	2.9	2.8	11.4	10.6	9.9
Hungary	3.9	3.7	3.8	6.9	4.6	4.2	5.8	5.9	6.0
Malta	1.0	1.5	1.8	3.7	3.1	2.6	8.6	8.5	8.4
Poland	5.8	4.9	4.5	3.5	3.3	3.0	19.0	18.7	18.1
Slovenia	4.0	3.6	3.8	3.9	3.4	3.0	6.3	6.1	5.8
Slovakia	4.9	4.5	5.2	7.7	3.9	3.0	18.4	17.9	17.2
Sweden	3.7	3.1	2.9	1.1	1.5	1.9	6.3	5.8	5.0
United Kingdom	3.3	2.8	2.8	1.4	1.9	2.0	4.9	4.9	4.9
EU-25	**2.5**	**2.3**	**2.4**	**2.2**	**2.1**	**1.9**	**9.1**	**9.1**	**8.8**
EU-15	**2.3**	**2.2**	**2.3**	**2.0**	**1.9**	**1.8**	**8.1**	**8.1**	**7.9**
United States	4.4	3.0	2.9	2.6	2.8	2.3	5.5	5.5	5.4
Japan	4.2	2.1	2.3	–0.2	0.2	0.3	4.8	4.7	4.6

NOTES: (*) Percentage real change.
(**) Percentage change in harmonized consumer price index except for United States and Japan which show national consumer price index.
(***) Percentage of labour force.
SOURCE: European Commission.

Euro area: recovery starting up

Euro area benefits from higher rate of economic activity in third quarter.

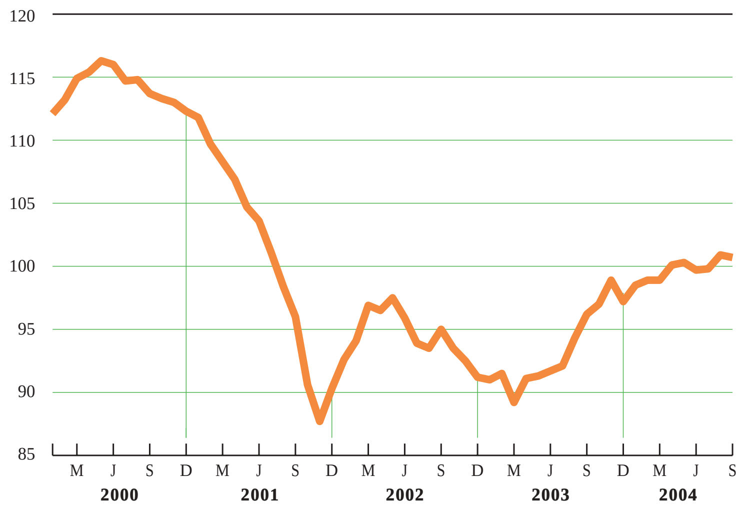
While economic recovery in the euro area is far from being consolidated, indicators for the third quarter are the best in a long time. Specifically, the trend in qualitative indicators confirms the more vigorous economic situation. The broadest of these indicators, the economic sentiment index, rose to a level of 100.5 points in the third quarter compared with a figure of 100 points in the second quarter. This increase arose from the higher figure in the indices for industrial and consumer confidence which came at the same time as a slight drop in sector confidence in services and construction.

Consumption showing incipient signs of improvement although still weak.

The increase in consumer confidence seems especially significant in the current situation, notable for a considerable slack in private consumption, which cannot be entirely explained by fundamental factors but rather is specifically linked to the lack of optimism reigning in European households. Other consumer indicators, still covering the summer months, may be reflecting this transition to a stage of increase in household consumption. For example, retail sales, which fell by 0.1% year-to-year in the second quarter, moved up to growth of 0.2% on average in July and August.

GRADUAL ECONOMIC IMPROVEMENT IN EURO AREA

Figure for economic sentiment index



SOURCE: European Commission.

EURO AREA: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003 3rd Qtr.	2003 4th Qtr.	2004 1st Qtr.	2004 2nd Qtr.	2004 July	2004 August	2004 September
GDP	0.8	0.5	0.4	0.7	1.4	2.0	–	...	–
Retail sales	0.0	0.3	–0.4	–0.3	0.6	–0.1	0.9	–0.4	...
Consumer confidence (*)	–11	–18	–17	–16	–14	–15	–14	–14	–13
Industrial production	–0.5	0.3	–0.3	1.4	1.0	2.9	2.2	1.5	...
Economic sentiment indicator (*)	94.4	93.5	94.2	97.7	98.8	100.0	99.8	100.9	100.7
Unemployment rate (**)	8.4	8.9	8.9	8.9	8.9	9.0	9.0	9.0	...
Consumer prices	2.2	2.1	2.0	2.0	1.7	2.3	2.3	2.3	2.1
Trade balance (***)	83.2	80.9	75.2	71.3	76.7	89.9	92.5	88.2	...

NOTES: (*) Value.
(**) Percentage of labour force.
(***) Cumulative balance for 12 months. Billion euros.
SOURCE: Eurostat, European Central Bank, European Commission and internal figures.

Investment continues to recover.

Another positive sign is maintenance of the expansionist cycle in investment. Industrial production of capital goods in August held at a rate of increase of 4.3% year-to-year compared with an increase of 3.6% year-to-year in July. The incipient recovery of domestic demand goes along with maintenance of a good situation in exports. The increase in exports in August meant that the cumulative trade balance for 12 months stood at 88.2 billion euros, approximately 18% higher than one year earlier.

Unexpected drop in industry in summer.

Among supply indicators, the economic situation was marked by an unexpected slowdown in industrial activity in July and August. In the latter month, industrial production grew by 1.5% year-to-year, an increase below the average for the second quarter (2.9% year-to-year). In any case, various early indicators for the sector (industrial orders, business climate) improved in the third quarter which should be an indication of some recovery in the secondary sector in coming months.

Inflation drops to 2.2% in September in spite of rise in oil.

On the other hand, inflation is surprisingly holding at relatively contained levels despite the trend in oil and, to a lesser extent, other raw materials. The harmonized consumer price index (HCPI) in September dropped by two decimals to 2.1% year-to-year thanks to the fact that pressure from the energy component (year-to-year growth of 6.4%, similar to that for August) was more than compensated by other categories (1.8% year-to-year, two decimals below the figure for August). The performance in the labour market was less positive. With economic recovery still at an initial stage, the unemployment rate was stuck at 9.0% of the labour force between April and August while employment grew by a modest 0.2% year-to-year in the second quarter of 2004.

Governments in Germany, France and Italy start process of privatizations amounting to 17 billion euros.

In another sphere, we should point out that the heavy impact of the economic slowdown on the public accounts is forcing a new round of privatizations in certain European countries. Since mid-September the three large euro area economies (Germany, France and Italy) have announced their intention to sell off part of the capital they still hold in various government-run corporations. The total amount foreseen in this process comes to 17 billion euros. Specifically, in its first privatization since 2000, the German government will try to place 7% of the capital of the Deutsche Telekom telecommunications operator for an amount of approximately 4.5 billion euros, while the French government will handle privatization of 9.6% of the capital of France Telecom, a transaction which will amount to 5 billion euros. In the case of Italy, the government has opted to launch a public offering of 20% of the capital of the Enel electrical power company which could amount to a figure of 7.6 billion euros.

Germany: first signs of improvement in domestic demand

Consumer drive in Germany may be recovering.

The economic situation in Germany is showing the first signs of a rise in domestic demand. While current consumer indicators are still weak (retail sales fell by 0.9% year-to-year in August), those indicators giving an indication of what is ahead point to improvement. Consumer confidence rose by two points to the level of –16 points. The trend in corporate investment is even better maintaining notable rates of increase, if we are to go by the trend in industrial production of capital goods. On average during the months of July and August, this indicator grew by 5.7% year-to-year, slightly less than the average in the second quarter when it was 6.3% year-to-year.

GERMANY: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003 3rd Qtr.	2003 4th Qtr.	2004 1st Qtr.	2004 2nd Qtr.	2004 July	2004 August	2004 September
GDP	0.1	–0.1	–0.3	0.0	0.8	1.5	–	...	–
Retail sales	–2.2	–0.4	–1.6	–0.8	–0.4	–1.9	–1.3	–0.9	...
Industrial production	–1.2	0.1	–1.3	1.4	1.1	3.1	2.3	3.5	...
Industrial activity index (IFO) (*)	89.4	91.7	92.5	96.2	96.4	95.7	95.6	95.3	95.2
Unemployment rate (**)	10.2	10.5	10.5	10.5	10.4	10.6	10.6	10.6	10.7
Consumer prices	1.4	1.1	1.1	1.2	1.1	1.8	1.8	2.0	1.9
Trade balance (***)	118.4	130.7	130.9	132.1	139.7	152.3	155.4	155.3	...

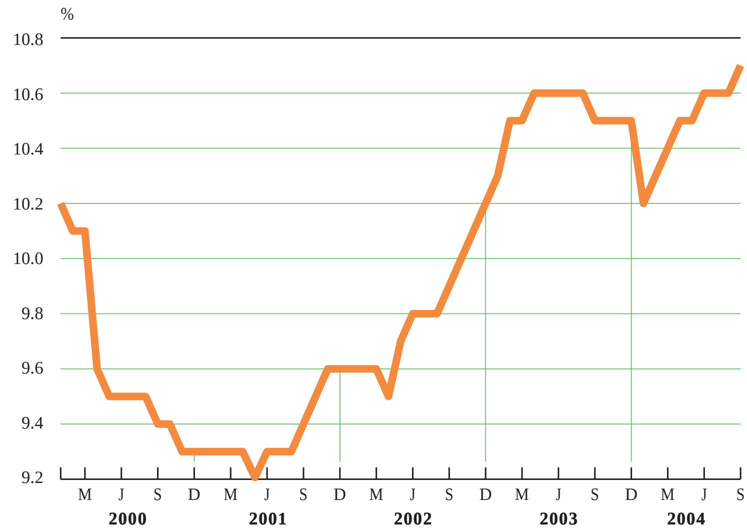
NOTES: (*) Value.
(**) Percentage of labour force.
(***) Cumulative balance for 12 months. Billion euros.
SOURCE: OECD, national statistical bodies and internal figures.

Industrial production grows nearly 4% in August.

On the supply side, we also see some improvement in economic activity. The most troubling factor on the scene, the weakness seen in industry in the middle months of the year, seems to be on the way to being corrected. Industrial production in August moved up to 3.5% year-to-year as against 2.3% in July. At the same time, the IFO indicator of industrial activity halted the drop seen in previous months to stabilize above 95 points in September and October. These figures are more in line with the increase in exports being recorded since the beginning of the year. The same trend continued in August when exports grew by 9% year-to-year while imports were up by 11% year-to-year. As a result, the cumulative trade surplus for 12 months stood at 155.3 billion euros, a figure practically the same as that for July.

UNEMPLOYMENT WORSENS IN GERMANY

Unemployment rate



SOURCE: Federal Statistics Office and internal figures.

While consumer prices drop by 1.9% in September unemployment goes up to 10.7%.

With regard to consumer prices in line with what has happened in other euro area economies, September brought a slight slowdown going from 2.0% year-to-year in August to 1.9%. In any case, the increases being seen in producer prices since the second quarter could shift to final prices as soon as domestic demand consolidates its improvement. In any case, somewhat more troubling is the trend in unemployment which reached 10.7% in September, the highest since February 1999.

France: economic activity up in third quarter

French economy continues to benefit from notable level in household consumption.

The French economy continues to enjoy a satisfactory level of economic activity without any signs of the expansionist phase wearing out as of this moment. The economic sentiment indicator stood at 108 points in September, the highest figure since May 2001. The basis for this good situation continues to be the strong rate of household spending. In August, three indicators involved (domestic consumption, industrial production of consumer goods and motor vehicle registrations) recorded an increase. In contrast to the situation in domestic demand, the French foreign sector continues to show a lower contribution. The cumulative trade balance for 12 months, which had been recording positive figures since October 2001, showed a deficit of 100 billion euros in August.

FRANCE: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
GDP	1.1	0.5	0.4	1.0	1.6	2.8	–	...	–
Domestic consumption	0.9	0.9	0.8	1.5	2.5	5.5	2.6	5.4	...
Industrial production	–1.4	–0.4	–0.8	0.9	0.5	2.4	2.3	0.7	...
Unemployment rate (*)	9.3	9.9	9.9	9.9	9.8	9.9	9.8	9.9	...
Consumer prices	1.9	2.1	2.0	2.2	1.9	2.4	2.3	2.4	2.1
Trade balance (**)	0.4	0.3	0.2	0.1	0.2	0.2	0.1	–0.1	...

NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion euros.
SOURCE: OECD, national statistical bodies and internal figures.

Little growth in industry while inflation down.

The difficulties in the foreign sector partly explain the modest performance in industrial production which grew by only 0.7% year-to-year in August. On the other hand, the confidence indicator for the tertiary sector, which recovered in the third quarter to the six points level, two points above the average for the second quarter, would indicate that activity in services is improving. Inflation, in turn, slowed to 2.1% year-to-year in September (2.4% in August), while the unemployment rate showed an increase of one decimal in August going to 9.9%.

Government budget for 2005 shows reduction in government deficit along with further tax cuts.

In this situation of strong recovery, the French government holds some margin for manoeuvre in terms of economic policy. The budget approved by the government for 2005 is based on economic growth of 2.5% for next year, close to a half-point higher than that expected for the euro area as a whole. As a result, maintenance of economic activity should make it possible to combine a reduction in the government deficit from 3.6% of the GDP in 2004 to 2.9% in 2005, along with application of a broad range of tax cuts. Notable among measures to reduce the tax load are the reduction of company tax, an increase in deductions for families and allowance for loans going into home purchase. Already in 2004 the government has begun to apply a reduction in taxes on farm diesel oil (4 cents of a euro) for fuel purchased between July and December.

Italy: weakness in consumption holds back exit from crisis

Italy not recovering due to poor state of domestic demand...

Italy continues to show a poor state of economic growth. In contrast to what has happened in the other large euro economies, the economic sentiment index dropped to the 99.3 points level in September, 2.2 points below the August figure. The major drop in private consumption which, if we are to go by the decrease in retail sales of 0.3% year-to-year in July, does not appear to be showing any relief, stands in the way of any clear recovery of economic activity. On the supply side, the weakness in the cycle is more clearly reflected in the drop in industrial production. After growing by 1.2% in the second quarter, that index went down by 0.6% year-to-year in July while showing a worse 1.5% year-to-year figure in August.

ITALY: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
GDP	0.4	0.4	0.4	0.1	0.8	1.2	–	...	–
Retail sales	2.4	2.0	1.8	0.9	1.2	–0.2	–0.3	...	...
Industrial production	–1.6	–0.6	–0.5	–0.2	–0.2	1.2	–0.6	–1.5	...
Unemployment rate (*)	8.6	8.4	8.3	8.2	8.2	8.1	–	...	–
Consumer prices	2.5	2.7	2.8	2.5	2.2	2.4	2.3	2.3	2.1
Trade balance (**)	10.8	3.4	1.5	2.0	1.4	2.8	3.0	2.8	...

NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion euros.
SOURCE: OECD, national statistical bodies and internal figures.

...which puts all economic drive on to foreign sector.

In this situation, practically all economic drive comes from the foreign sector. Thanks to the growth in exports, which reached 13% year-to-year for the average of July and August, the cumulative surplus for 12 months stood at 2.9 billion euros on average for those two months (2.8 billion euros in the second quarter). Finally, we should point out that the CPI eased in September going to 2.1% year-to-year compared with 2.3% in July and August.

United Kingdom: domestic demand strong in third quarter

U.K. consumption and investment continue good performance in third quarter.

As the third quarter advanced, indicators confirmed that domestic demand was continuing to act as the engine of current economic growth. Both current indicators and early figures show that private consumption is holding along the lines of the dynamic second quarter. Retail sales grew by 6.9% year-to-year in September in line with the average for the second quarter (6.8% year-to-year) while consumer confidence in the third quarter stayed at the –4 points level with no change over the previous quarter. The course of investment is equally positive, if we are to go by the trend in industrial production of capital goods which for the July-August average grew by 3.4% year-to-year as against 3.7% in the second quarter.

UNITED KINGDOM: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
GDP	1.8	2.2	2.2	2.9	3.4	3.6	–	...	–
Retail sales	6.8	2.9	2.9	3.1	6.3	6.8	6.5	6.7	6.9
Industrial production	–2.5	–0.1	–0.1	0.5	–0.1	1.3	–0.1	–0.1	...
Unemployment rate (*)	3.0	2.9	3.0	2.9	2.8	2.7	2.7	2.7	2.7
Consumer prices	2.2	2.8	2.8	2.6	2.3	2.2	2.2	2.2	1.9
Trade balance (**)	–43.5	–46.8	–47.1	–47.3	–50.0	–53.2	–55.3	–56.8	...

NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion pounds.
SOURCE: OECD, national statistical bodies and internal figures.

Growth side by side with absence of inflationary pressures.

On the supply side, industry continues to maintain a negative trend. After marking up year-to-year growth of 0.9% in June, industrial production fell by 0.1% year-to-year in July and held at this level in August. The recovery of industrial confidence recorded in the third quarter and a moderately stronger trend in exports could mean that the secondary sector will undergo some recovery in coming months. On the contrary, both construction and services increased their rate of economic activity in the summer months. A review of the British economic situation would conclude with recognition of the maintenance of stability in both inflation and unemployment. Consumer prices moved down from 2.2% year-to-year in August to 1.9% in September while the unemployment rate held at 2.7% between June and September.

MONETARY AND CAPITAL MARKETS

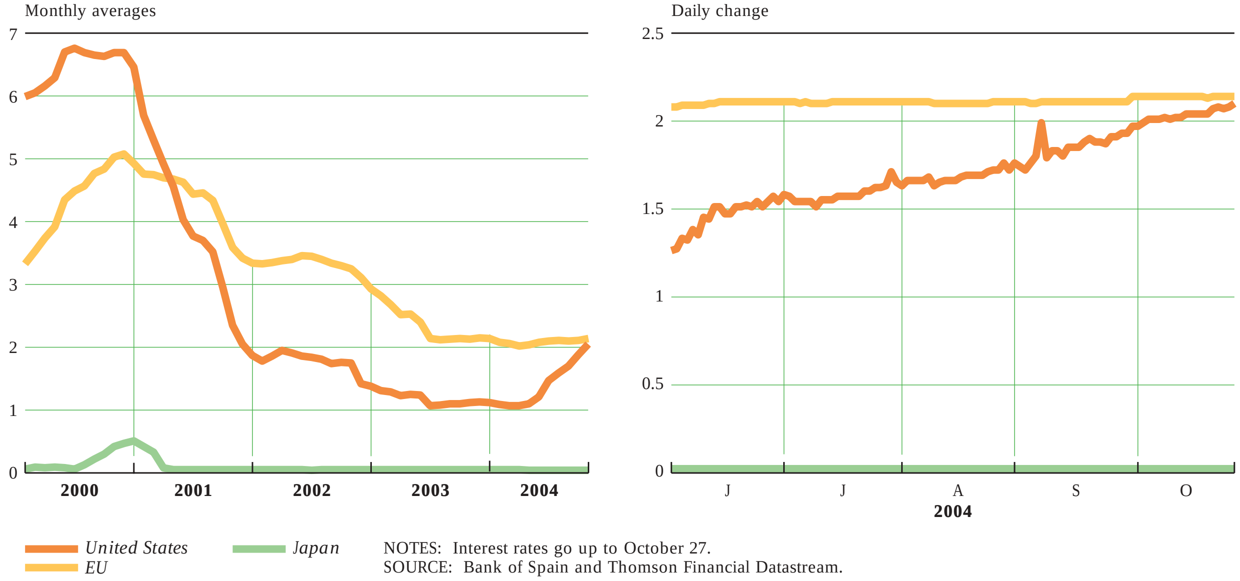
Rise in oil prices not changing monetary policies

Increase in oil prices makes no upward change in interest rate prospects.

The increase in oil prices to all-time highs in October did not increase upward prospects on official interest rates. The main central banks believe that inflationary pressure will be moderate as opposed to the oil shock in the Seventies. This analysis is based on a number of factors. Firstly, the price of oil in real terms is far from the level reached in 1980. Secondly, energy efficiency has notably improved since that time. Furthermore, markets for goods, services and production factors are developing with greater flexibility. Because of this, prospects continue to indicate that the all-time low levels in interest rates will gradually be abandoned.

U.S. SHORT-TERM INTEREST RATES LEVEL WITH EUROPEAN RATES

3-month interbank interest rates as annual percentage



NOTES: Interest rates go up to October 27.
SOURCE: Bank of Spain and Thomson Financial Datastream.

Further rise expected in Fed reference rate this year...

In the United States, economic indicators published in recent months have reinforced the policy of the Federal Reserve toward a gradual increase in the reference rate. Job creation in September was somewhat less than expected and the inflation rate showed a slight decrease. It should be remembered that the real short-term interest rate, that is to say, discounting inflation, remains negative. The market as a whole is betting on a further increase of 25 basis points before the year ends so that the objective level of Federal Funds would stand at 2% at the end of the year.

...according to the yield curve.

As a result, the interest rate on U.S. 1-year interbank deposits went up to 2.52% on October 7 although it slipped down following publication of the disappointing figure on job creation in September. At the middle of the last week of the month it stood at 2.42%, some 102 basis points above the level at the end of 2003.

SHORT-TERM INTEREST RATES IN NATIONAL MARKETS

Monthly averages as annual percentage

	Euro area			United States		Japan	United Kingdom		Switzerland
	ECB auctions (2)	Euribor 3-month	Euribor 1-year	Federal Reserve Board target level (3)	3-month	3-month	Bank of England intervention rate (4)	3-month	3-month
2003									
September	2.07	2.15	2.26	1.00	1.10	0.00	3.50	3.60	0.25
October	2.05	2.14	2.30	1.00	1.12	0.00	3.50	3.71	0.24
November	2.02	2.16	2.41	1.00	1.13	0.01	3.71	3.89	0.25
December	2.01	2.15	2.38	1.00	1.12	0.01	3.75	3.93	0.26
2004									
January	2.01	2.09	2.22	1.00	1.09	0.01	3.75	3.96	0.24
February	2.00	2.07	2.16	1.00	1.07	0.01	3.96	4.08	0.25
March	2.00	2.03	2.06	1.00	1.07	0.01	4.00	4.21	0.25
April	2.00	2.05	2.16	1.00	1.10	0.00	4.00	4.30	0.28
May	2.00	2.09	2.30	1.00	1.21	0.00	4.21	4.44	0.26
June	2.00	2.11	2.40	1.25	1.47	0.00	4.42	4.71	0.41
July	2.01	2.12	2.36	1.25	1.59	0.00	4.50	4.77	0.50
August	2.01	2.11	2.30	1.43	1.70	0.00	4.72	4.88	0.54
September (*)	2.02	2.12	2.38	1.59	1.88	0.00	4.75	4.85	0.67
October (1)	2.03	2.15	2.28	1.75	2.11	0.00	4.75	4.84	0.71

NOTES: (*) Provisional figures.
(1) October 27.
(2) Marginal interest rate. Latest dates showing change in minimum rate: 6-3-03 (2.50%), 5-6-03 (2.00%).
(3) Latest dates showing change: 25-6-03 (1.00%), 30-6-04 (1.25%), 10-8-04 (1.50%), 21-9-04 (1.75%).
(4) Latest dates showing change: 6-2-03 (3.75%), 10-7-03 (3.50%), 6-11-03 (3.75%), 5-2-04 (4.00%), 6-5-04 (4.25%), 10-6-04 (4.50%), 5-8-04 (4.75%).
SOURCE: European Central Bank, Bank of Spain, Thomson Financial Datastream and internal figures.

ECB maintains cautious position making no change in reference rates...

In the euro area, the Governing Council of the European Central Bank (ECB) made no change in its reference rates at its meeting on October 7. The ECB recognized that the increased price of oil had had an upward impact on prices this year but pointed out that the risk of further rises through wage increases was minimal. As a result, it felt that the stability of prices over the medium term was not in danger. Nevertheless, it stated that it was necessary to increase vigilance over all those factors which could involve risks for price stability over the medium term, such as a rise in oil prices, in indirect taxes or in controlled prices. Maintaining such vigilance was especially important when monetary liquidity continues to grow above the reference level of 4.5% and while loans to the private sector are increasing at the notable rate of 6% annual, largely driven by mortgage loans.

...and market not anticipating any immediate restrictive turn.

Nevertheless, the decrease in inflation in the euro area to 2.1% in September from the previous 2.3% and the appreciation of the euro provide some margin for maintaining reference rates. Added to this is the fact that growth in the euro area is also threatened by the increase in oil prices. As a result, monetary market operators are not expecting any restrictive move until the end of the first quarter next year.

1-year Euribor up slightly in September with drop in October.

In this framework, the 3-month Euribor has tended to move very slightly upward in recent weeks to stand at 2.14% in the middle of the last week of October. The 12-month Euribor rose slightly in September following two months of slight decreases, going to 2.38%. Nevertheless, in the early weeks of October, the 1-year Euribor dropped to some extent to stand at 2.28% at the middle of the final week in the month to show a decrease of 9 basis points compared with the same date last year.

No further increases expected in official interest rate by Bank of England.

The Bank of England, in turn, made no change in its reference rate in October for the second consecutive month. The slowdown in real estate prices, poorer economic indicators and a drop in the inflation rate meant this position was to be expected. In this situation the market is not discounting further increases in the British reference rate within the near future.

Bank of Canada raises key rates.

On the other hand, on October 19 the Bank of Canada announced an increase of 25 basis points in its reference rates. The objective level of the overnight interest rate went to 2.50% while the discount rate was put at 2.75%. This was the second increase in one month and was justified by the recovery of the economy.

Dollar weakens in October

G7 summit disappoints foreign exchange markets.

The dollar tended to weaken before the meeting of the seven most industrialized countries, which for the first time included the participation of China, held on the first weekend in October. Nevertheless, the markets were disappointed following this meeting which ended without taking any firm measures and the dollar subsequently recovered lost ground.

Series of poor economic indicators and increase in trade deficit push dollar down.

Later on, however, various factors pushed the U.S. currency down. Among these factors may be mentioned the slowdown in job creation in September, the decrease in inflation rate and especially, the increase in the trade deficit. Also having an impact in the same direction were lower prospects for an increase in official interest rates following statements by executives of the Federal Reserve Board. Uncertainty about the presidential elections may also have contributed to the volatility of the dollar. As a result, at the middle of the final week in October, the dollar showed a drop of 1.6% compared with the group of currencies of its main trading partners.

EXCHANGE RATES OF MAIN CURRENCIES
September 2004

	Final session of month		Monthly figures				Exchange rate October 27, 2004
	Exchange rate	% monthly change (2)	Average exchange rate	% change (2) Monthly	Over December 2003	Annual	
Against U.S. dollar							
Japanese yen	110.1	0.9	110.1	–0.2	2.2	–4.3	*106.6*
Pound sterling (1)	1.812	0.5	1.793	–1.4	2.2	11.2	*1.827*
Swiss franc	1.246	–1.6	1.262	0.0	0.0	–8.2	*1.208*
Canadian dollar	1.262	–3.8	1.288	–1.9	–1.8	–5.6	*1.226*
Mexican peso	11.39	0.1	11.49	0.8	2.1	5.1	*11.50*
Nominal effective index (4)	*113.9*	*–1.1*	*114.8*	*–0.4*	*0.3*	*–3.2*	*112.1*
Against euro							
U.S. dollar	1.241	2.5	1.222	0.3	–0.6	8.9	*1.279*
Japanese yen	137.2	3.1	134.5	0.0	1.5	4.3	*136.4*
Swiss franc	1.552	0.6	1.543	0.3	–0.8	–0.3	*1.532*
Pound sterling	0.687	1.7	0.681	1.8	–2.9	–2.2	*0.695*
Swedish krona	9.059	–0.7	9.092	–1.0	0.7	0.3	*9.024*
Danish krone (3)	7.442	0.0	7.438	0.0	–0.1	0.1	*7.435*
Polish zloty	4.380	–1.8	4.375	–1.3	–6.1	–2.0	*4.348*
Czech crown	31.66	–0.7	31.60	–0.1	–2.3	–2.3	*31.60*
Hungarian forint	247.4	–0.7	247.7	–0.5	–6.3	–3.1	*247.6*
Nominal effective index (5)	*104.1*	*1.6*	*103.0*	*0.3*	*–1.2*	*3.4*	*105.2*

NOTES: (1) Units to pound sterling.
(2) Percentages of change refer to rates as shown in table.
(3) Danish krone has central parity of 7.46038 against euro with fluctuation band of ±2.25%.
(4) Broad nominal effective index of U.S. Federal Reserve Board. Calculated as a weighted average of the foreign exchange value of the U.S. dollar against the 26 currencies of those countries with greatest volume of trade with the United States. Base: 1-1997 = 100.
(5) European Central Bank nominal effective exchange rate index for the euro. Calculated as a weighted average of the bilateral value of the euro against the currencies of the 23 main trading partners of the euro area. Base: I-1999 = 100.
SOURCE: Thomson Financial Datastream and internal figures.

Euro close to all-time high in January.

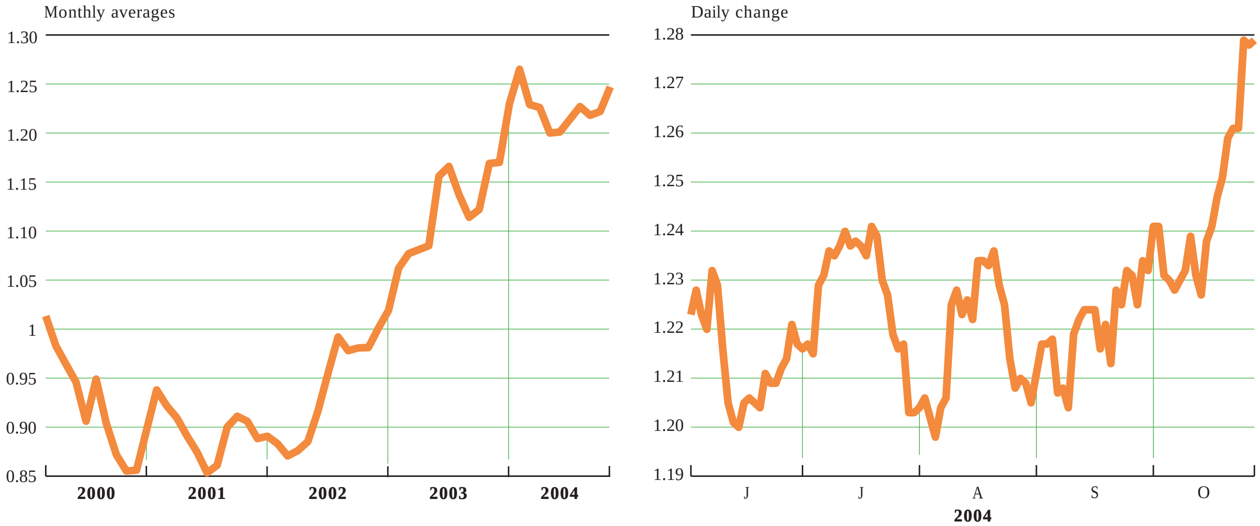
The euro recovered positions against a wide group of currencies following the drop in the first three and a half months of the year. Toward the end of October, the European single currency showed an appreciation of 4.2% over the low on April 13 although it stood 0.6% below the level at the beginning of the year. In this context, the euro took advantage of the weakness of the dollar and the euro exchange rate went well above the range in which it had stood in recent months. On October 27, it was running at 1.28 dollars, close to the all-time high recorded in mid-January. As a result, the European currency appreciated by 3.1% against the dollar compared with the end of September to stand 1.3% above the level at the beginning of 2004.

Pound sterling continues to depreciate although showing positive balance over December.

The pound sterling has continued weaken in recent weeks following the trend begun in August. The feeling that British interest rates had reached a ceiling and certain disappointing figures for the U.K. economy hurt the pound sterling. As a result, the British currency lost 1.1% against the euro in the first four and a half weeks of October. Nevertheless, since the beginning of the year the British currency has appreciated by 2.3% against the dollar and 1.5% against the euro.

EURO APPRECIATES AGAINST DOLLAR

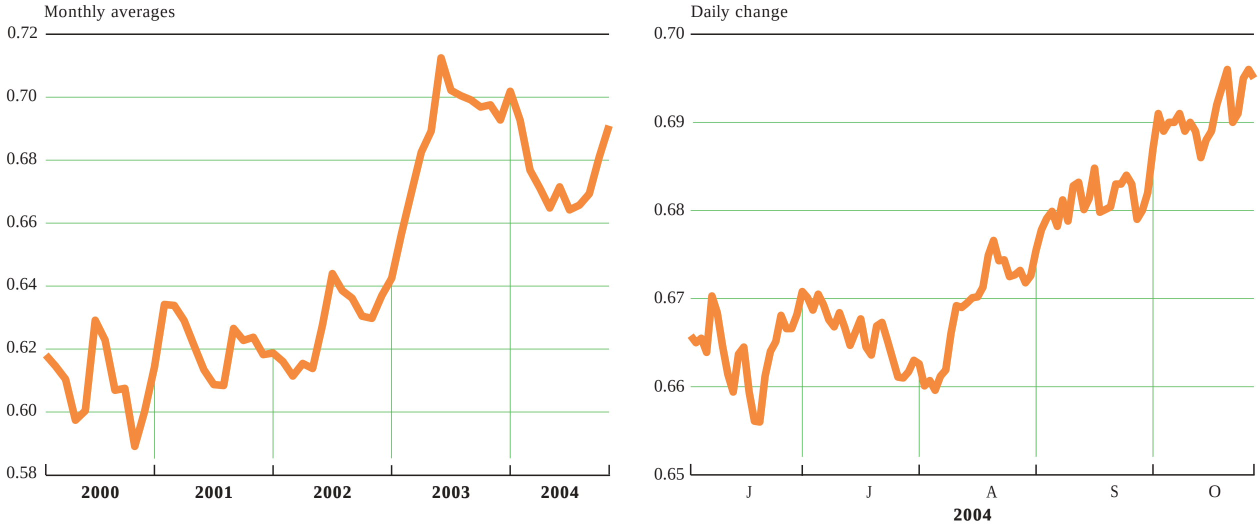
U.S. dollars to euro



NOTES: Figures go up to October 27. SOURCE: OECD, Thomson Financial Datastream and internal figures.

POUND STERLING MARKS UP LOWEST LEVEL AGAINST EURO IN LAST 9 MONTHS

Pounds sterling to euro



NOTES: Figures go up to October 27. SOURCE: Thomson Financial Datastream.

Norwegian crown, zloty, Swedish krona and Czech crown rise against euro in October.

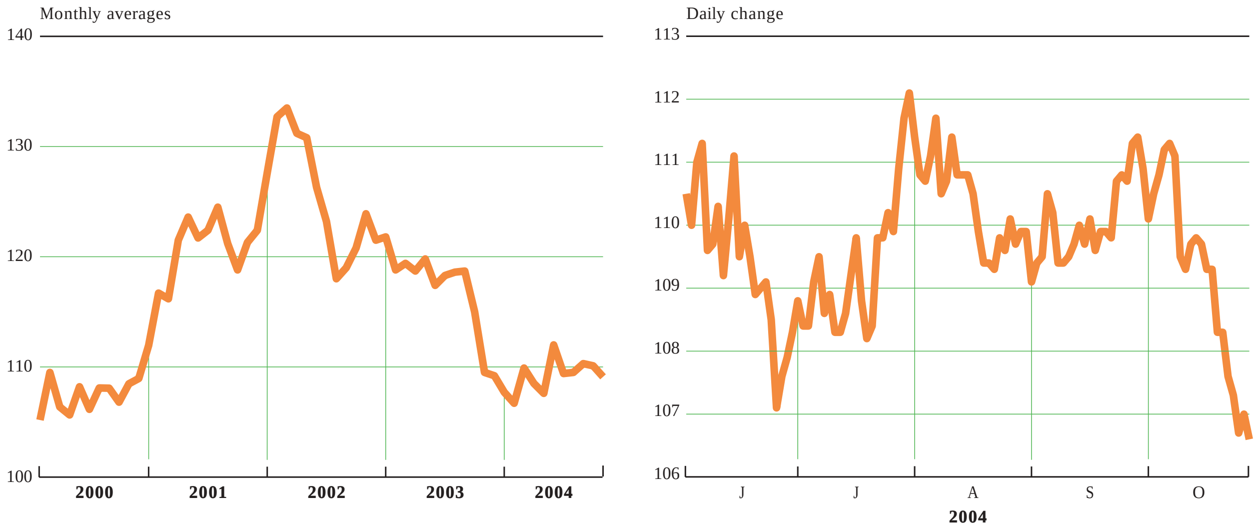
On the other hand, the Swedish krona appreciated slightly against the euro in the early weeks of October (0.4%) showing an appreciation of 0.6% so far this year. In the four and a half weeks of October the Norwegian crown rose by 2.2% compared with the euro to show a high for the last five months in the expectation that interest rates would move up. In the same period, the Polish zloty and the Czech crown also rose against the euro by 0.7% and 0.2% respectively.

Yen recovers level at start of year.

The exchange rate of the yen against the dollar has also reflected the latter's weakness in recent weeks. On October 27, the Japanese currency showed an increase of 3.3% against the dollar with an increase of 0.6% compared with the beginning of the year.

YEN RISES AGAINST DOLLAR

Yen to dollar



NOTES: Figures go up to October 27. SOURCE: OECD, Thomson Financial Datastream and internal figures.

Long-term interest rates hold close to 4%

Yield on government bonds drops following lower than expected job creation in United States.

In recent weeks, the yield on U.S. 10-year Treasury bonds continued the downward course begun in mid-June. Notable among factors behind this trend was the figure for new job creation in September, which was lower than expected. With regard to the increase in oil prices, investors have felt that it would have a greater effect on growth than on inflation. As a result, the yield on U.S. Treasury bonds has dropped by 78 basis points since mid-June to stand at 4.09% on October 27, although it was 40 basis points above the annual low in March. As a result, the interest rate curve has flattened out to some extent thus reflecting economic uncertainty.

Widening differential between U.S. and German bonds.

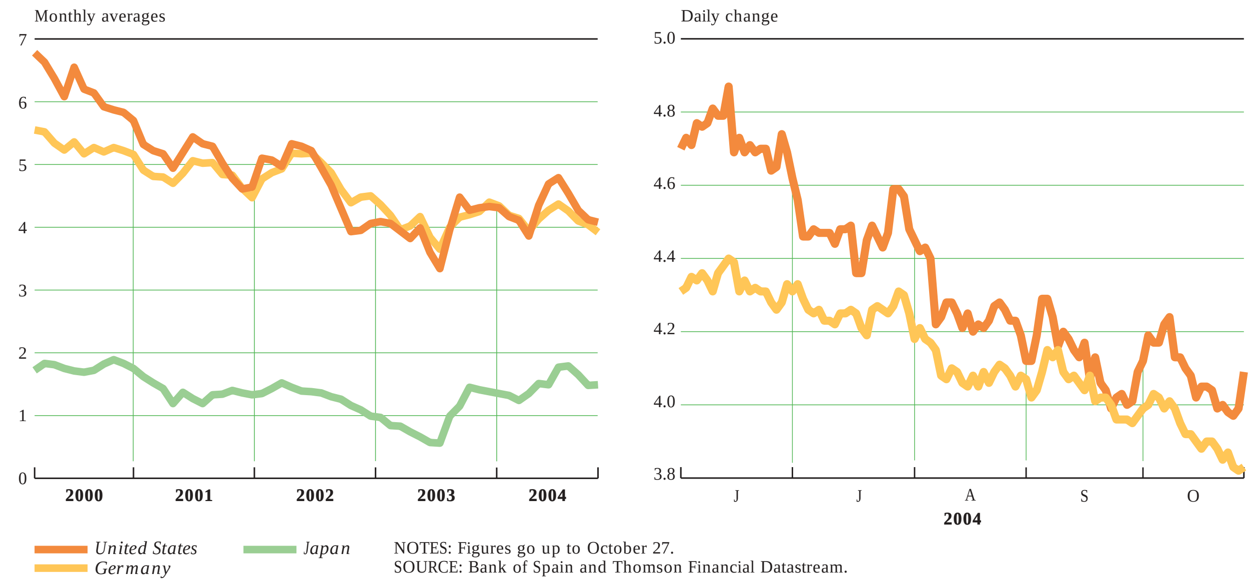
European government bonds have followed a course similar to those on the other side of the Atlantic. As a result, the yield on German government bonds dropped to 3.83% on October 27, a decrease of 56 basis points since mid-June. The differential in long-term interest rates between U.S. and German government bonds stood at 25 basis points in the last week of October, a slight increase compared with one month earlier.

Interest rate on Japanese bonds less than 1.5%.

The interest rate on Japanese government bonds stands at very low levels, below 1.5%. On October 27, it was 1.43%, a decrease of 44 basis points compared with the high recorded in June.

YIELD ON GERMAN GOVERNMENT BONDS MARKS UP LOW FOR LAST 15 MONTHS

Yield on 10-year government bonds as annual percentage



NOTES: Figures go up to October 27.
SOURCE: Bank of Spain and Thomson Financial Datastream.

LONG-TERM INTEREST RATES IN NATIONAL MARKETS

10-year government bonds: average for period as annual percentage

	2002	2003	2004					
			1st Qtr.	2nd Qtr.	July	August	September	October 27
United States	4.65	4.04	4.05	4.64	4.54	4.33	4.15	4.09
Japan	1.27	0.99	1.30	1.59	1.79	1.63	1.50	1.43
Germany	4.80	4.10	4.09	4.26	4.26	4.10	4.04	3.83
France	4.88	4.13	4.11	4.31	4.28	4.12	4.09	3.84
Italy	5.04	4.24	4.24	4.47	4.44	4.28	4.20	3.99
Spain	4.96	4.12	4.12	4.31	4.28	4.15	4.08	3.84
United Kingdom	4.93	4.53	4.83	5.14	5.15	5.04	4.96	4.71
Switzerland	3.02	2.47	2.46	2.74	2.83	2.66	2.61	2.43

SOURCE: Bank of Spain, Thomson Financial Datastream and internal figures.

Stock markets riding out storm

Increase in oil prices halts recovery of stock markets...

The stock markets began October in great form recording major increases with the help of long-term government bond interest rates at low levels. The later rise in oil prices, however, which went above 50 dollars a barrel, undermined the markets. On the other hand, publication of corporate profits showed varied results which also contributed to the volatility of the market indices. In any case, many stock markets recorded a positive result in the early weeks of October with some marking up annual highs.

...but overall result remains positive.

INTERNATIONAL STOCK EXCHANGES

Indices at month-end

NOTES: October 27, 2004. SOURCE: Thomson Financial Datastream.

Standard & Poor's 500 in United States manages to recover par for year.

In the United States, the rise at the beginning of October was counteracted by a later drop. Nevertheless, at the beginning of the last week in the month, the Standard & Poor's 500 showed a rise of 1.0% and 1.2% compared with the end of 2003. The Dow Jones Industrials index reported a worse performance with a decrease of 0.8% over the end of September continuing a downward move which brought it cumulative losses of 4.3% over December. On the other hand, the Nasdaq index which is representative of hi-tech shares, rose by 3.9% in the four and a half weeks of October, although it has lost 1.7% so far this year.

Sectors showing best for year are energy, utilities and communications.

By sectors making up the Standard & Poor's 500 index, those showing the most favourable trend so far this year were energy, with an increase of 24.4% thanks to the rise in oil prices, utility companies, with an increase of 12.5%, and telecommunications, with a rise of 8.5%. On the other hand, those sectors showing a worse performance included health services, with a drop of 6.5%, and information technology, with capital losses of 5.7%.

INDICES OF MAIN WORLD STOCK EXCHANGES
September 30, 2004

	Index (*)	% monthly change	% cumulative change	% annual change	Figures on October 27, 2004 % cumulative change	Figures on October 27, 2004 *% change over same date in 2001*
New York						
Dow Jones	*10,080.3*	*–0.9*	*–3.6*	*8.7*	*–4.3*	*4.8*
Standard & Poor's	*1,114.6*	*0.9*	*0.2*	*11.9*	*1.2*	*1.9*
Nasdaq	*1,896.8*	*3.2*	*–5.3*	*6.2*	*–1.7*	*11.4*
Tokyo	10,823.6	–2.3	1.4	5.9	0.1	*–1.0*
London	4,570.8	2.5	2.1	11.7	3.4	*–10.8*
Euro area	2,726.3	2.1	–1.2	13.8	1.0	*–22.8*
Frankfurt	*3,892.9*	*2.8*	*–1.8*	*19.5*	*–0.9*	*–18.5*
Paris	*3,640.6*	*1.3*	*2.3*	*16.1*	*3.4*	*–17.9*
Amsterdam	*323.9*	*0.3*	*–4.1*	*5.6*	*–2.9*	*–30.7*
Milan	*1,326.1*	*3.7*	*5.5*	*13.7*	*7.3*	*–3.1*
Madrid	*8,029.2*	*2.0*	*3.8*	*19.8*	*7.8*	*4.8*
Zurich	5,465.3	0.8	–0.4	8.4	–2.1	*–14.1*
Hong Kong	13,120.0	2.1	4.3	16.8	2.1	*23.4*
Buenos Aires	1,142.5	20.0	6.6	38.0	20.0	*435.0*
São Paulo	23,245.0	1.9	4.5	45.2	4.2	*96.7*

NOTES: (*) New York: Dow Jones Industrials, Standard & Poor's Composite, Nasdaq Composite; Tokyo: Nikkei 225; Euro area: DJ Euro Stoxx 50; London: Financial Times 100; Frankfurt: DAX; Paris: CAC 40; Amsterdam: AEX; Milan: Banca Commerciale Italiana; Madrid: IBEX 35 for Spanish stock exchanges; Zurich: Swiss Market Index; Hong Kong: Hang Seng; Buenos Aires: Merval; São Paulo: Bovespa.
SOURCE: Thomson Financial Datastream and internal figures.

Annual high on Italian stock market in October…

Stock markets in the euro area showed a slightly more favourable balance than those on the other side of the Atlantic so far this year. At the middle of the last week of October, the DJ Eurostoxx 50 index, which is representative of the largest companies in the euro area, stood 2.2% above the end of September with cumulative gains of 1.0%. It is worth noting that the indices for the Milan and the Madrid stock markets showed cumulative capital gains of more than 7%. The index for the Italian stock market showed an annual high in the second week of October.

…along with London.

Outside the euro area, the Financial Times 100 index for the London stock exchange also recorded an annual high in the second week of October to reach a cumulative increase of 3.4%. On the other hand, on October 27 the SMI index for the Swiss stock market stood 2.1% below the end of last year. As a result of further drops in the Nikkei 225 index in Japan in the early weeks of October, the balance compared with December was only an increase of 0.1% whereas at the end of April it was showing a rise of 13.9%, this being due to investor doubts about the progress of Japan's economy.

IBEX 35 up 8% over December.

With regard to the Spanish stock market, the IBEX 35 index managed to overcome the resistance seen in recent months and went above the 8,300 points level. On October 27 it stood at 8,338.4 points, an increase of 3.9% over September and 7.8% compared with the end of 2003.

Substantial rise in Argentine stock market this year.

With regard to stock markets in emerging countries, mention should be made of the good trend in Latin American markets thanks to the rise in raw materials prices and the moderate increase in interest rates expected from the U.S. Federal Reserve Board. The IPC index for the Mexican stock exchange marked up an all-time high level in the final week of October, recording a cumulative increase of 31.0%. The Merval index for the Argentine stock market went up 12.6% in the four and a half weeks of October to show a cumulative increase of 20.0%. The Bovespa index for the Brazilian stock market dropped by 0.3% in the four and a half weeks of October but showed a rise of 4.2% over December.

ECONOMIC ACTIVITY

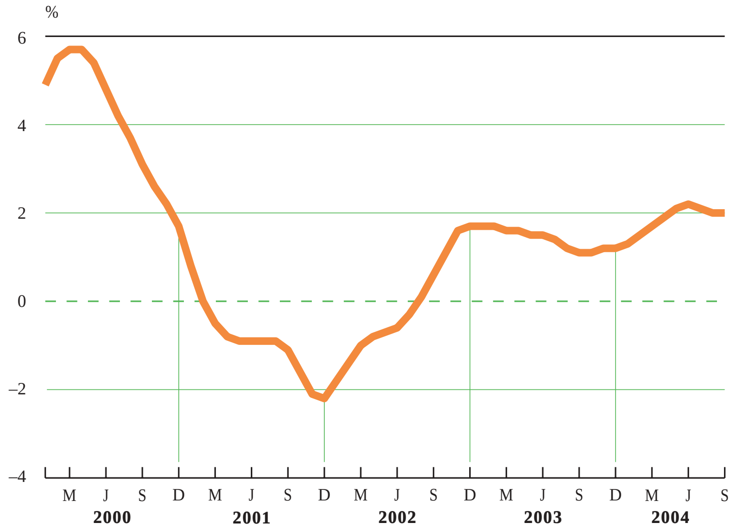
Domestic demand driving growth

Domestic demand continues as main engine of economic growth.

In the third quarter of 2004 the growth rate of economic activity was fairly similar, or perhaps slightly lower, than that seen in the first half-year, if we are to go by the trend in the main economic activity indicators. The strength of domestic demand continues to be the main engine of growth in the gross domestic product (GDP) partly contained by the negative contribution from the foreign sector. In more overall terms, electrical power consumption, which is highly representative of the level of general economic activity, in recent times has recovered a very lively growth rate (4.2% year-to-year in the third quarter after adjustment for number of working days and temperature).

RECOVERY IN INDUSTRY LOSING STEAM

Year-to-year change in industrial production index



NOTES: Cycle-trend series adjusted for number of working days.
SOURCE: National Institute of Statistics and internal figures.

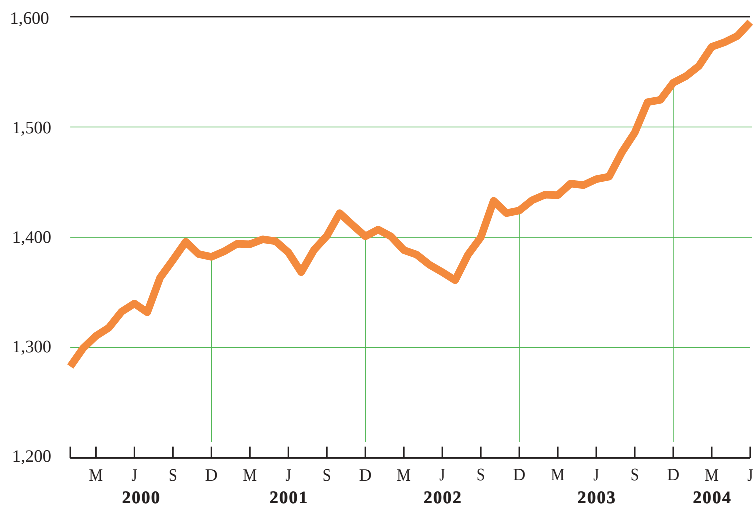
Recovery in industrial sector weakening with very uneven performance in various branches.

On the other hand, recovery in industry has lost strength in recent months, as indicated by the trend in the general production index which, adjusted for number of working days, tended to stabilize growth at around 2% year-to-year in the summer months after the drive shown in the first half of the year. In the first eight months of the year branches such as metallurgy, machinery, electrical equipment, medical equipment and publishing were the most expansionist with growth running between 5% and 10% compared with the same period last year. Sectors such as food and beverages, papermaking, metal products, rubber industries and motor vehicles came next with growth rates between 2.5% and 4%. At the opposite extreme, there were notable drops in the tobacco industry and data processing equipment (20% and 26% respectively) with more moderate, although equally significant drops, in the textile sector (5.1%), clothing and furs (1.9%), leather (12.0%), electronic equipment (1.6%) and chemicals (0.9%).

Construction, on other hand, continues to show great strength.

On the other hand, construction continues to report a very strong performance. While some early indicators show a downward turn from the previous high growth rates, the rate of activity continues to be notable if we are to go by the main current indicators. In this respect, cement consumption grew by 3.1% in the third quarter, slightly above the three preceding months. In addition, the number of housing units under construction stood at 1,595,000 in June, the highest level ever recorded with a significantly high growth profile. On the other hand, the situation in government tendering has been quite uneven in recent months. In overall terms the total amount tended as of July was 1.8% lower than the high figure for one year earlier.

NUMBER OF HOUSING STARTS CONTINUES TO RISE
Thousand housing units under construction



SOURCE: National Institute of Statistics.

In services, what stands out is modest balance in tourism…

In services, the most notable feature is the modest balance in tourism. While the total number of foreign tourists rose by 1.9% in the first nine months of the year, the trend in inflows for tourism in the balance of payments is turning out to be fairly negative with a nominal decrease of 0.5% as of July (more than 3% in real terms). The good performance in national tourism (overnight stays in hotels by Spanish residents were up 8.7% as of August) to some extent cushioned the impact of weaker flows from foreign tourism. Overnight stays by non-residents were down by 3.2% in the same period.

...with situation in other sector activities generally more positive.

In other activities in the services sector, the situation is generally positive although the index for business volume in the sector reflects a drop in growth spread over all branches except in information technology and communications. Along with tourism, the most modest trend showed up in activities related to company services. Retail trade and transportation are also tending to show lower growth while still maintaining high growth rates. This is so, for example, in air passenger traffic which rose by 7.7% as of September in spite of having lost some drive since April. In other passenger lines the results are generally modest (moderately positive by road and negative by railway), while goods traffic is generally expansionist.

SUPPLY INDICATORS

Percentage change over same period year before

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
Industry									
Electricity consumption (1)	3.8	4.8	6.1	4.7	3.7	2.8	4.9	2.2	5.5
Industrial production index (2)	0.2	1.4	1.1	1.2	1.4	2.5	1.6	1.7	...
Confidence indicator for industry (3)	–5.7	–0.9	–1.3	–2.3	–3.0	–2.0	–3.0	–3.0	–2.0
Utilization of production capacity (4)	78.5	79.1	79.7	80.6	78.7	79.3	–	80.5	–
Imports of non-energy intermediate goods (5)	6.4	3.3	–0.1	–3.7	0.6	6.4	12.5	...	...
Construction									
Cement consumption	4.7	4.8	4.5	5.7	5.6	2.8	–2.6	9.5	4.3
Confidence indicator for construction (3)	–2.3	–1.5	–2.3	1.0	–1.0	–2.7	–6.0	–9.0	–10.0
Housing (new construction approvals)	4.3	21.4	14.1	26.0	8.0	9.2	10.7	...	...
Government tendering	13.1	–10.9	–31.5	–50.2	8.6	–33.5	54.6	...	...
Services									
Retail sales	5.7	5.7	5.0	6.1	6.7	5.5	6.3	2.6	...
Foreign tourists	4.5	–0.3	–3.1	1.3	5.4	0.3	0.6	–0.8	5.7
Tourist revenue inflows	–2.9	3.7	3.9	2.3	4.0	–2.2	–3.7	...	...
Goods carried by rail (km-tonnes)	–0.7	1.7	5.8	3.0	6.4	6.2	–9.2	–4.9	...
Air passenger traffic	–1.1	7.5	7.8	8.5	11.0	6.7	7.9	5.1	6.7
Motor vehicle diesel fuel consumption	6.2	8.0	7.2	6.0	7.8	6.8	6.5	...	...

NOTES: (1) Corrected for number of working days and temperature.
(2) Corrected for difference in number of working days.
(3) European Commission survey: difference between percentage of positive and negative replies.
(4) Business survey: percentage of utilization inferred from replies.
(5) By volume.
SOURCE: Red Eléctrica Española, OFICEMEN, SEOPAN, Civil Aviation, National Institute of Statistics, Bank of Spain.

Consumption maintaining notable strength...

On the demand side, consumption is maintaining considerable strength but recently has tended to lose some steam particularly under the heading of non-food products. The trend in passenger car registrations clearly illustrates the situation created. Growth in the third quarter of 2004 was quite high (5.3% year-to-year with the highest sales volume in recent history in that period) but this was substantially lower than the figure recorded in the first half of the year (14.5%). In a similar way, imports of consumer goods in July were up by 8.7% real, compared with the same month the year before, although below the 18.4% recorded in the first half-year.

...but rise in oil prices contributing to dampen consumer spirits.

Along the same lines, the retail sales index recorded a very modest increase in the months of July and August (1.2% real compared with the same period in 2003), brought about partly by the lower level of tourism. Naturally, the current rise in fuel prices results in a loss of household purchasing power and brings about an erosion of consumer confidence which, in September, dropped to the –13 points level, the lowest in the last 12 months.

DEMAND INDICATORS

Percentage change over same period year before

	2002	2003	2003		2004				
			3rd Qtr.	4th Qtr.	1st Qtr.	2nd Qtr.	July	August	September
Consumption									
Production of consumer goods (*)	2.4	0.2	0.3	–1.7	–0.1	–0.7	–1.3	0.4	...
Imports of consumer goods (**)	5.0	10.0	12.6	8.9	20.4	16.6	8.7	...	...
Car registrations	–6.6	3.8	7.4	10.3	20.8	9.6	3.8	7.3	6.2
Credit for consumer durables	12.6	1.6	4.0	1.1	3.7	4.8	–	–	–
Consumer confidence index (***)	–11.6	–13.7	–12.3	–11.7	–11.7	–9.3	–11.0	–11.0	–13.0
Investment									
Capital goods production (*)	–4.9	0.5	–2.2	3.2	1.3	3.7	3.9	2.3	...
Imports of capital goods (**)	–5.8	16.8	26.2	9.9	18.7	14.3	48.2	...	...
Commercial vehicle registrations	–6.0	13.5	16.3	11.9	14.9	13.1	3.9	12.0	14.9
Foreign trade (**)									
Non-energy imports	3.7	7.4	7.6	2.1	8.9	10.6	17.3	...	...
Exports	1.4	6.2	4.6	3.3	7.3	2.2	15.4	...	...

NOTES: (*) Corrected for difference in number of working days.
(**) By volume.
(***) European Commission survey: difference between percentage of positive and negative replies.
SOURCE: ANFAC, National Institute of Statistics, Bank of Spain, Ministry of Economy, European Commission and internal figures.

Capital goods investment continues expansionist note.

On the other hand, indicators for capital goods investment are still showing notably expansionist growth profiles. Imports of goods of this type, for example, grew by 16.3% year-to-year in the first half-year and more than 48% in July. In the third quarter, commercial vehicle registrations rose by 9.4% although, in this case, they exhibited a profile of decreasing growth.

Non-financial companies show record profits in first half of 2004

Ordinary profits of companies continue to rise...

In the first half of 2004, non-financial companies continued to grow at a sustained rate, thanks to the strength of the services sector and the recovery in industrial activity. Along with this, the moderate increase in labour costs and the continuing decrease in financial costs made record profits possible, according to figures supplied by Composite Company Statistics prepared by the Bank of Spain.

PROFIT AND LOSS ACCOUNT OF NON-FINANCIAL COMPANIES

Annual change rates

	Annual Composite Company Statistics		Quarterly Composite Company Statistics		
				1st quarter	
	2001	2002	2003	2003	2004
Value of production	4.0	2.7	3.9	4.5	4.9
Intermediate consumption	3.2	1.6	2.8	3.5	4.7
Gross value added (GVA)	**5.9**	**5.1**	**5.7**	**6.1**	**5.1**
Labour costs	5.8	5.3	3.8	4.6	2.4
Gross operating profit	**5.9**	**4.8**	**7.3**	**7.4**	**7.2**
Financial income	40.9	–7.8	21.4	5.6	21.7
Financial costs	19.1	–3.8	–0.9	0.7	–5.4
Depreciation and operating provisions	4.3	3.4	0.0	3.8	–2.8
Net ordinary profits	**13.6**	**3.8**	**20.8**	**12.1**	**22.5**
Capital gains and extraordinary income	–11.8	59.5	–11.5	–3.1	–63.1
Capital losses and extraordinary costs	10.5	35.6	–26.8	–8.6	–45.3
Provisions and tax	30.4	109.8	–53.8	–75.5	15.1
Net profit (*)	**–17.6**	**–75.9**	**–**	**–**	**–9.3**

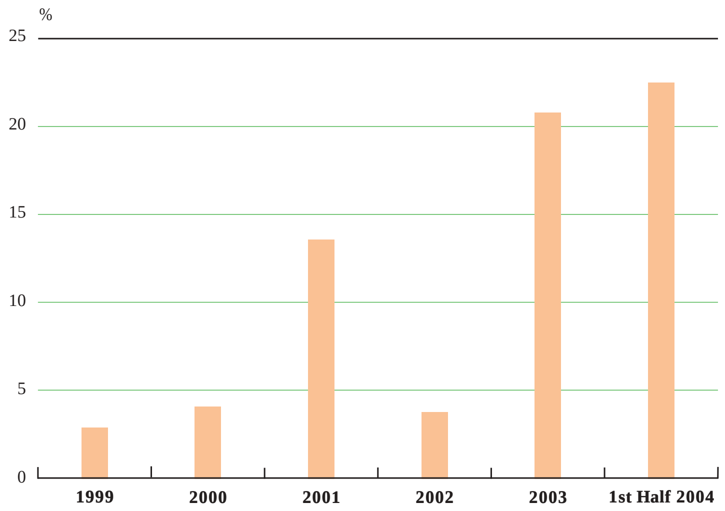
SOURCE: Bank of Spain.

...due to boost in economic activity...

In overall terms, gross value added (GVA) of those companies included in the sample grew by 5.1%, somewhat lower than the increase recorded in the same period in 2003, due to the bias brought about by refining companies, the performance of which was affected by the sharp upward swings in oil prices and margins in that sector. If the figures for those companies are removed, growth in 2004 shows slightly above that for 2003. Those companies involved in the retail trade were the ones recording the highest growth (10.4% excluding companies involved in fuel marketing), which was very similar to the figure for one year earlier. The growth of the GVA generated by transportation and communication companies (5.4%) and the industrial sector (3.9%) was more than one point above the figure in 2003.

CORPORATE PROFITS CONTINUE TO GROW

Annual change in net ordinary profit



NOTES: 1999-2002: Annual Composite Company Statistics. 2003-2004: Quarterly Composite Company Statistics.
SOURCE: Bank of Spain.

...moderation in labour costs, drop in financial costs and decrease in write-offs and provision.

Labour costs rose by 2.4% in the first half of 2004 (2.2 points less than in the first six months of 2003) due to the slight drop in employment (0.5%) in the companies included in the sample and moderation in average wages which grew by 2.9%, which was below the rate in 2003. At the same time, financial costs decreased by 5.4% thanks entirely to the decrease in interest rates which compensated for the positive changes of lesser amount due to the increase in borrowing and for commissions and discounts. As well as this, the decrease in write-offs and operating provision meant that the net ordinary profit (the most representative of typical company activity) grew by 22.5%, the highest rate for the first six months of the year in recent years.

LABOUR MARKET

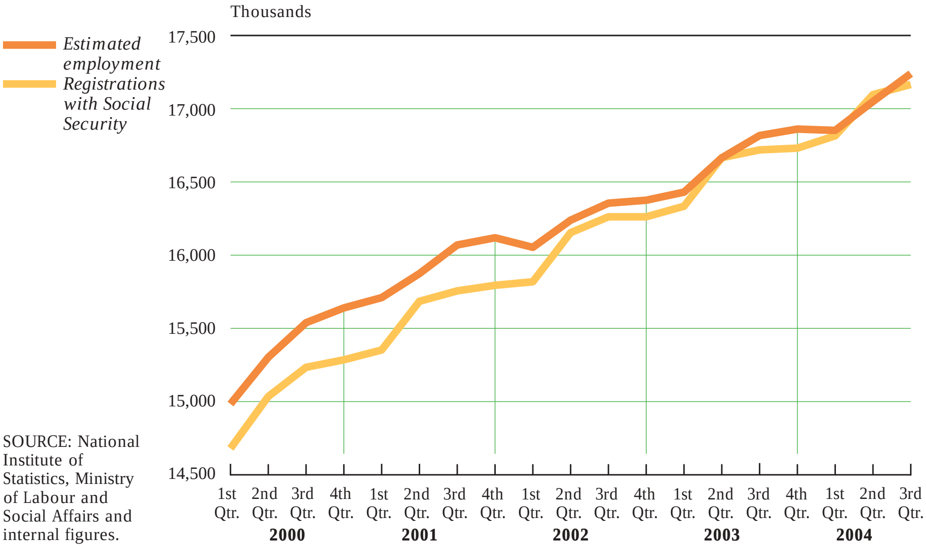
Job creation continues in third quarter

Employment shows increased growth in third quarter.

Spain's economy created 190,300 net new jobs in the third quarter of 2004, according to the Labour Force Survey, a figure substantially higher than that for the same period last year. As a result, the job creation rate rose to 2.5% year-to-year, two decimals higher than in the previous quarter. This performance confirms the relatively strong state of the labour market in the summer period, already suggested by other indicators such as registrations with Social Security and figures on hiring contracts.

EMPLOYMENT CONTINUES TO RISE

Registrations with Social Security and estimated employment (Labour Force Survey)



SOURCE: National Institute of Statistics, Ministry of Labour and Social Affairs and internal figures.

Social Security figures confirm strength of labour market as do hiring contracts registered with INEM.

In fact, registrations with Social Security also recovered in September raising their growth rate to 2.8% year-to-year, three decimals more than in the month before. This meant a recovery from the drop in August, presumably attributable to distortions arising from changes in job situation brought about by the beginning of the holiday period. The same situation of firmness was to be seen in new hiring contracts registered with the National Institute of Employment (INEM) with an increase of 15.0% in September, putting the cumulative increase at 14.3%.

ESTIMATED EMPLOYMENT

Third quarter 2004

	No. of employees (thousands)	Quarterly change		Cumulative change		Annual change		Share
		Absolute	%	Absolute	%	Absolute	%	%
By sector								
Agriculture	895.4	–13.5	–1.5	–56.4	–5.9	–15.3	–1.7	5.2
Non-farm	16,345.0	203.8	1.3	434.8	2.7	437.9	2.8	94.8
Industry	*3,104.5*	*13.4*	*0.4*	*29.0*	*0.9*	*–42.3*	*–1.3*	*18.0*
Construction	*2,072.2*	*12.3*	*0.6*	*80.3*	*4.0*	*83.0*	*4.2*	*12.0*
Services	*11,168.3*	*178.1*	*1.6*	*325.5*	*3.0*	*397.2*	*3.7*	*64.8*
By type of employer								
Private sector	14,396.7	120.8	0.8	282.0	2.0	321.5	2.3	83.5
Public sector	2,843.7	69.5	2.5	96.4	3.5	101.1	3.7	16.5
By work situation								
Wage-earners	14,076.6	199.6	1.4	324.0	2.4	346.3	2.5	81.6
Permanent contract	*9,684.0*	*20.0*	*0.2*	*150.3*	*1.6*	*173.9*	*1.8*	*56.2*
Temporary contract	*4,392.6*	*179.6*	*4.3*	*173.7*	*4.1*	*172.3*	*4.1*	*25.5*
Non-wage-earners	3,145.3	–13.6	–0.4	53.6	1.7	82.1	2.7	18.2
Entrepreneurs with employees	*941.8*	*–10.1*	*–1.1*	*9.6*	*1.0*	*33.6*	*3.7*	*5.5*
Entrepreneurs without employees	*1,945.9*	*–14.8*	*–0.8*	*47.7*	*2.5*	*59.4*	*3.1*	*11.3*
Family help	*257.6*	*11.3*	*4.6*	*–3.7*	*–1.4*	*–10.9*	*–4.1*	*1.5*
Other	18.5	4.4	30.9	0.8	4.5	–5.9	–24.1	0.1
By time worked								
Full-time	15,774.6	198.6	1.3	288.0	1.9	241.9	1.6	91.5
Part-time	1,465.8	–8.2	–0.6	90.4	6.6	180.7	14.1	8.5
By sex								
Males	10,467.5	89.5	0.9	144.4	1.4	113.8	1.1	60.7
Females	6,772.9	100.9	1.5	234.0	3.6	308.7	4.8	39.3
TOTAL	**17,240.4**	**190.4**	**1.1**	**378.4**	**2.2**	**422.6**	**2.5**	**100.0**

SOURCE: National Institute of Statistics and internal figures.

Employment reaches 17.24 million persons with foreign workers making up 29% of new employment created in twelve month period.

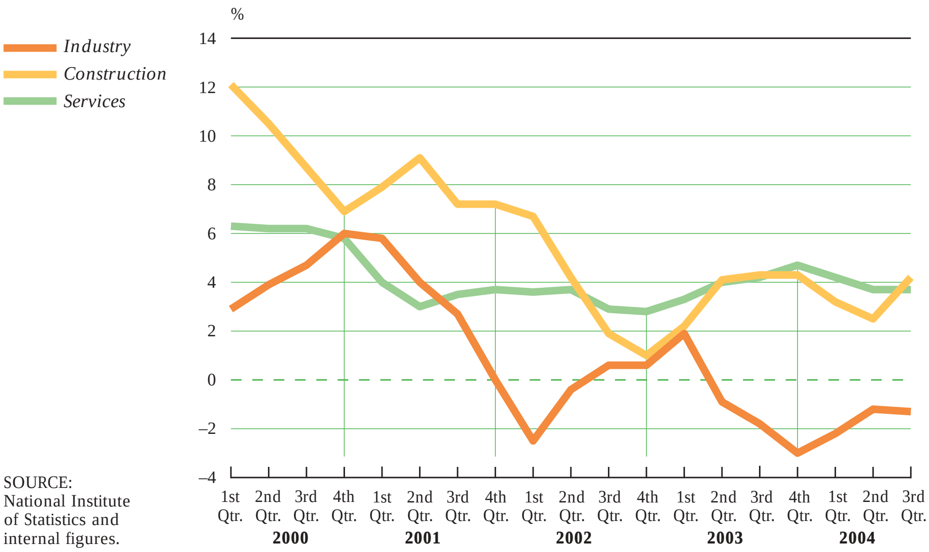
Recovery of the labour market, according to the results of the Labour Force Survey, raised the number of those working to 17.24 million persons, a figure never before reached, with 422,600 new jobs being created over the past year. The increased strength in employment was confined to nationals seeing that among foreign workers employment showed a drop in growth in spite of the fact that it held at very high levels (19.1% year-to-year). As a result, the proportion of foreign workers in new jobs created over the past twelve months again dropped to stand at 29.1% (123,000 jobs). In any case, the foreign worker population stood at all-time highs with a figure of 768,000 persons in the third quarter, that is to say, 4.5% of total employment.

Construction continues to show very notable strength and employment in services growing at high sustained rate.

The increased strength of employment in the third quarter was especially notable in construction, given that both in industry and services the situation in previous periods was maintained. In the first case, there was a moderate but sustained decrease while, in the second case, sharp stable growth was reported. Agriculture, in turn, continued the downward trend in the number of persons employed.

EMPLOYMENT RECOVERS IN CONSTRUCTION AND HOLDS STEADY IN SERVICES

Year-to-year change in estimated employment in sector



SOURCE: National Institute of Statistics and internal figures.

Very sharp improvement in employment among those under 20 years of age and women.

The improvement in employment during the quarter was especially notable among young people, particularly those under 20 years of age, a situation which may be explained by the increase in temporary work in the holiday period. Some 27.7% of all new employment created in the third quarter was within this age segment (19.4% in the same quarter last year). By sex, females continued to show a higher level in the matter of finding a new job, to the point where 73.1% of the new jobs created since the third quarter of 2003 were taken up by women.

Self-employment stabilizes increase at notable levels while wage employment makes progress boosted by public sector.

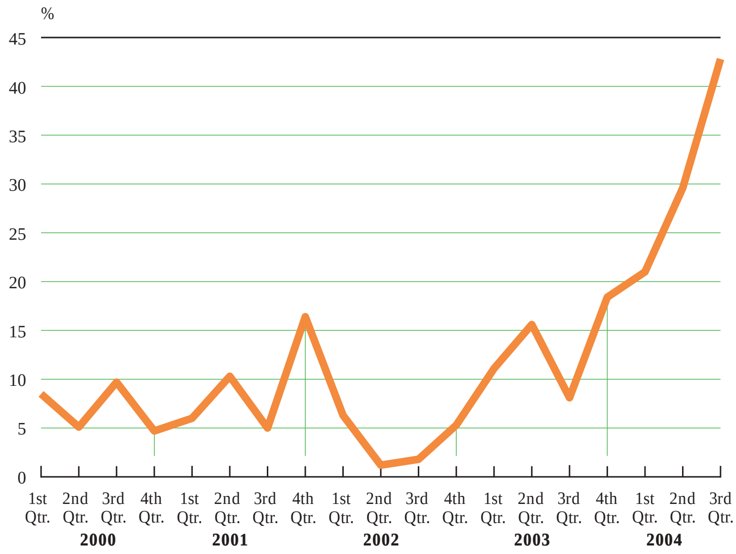
The increased growth of employment came about among wage earners, given that non-wage earner employment stabilized its increase at 2.7% year-to-year. The better state of wage employment came from the increase in public employment which moved up to growth of 3.7% year-to-year, one and a half points above the figure for private wage employment. As a result, personnel working in government and public corporations came to represent 23.9% of new jobs created in the last 12 months, a relatively high proportion compared with the 16.5% which public sector employees represent over total employment.

Increase in temporary jobs and part-time jobs shows unusual boost.

Figures for the third quarter also confirmed an increase in temporary jobs over permanent employment, so that the temporary job rate measured over the wage-earning population rose to 31.2%, a half-point above the third quarter of 2003. The rise in temporary jobs was parallel to that in part-time work which moved up to growth at a very high rate (14.1%), particularly because of the boost in this type of employment among males. In fact, part-time work represented 42.8% of all new employment created in the past 12 months, a proportion representing an all-time high. In spite of this, the proportion of total employment involving part-time work held at a modest level, 8.5% of the total. Among the female population, the level reached 17.3% of all those employed in the third quarter of 2004, as against 2.8% in the case of males.

BOOST IN PART-TIME WORK

Part-time work over total employment created in past year



SOURCE: National Institute of Statistics and internal figures.

Asturias, Catalonia and Basque Country step out of general recovery.

From a geographical perspective, the highest growth in employment was recorded in Murcia, Andalusia and Madrid with rates of around 4%. at the other end of the scale stood Catalonia, Asturias and Galicia with rates of around 1% and the Basque Country where employment dropped by 0.4% compared with the third quarter of 2003.

Lower growth of labour force eases reduction in unemployment.

Estimated unemployment, 2,031,300 persons in the third quarter, dropped by 83,300 compared with the same period in 2003, both because of growth of employment and the moderation in the increase in labour force which went to 1.8%, the lowest figure in recent years. In any case, this increase was higher than that for the population of 16 years and older. As a result, in the past 12 months the labour force grew by 339,300 persons as against 197,700 for the population over 16 years. This differential was especially significant in the case of females given that those newly joining the labour force, 247,500, was well above the increase in population which would indicate an increased desire on the part of women to move into the labour market. In the case of men, on the other hand, the increase in population of working age was the same as that for those joining the labour force.

LABOUR FORCE, EMPLOYMENT AND UNEMPLOYMENT BY AUTONOMOUS COMMUNITY
Third quarter 2004

	Labour force			Employed			Unemployed			Unem-ployment rate %
	Total (1,000s)	Annual change	% annual change	Total (1,000s)	Annual change	% annual change	Total (1,000s)	Annual change	% annual change	
Andalusia	3,248.2	66.8	2.1	2,686.6	100.1	3.9	561.6	–33.3	–5.6	17.3
Aragon	532.1	11.3	2.2	507.2	15.3	3.1	24.9	–4.0	–13.9	4.7
Asturias	433.0	–8.6	–2.0	392.9	2.9	0.7	40.1	–11.5	–22.3	9.3
Balearic Islands	453.0	11.1	2.5	423.5	11.0	2.7	29.5	0.1	0.3	6.5
Canary Islands	887.5	17.3	2.0	786.9	15.2	2.0	100.6	2.1	2.2	11.3
Cantabria	245.1	0.2	0.1	222.6	5.1	2.3	22.5	–4.9	–17.8	9.2
Castile-Leon	1,083.8	21.0	2.0	980.4	32.2	3.4	103.4	–11.1	–9.7	9.5
Castile-La Mancha	751.2	11.6	1.6	684.8	14.5	2.2	66.4	–2.9	–4.2	8.8
Catalonia	3,207.4	21.6	0.7	2,920.7	27.8	1.0	286.7	–6.2	–2.1	8.9
Valencian Community	2,060.3	60.6	3.0	1,840.6	59.2	3.3	219.7	1.4	0.7	10.7
Extremadura	471.1	11.4	2.5	395.4	9.7	2.5	75.7	1.7	2.3	16.1
Galicia	1,293.2	20.3	1.6	1,128.4	12.7	1.1	164.8	7.6	4.8	12.7
Madrid Community	2,606.5	65.9	2.6	2,444.5	89.5	3.8	162.0	–23.6	–12.7	6.2
Murcia	551.9	22.2	4.2	495.4	20.6	4.3	56.5	1.6	2.9	10.2
Navarre	261.6	2.9	1.1	249.8	5.4	2.2	11.8	–2.6	–17.8	4.5
Basque Country	1,001.5	–3.9	–0.4	910.3	–3.5	–0.4	91.2	–0.4	–0.4	9.1
La Rioja	125.7	2.2	1.8	119.0	2.8	2.4	6.7	–0.5	–7.1	5.3
Ceuta and Melilla	58.7	5.5	10.3	51.4	2.2	4.5	7.3	3.3	–	12.4
TOTAL	**19,271.7**	**339.3**	**1.8**	**17,240.4**	**422.6**	**2.5**	**2,031.3**	**–83.3**	**–3.9**	**10.5**

SOURCE: National Institute of Statistics and internal figures.

Unemployment rate drops to 10.5% in third quarter…

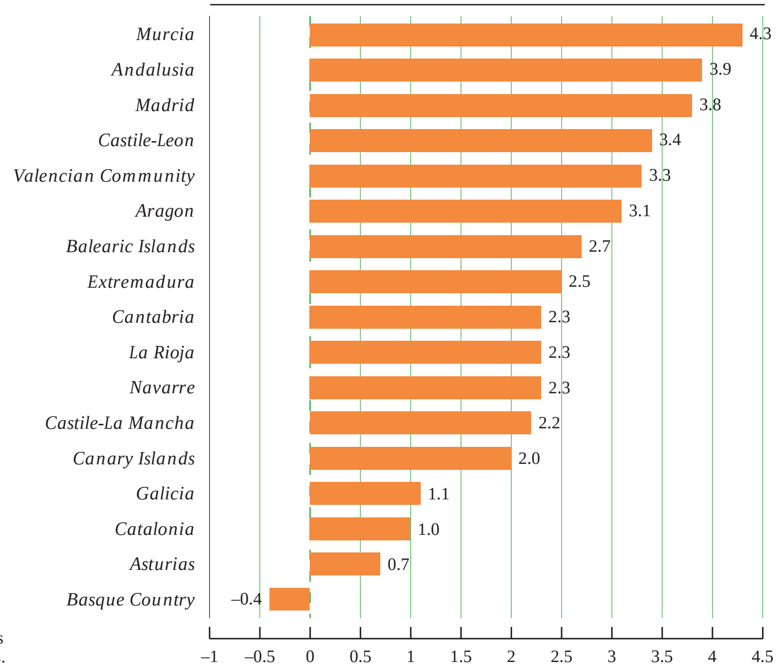
The unemployment rate stood at 10.5%, seven decimals below the same quarter last year, while there continued to be sharp differences between the indices for males and females at 7.9% and 14.4% respectively. The level of unemployment among those under 25 years of age, in turn, stood at 21.4%, nine decimals less than in the same quarter last year.

…while number of households with all members unemployed drops to 3.4% of total.

The improvement in the unemployment rate was also reflected in the proportion of households in which all members were without work, 3.4% of the total, one decimal less than in the third quarter of 2003. In addition, the situation was not substantially different for heads of family, a population group in which the unemployment rate held at 6.1%. For spouses and children of the person of reference, on the other hand, the situation was notably more favourable, although among these groups the unemployment rates were higher than in the case of heads of family at 11.7% and 16.4% respectively. Long-term unemployment affected 12.4% of those without work, one decimal less than in the same period last year.

MURCIA, ANDALUSIA, MADRID AND VALENCIAN COMMUNITY LEAD JOB CREATION

Annual change in percentage estimated employment



SOURCE: National Institute of Statistics and internal figures.

UNEMPLOYMENT

Third quarter 2004

	No. of unemployed	Quarterly change		Cumulative change		Annual change		Share	Unemployment rate
		Absolute	%	Absolute	%	Absolute	%	%	% of labour force
By sex									
Males	894.1	–4.2	–0.5	–28.0	–3.0	–22.1	–2.4	44.0	7.9
Females	1,137.2	–57.1	–4.8	–67.7	–5.6	–61.2	–5.1	56.0	14.4
By age									
Under 25 years	484.1	–3.8	–0.8	–20.6	–4.1	–32.9	–6.4	23.8	21.4
Other	1,547.1	–57.5	–3.6	–75.2	–4.6	–50.5	–3.2	76.2	9.1
By personal situation									
Long-term unemployment	251.5	–16.7	–6.2	–21.7	–7.9	–13.5	–5.1	12.4	–
Seeking first job	316.1	13.2	4.4	–20.3	–6.0	–40.1	–11.2	15.6	–
Other	1,463.7	–57.7	–3.8	–53.7	–3.5	–29.8	–2.0	72.1	–
TOTAL	**2,031.3**	**–61.3**	**–2.9**	**–95.7**	**–4.5**	**–83.3**	**–3.9**	**100.0**	**10.5**

SOURCE: National Institute of Statistics and internal figures.

Reluctance to change location goes against accepting new jobs.

In addition, reluctance to change location remained the main obstacle to moving out of an unemployment situation as only 19.4% of unemployed persons were ready to make a change of residence in order to obtain a job (20.7% in the same period in 2003).

More unemployed persons prepared to accept lower wages.

An obstacle of lesser importance seems to be the possibility of having to take a different kind of work to that formerly followed, seeing that 68.9% of those unemployed were ready to take a new job when it meant a change from previous occupation. Finally, the proportion of unemployed persons ready to accept a new job when it meant wages lower than the person's level of skill or a job category lower than expected was up by nearly three points to stand at 44.2% and 49.4% respectively, thus to some extent reflecting a worsening of employment expectations.

Registered unemployment: recovery from dip in August

Registered unemployment in September shows lower than usual increase during this period.

The number of unemployed registered at INEM rose by 20,023 in September to stand at a total of 1,618,415 at the end of the month. This increase, normal for this period of the year, was well below that for the same month last year so that the rate of increase in unemployment again moderated going to 0.7% year-to-year. As a result, there was a full recovery from the poor figure for August.

Cumulative balance as of September best in last four years.

The cumulative balance for the first nine months of the year which showed a decrease in registered unemployment of 93,072 persons, which was somewhat higher than in 2003 and the most favourable in the last four years. The decreases were spread over various sectors and groups to a sharper extent than in 2003, with the exception of services where the drop was fairly similar.

REGISTERED UNEMPLOYMENT BY SECTOR, SEX AND AGE
September 2004

	No. of unemployed	Change over December 2003		Change over same period year before		% share
		Absolute	%	Absolute	%	
By sector						
Agriculture	36,891	–1,033	–2.7	606	1.7	2.3
Industry	245,019	–19,274	–7.3	–5,796	–2.3	15.1
Construction	179,481	–32,407	–15.3	4,084	2.3	11.1
Services	938,843	–29,872	–3.1	25,789	2.8	58.0
First job	218,181	–10,486	–4.6	–14,115	–6.1	13.5
By sex						
Males	649,283	–75,979	–10.5	3,783	0.6	40.1
Females	969,132	–17,093	–1.7	6,695	0.7	59.9
By age						
Under 25 years	235,354	–22,396	–8.7	–17,364	–6.9	14.5
All other ages	1,383,061	–70,676	–4.9	27,842	2.1	85.5
TOTAL	**1,618,415**	**–93,072**	**–5.4**	**10,568**	**0.7**	**100.0**

SOURCE: National Employment Institute and internal figures.

PRICES

CPI further contained in September

Inflation rate drops another decimal in September to stand at 3.2%.

The consumer price index (CPI) rose by 0.2% in September, one decimal less than in the same month in 2003. As a result, the year-to-year rate dropped to 3.2%, thus continuing a slight downward trend for the third consecutive month. In any case, the inflation rate held somewhat more than one point above the lows seen in the first quarter. Underlying inflation, in turn, held stable at 2.9%, with a cumulative increase of seven decimals over the low for the year.

INFLATION GRADUALLY EASING

Year-to-year change rate in consumer price index

SOURCE: National Institute of Statistics.

Fresh food behind more moderate inflation.

The moderation seen in the CPI is again entirely attributable to fresh food prices which compensated for the rise in energy prices and the slight increase in processed foods and services. Industrial product prices, on the other hand, played a neutral role during the month.

CONSUMER PRICE INDEX

	2003			2004		
	% monthly change	% change over Dec. 2002	% annual change	% monthly change	% change over Dec. 2003	% annual change
January	–0.4	–0.4	3.7	–0.7	–0.7	2.3
February	0.2	–0.2	3.8	0.0	–0.7	2.1
March	0.7	0.5	3.7	0.7	0.0	2.1
April	0.8	1.3	3.1	1.4	1.4	2.7
May	–0.1	1.2	2.7	0.6	2.0	3.4
June	0.1	1.3	2.7	0.2	2.2	3.5
July	–0.6	0.6	2.8	–0.8	1.4	3.4
August	0.5	1.1	3.0	0.4	1.8	3.3
September	0.3	1.4	2.9	0.2	2.0	3.2
October	0.7	2.1	2.6			
November	0.3	2.4	2.8			
December	0.2	2.6	2.6			

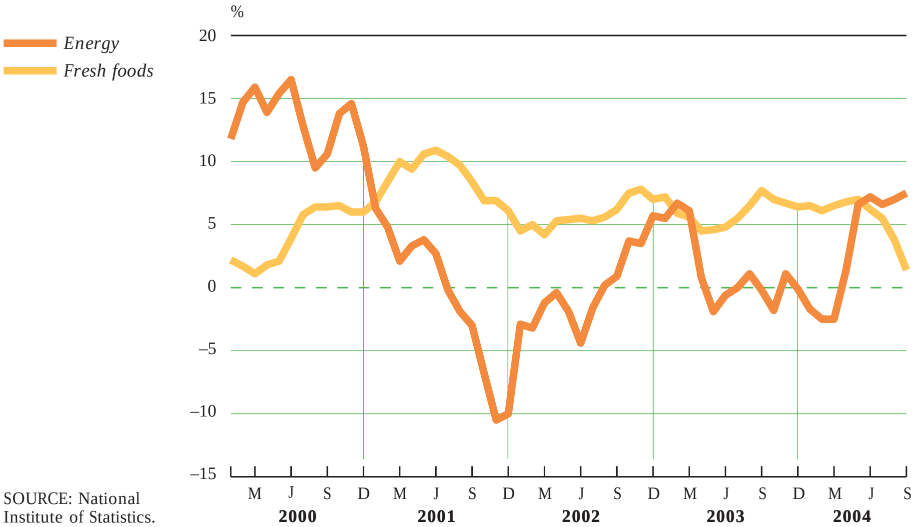
SOURCE: National Institute of Statistics.

Weakness in certain farm markets at origin and drop in import prices favour moderation in fresh foods.

The decrease in fresh food prices for the fourth consecutive month was especially strong in September thus reflecting the weakness in prices at origin. The reasons behind this trend are to be found both in the drop in import prices and the weaker state of the domestic market in certain products. Year-to-year growth of this component stood at 1.4%, the lowest figure in more than four years. The sharp drop in poultry prices, certain types of meat and vegetables and fresh produce were the main reasons behind this performance.

FRESH FOODS COMPENSATE FOR RISE IN ENERGY

Year-to-year change in consumer price index by component



SOURCE: National Institute of Statistics.

Processed foods, on other hand, not dropping.

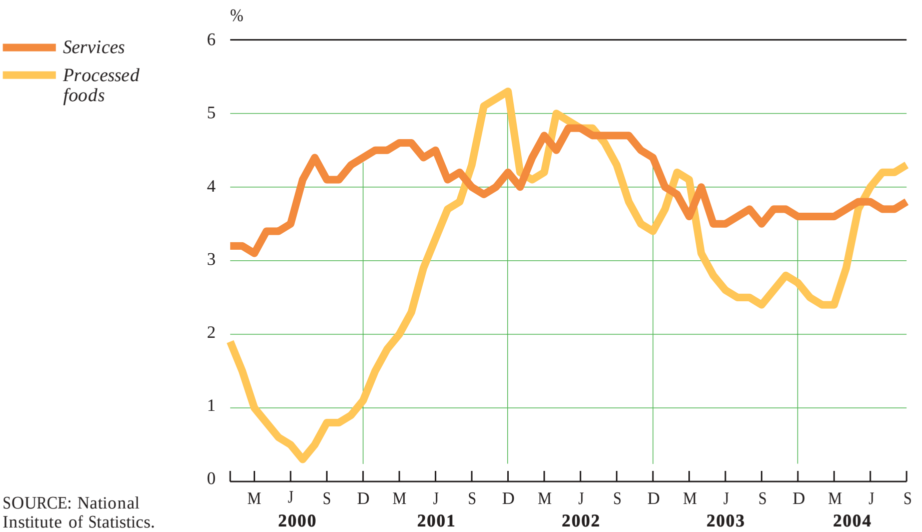
The moderation in fresh food prices stands in contrast to the difficulties experienced in processed food prices which rose slightly in September after two months of stability, to some extent going against some prospects of containment. In any case, the rise in prices (going up one decimal to 4.3% year-to-year) is not troubling especially in a context of moderation in prices at origin.

Services prices maintaining high but stable growth levels.

The profile of prices in services was quite similar also showing growth of one decimal to stand at 3.8% year-to-year, a rate which does not constitute any significant change over the state of sustained and stable increase over the past 12 months. Nevertheless, some headings, such as air transportation, recreational services and financial services are showing substantial growth. This growth is being compensated by modest increases in medical services, cultural activities and organized travel, as well as relative containment in prices for tourism and the hotel trade, thanks to moderation in hotel prices.

SERVICES AND PROCESSED FOODS STABILIZE GROWTH RATE

Year-to-year change in consumer price index



SOURCE: National Institute of Statistics.

Energy continues to move up as result of pressure in oil market.

Non-energy industrial prices, on the other hand, maintained a neutral performance thus consolidating a tendency to low growth (1.0% year-to-year in September) in spite of the end of the summer sales which, naturally, brought about increases in clothing and footwear prices although these were of similar size to those at the same time last year. In addition, the moderation in this component may be explained by the compensating effect of decreases in prices of data processing products, photographic and audiovisual goods, which underwent sharp competition.

CONSUMER PRICE INDEX BY COMPONENT

September

	Indices (*)	% monthly change		% change over previous December		% annual change	
		2003	2004	2003	2004	2003	2004
By type of spending							
Food and non-alcoholic beverages	113.9	0.9	0.0	3.4	2.3	4.4	3.0
Alcoholic beverages and tobacco	116.0	0.0	0.1	2.7	5.6	2.7	5.7
Clothing and footwear	107.2	2.8	3.0	–7.5	–7.9	3.9	2.1
Housing	109.7	0.1	0.2	2.2	3.3	2.5	4.0
Household equipment	105.7	0.3	0.2	0.9	0.6	2.0	1.5
Health	105.4	0.1	0.1	1.8	0.0	2.2	0.2
Transport	110.7	–0.1	0.2	1.8	6.8	1.5	6.0
Communications	93.5	0.0	–0.1	0.6	–0.2	–3.0	–1.0
Recreation and culture	104.1	–1.6	–1.3	0.3	0.7	0.5	0.5
Education	113.3	0.7	0.8	1.7	1.4	5.0	4.0
Hotels, cafés and restaurants	115.6	–0.8	–0.8	3.9	3.8	4.0	4.0
Other	111.1	0.3	0.2	2.8	2.6	3.2	2.9
By group							
Processed food	112.3	0.1	0.2	2.0	3.7	2.4	4.3
Unprocessed food	117.8	2.2	–0.2	5.9	0.9	7.7	1.4
Non-food products	109.1	0.1	0.2	0.8	1.8	2.5	3.2
Industrial goods	105.6	0.7	0.8	–1.3	0.3	1.6	2.6
Energy products	*108.6*	*–0.4*	*0.1*	*1.0*	*8.7*	*–0.2*	*7.5*
Fuels and oils	*110.7*	*–0.6*	*0.1*	*0.9*	*11.4*	*–0.8*	*9.7*
Industrial goods excluding energy products	*104.5*	*1.0*	*1.1*	*–2.0*	*–2.2*	*2.1*	*1.0*
Services	113.3	–0.5	–0.4	3.3	3.4	3.5	3.8
Underlying inflation (**)	109.8	0.2	0.2	1.0	1.4	2.8	2.9
GENERAL INDEX	**110.4**	**0.3**	**0.2**	**1.4**	**2.0**	**2.9**	**3.2**

NOTES: (*) Base 2001 = 100.
(**) General index excluding energy products and unprocessed foods.
SOURCE: National Institute of Statistics.

Industrial goods prices maintain 1% growth rate.

On the other hand, a negative note continued to show up in energy prices because of their constant increase which put year-to-year growth at 7.5% in September as a result of the impact of the sharp rise in oil prices in recent months. Since last March, this component has added somewhat more than nine decimals to the inflation rate, that is to say, practically all the increase in the general index.

Oil prices threaten immediate future of CPI.

The slight moderation in the CPI in September confirmed forecasts regarding the deflationary impact of fresh food prices and their potential for compensating for increases in energy. Over the short term, however, the recent increases in oil prices put any continuation of this trend in doubt so that they could increase pressure on the CPI if the price of energy continues at its current high levels. With regard to other segments, the relative stability of remaining components of the CPI will not contribute to any further worsening of the inflation rate.

Price differential with euro area up 1.1 points in September.

Spain's inflation differential with the euro area rose by one decimal in September to stand at 1.1 percentage points, according to the harmonized consumer price index. Growth of prices in Spain was higher than in the euro area in practically all groups making up the index with the exception of alcoholic beverages and tobacco and medical services, both of which are rising sharply in Europe. The widest differentials continued to show up in food and transportation, in the latter case because of the higher relative increase of these prices in Spain in recent months. In addition, the clothing and communications groups also showed differentials somewhat higher than the average for the general index and, furthermore, exhibiting an upward profile.

Producer prices continue upward trend

Producer prices increase growth by four points since March...

Producer prices continued their upward trend in September with a growth rate going to 4.6% year-to-year, two decimals above the figure for the month before. As a result, the increase in factory-gate prices since March has moved up by practically four percentage points.

INFLATION INDICATORS

Percentage change over same period year before

	Farm prices	Producer price index					Import prices				GDP deflator (*)
		General index	Consumer goods	Capital goods	Intermediate goods	Energy goods	Total	Consumer goods	Capital goods	Intermediate goods	
2003											
June	7.8	0.9	2.0	1.2	0.4	–0.9	0.7	–0.6	–7.2	3.8	–
July	5.6	1.1	2.5	1.1	0.1	0.2	0.0	–3.4	–7.2	3.2	–
August	7.1	1.1	2.7	1.1	0.0	0.1	1.5	4.5	–9.1	2.9	3.7
September	13.5	0.8	2.7	1.2	0.3	–2.4	–2.8	–0.2	–17.7	0.9	–
October	10.0	0.6	2.5	1.2	0.7	–3.6	0.8	2.8	–0.6	–0.0	–
November	9.7	1.3	2.6	1.4	0.9	–0.4	–0.2	–0.4	–7.0	1.8	3.8
December	9.8	1.1	2.4	1.3	1.0	–1.1	–1.4	–1.4	–9.4	1.0	–
2004											
January	4.4	0.7	2.1	1.3	1.4	–3.6	–3.7	–1.0	–8.4	–3.6	–
February	–2.6	0.7	2.1	1.3	2.0	–5.4	1.8	–6.0	–6.2	7.5	3.6
March	1.3	0.8	2.3	1.3	2.6	–5.6	–2.3	–3.6	–7.0	–0.5	–
April	3.3	2.6	2.9	1.3	3.7	1.2	1.4	–3.9	2.6	3.4	–
May	7.1	3.8	3.1	1.2	4.4	7.2	5.3	2.9	–1.1	8.6	3.7
June	12.0	4.0	3.1	1.2	4.8	7.1	–0.5	–3.3	–2.0	1.4	–
July	...	4.1	2.8	1.6	5.3	7.2	–0.3	2.6	–8.9	1.8	–
August	...	4.4	2.2	1.7	5.7	9.0	...	...	...	...	...
September	...	4.6	2.0	1.6	5.8	11.0	...	...	...	...	...

NOTES: (*) Gross figures corrected.
SOURCE: National Institute of Statistics, Ministry of Economy and internal figures.

…because of pressure from energy and intermediate goods.

The increase in energy prices and the sustained rise in non-energy intermediate goods was behind this trend. The increase was not of greater size thanks to the relative moderation in prices for consumer goods, including food, and the relative weakness in capital goods. As a result, consumer goods prices in September eased their growth rate by two decimals going to 2.0%. Capital goods, in turn, showed a growth rate of 1.6% year-to-year, one decimal less than the month before.

Import prices, on other hand, grow by a modest 0.3% in first seven months of year.

Import prices dropped slightly in July, particularly in the area of non-energy goods, although the decrease was not spread generally over all product groups. This decrease did not prevent a modest average increase of 0.3% being recorded in the first seven months of the year as a whole, brought about by the relative strength of the euro and the sharp increase in imports from low-cost manufacturing countries.

…in spite of sharp increase in energy in recent months.

The moderation in import prices might have been somewhat greater if it were not for the continued rise in energy prices. In any case, in the first seven months of the year as a whole, the cumulative average change in energy prices continued to be negative (–0.9%), in spite of the fact that the average cost of imported oil went to 195.6 euros a tonne, 3.7% more than in the January-July period in 2003. Other intermediate goods showed a lower increase in July but recorded a cumulative increase of 4.8%, mainly because of metal products. Thirdly, consumer goods maintained a moderate decrease, somewhat sharper in non-food products. Finally, capital goods recorded a weaker state with an average cumulative drop of 4.3%.

Surprising sharp rise in farm prices in June.

Farm prices underwent a sharp rise in June repeating the performance seen the month before and thus breaking away from the moderate tone seen in previous months. As a result, in the first six months of the year as a whole, the average increase in farm prices went up to 4.4%, a rate which to some extent increases uncertainty in an overall situation where prospects had pointed to moderation.

FOREIGN SECTOR

Growth of trade deficit eases in July

Trade deficit grows by nearly 29% as of July.

The trade deficit of Spain's economy slackened its growth in July thanks to some recovery in exports in a framework of a lower imports. In spite of this, the cumulative imbalance for the first seven months of 2004 was 28.9% above the same period last year reaching a figure of 31.7 billion euros. The export/import ratio, in turn, stood at 73.1%, some 3.7 points below the January-July period in 2003.

FOREIGN TRADE
January-July 2004

	Imports			Exports			Balance	Export/ Import ratio (%)
	Million euros	% annual change in value	% share	Million euros	% annual change in value	% share	Million euros	
By product group								
Energy products	12,393	10.2	10.5	2,920	20.8	3.4	–9,473	23.6
Consumer goods	33,564	14.9	28.4	34,336	1.6	39.8	772	102.3
Food	*7,424*	*9.5*	*6.3*	*10,378*	*2.0*	*12.0*	*2,954*	*139.8*
Non-foods	*26,140*	*16.1*	*22.1*	*23,958*	*0.1*	*27.7*	*–2,182*	*91.7*
Capital goods	18,993	15.4	16.1	11,081	14.2	12.8	–7,912	58.3
Non-energy intermediate goods	53,129	7.9	45.0	37,999	6.7	44.0	–15,131	71.5
By geographical area								
European Union	74,143	9.3	62.8	61,781	4.6	71.6	–12,363	83.3
Euro area	*64,741*	*9.8*	*54.8*	*51,632*	*4.4*	*59.8*	*–13,109*	*79.8*
Other countries	43,935	14.6	37.2	24,554	9.3	28.4	–19,381	55.9
Eastern Europe and Ex-USSR	*5,694*	*24.6*	*4.8*	*3,613*	*2.1*	*4.2*	*–2,081*	*63.4*
United States	*4,342*	*6.8*	*3.7*	*3,325*	*0.3*	*3.9*	*–1,018*	*76.6*
Japan	*3,324*	*19.9*	*2.8*	*740*	*26.0*	*0.9*	*–2,584*	*22.3*
Latin America	*4,691*	*11.9*	*4.0*	*4,102*	*6.6*	*4.8*	*–589*	*87.4*
OPEC	*6,982*	*2.0*	*5.9*	*1,925*	*–1.0*	*2.2*	*–5,057*	*27.6*
Rest	*18,902*	*19.0*	*16.0*	*10,850*	*17.4*	*12.6*	*–8,052*	*57.4*
TOTAL	**118,078**	**11.2**	**100.0**	**86,335**	**5.9**	**100.0**	**–31,743**	**73.1**

SOURCE: Department of Customs and Special Taxes and internal figures.

Imports continue strong growth particularly in capital goods and non-food consumer goods.

Imports were up by 15.9% nominal in July going to a cumulative figure of 118.1 billion euros for the year, 11.2% more than the year before. In real terms, the increase was somewhat less at 10.9% if we take into account the slight rise in import prices. Capital goods, with a cumulative increase of 20.6% in volume and non-food consumer goods, with 19.0%, were the product groups showing the highest increases. Consumer electronics, motor vehicles, furniture and footwear were the sectors most affected by the flow of imports. Purchases of capital goods showed particularly strong growth in the case of railway equipment. There was a somewhat lower increase in imports of food products (11.0%) although here again it was higher than last year. Finally, purchases of intermediate goods showed a repetition of the notable increase seen the month before, especially in non-energy products. In spite of this, the cumulative increase by volume was still below that for the same period in 2003.

Purchases from the EU-15 grow above 7% while those from 10 new member states up by 37%.

By geographical area, purchases from the European Union made up of 15 member states (EU-15) grew by 7.2% real in the first seven months of the year as against 17.4% in the case of those from the rest of the world. We should point out the sharp increase in purchases from the ten new member states at 37.0% nominal up to July 2004. Outside the EU, the biggest increases showed up in trade with the Middle East, China, Japan and Brazil.

Exports consolidate recovery in July but cumulative annual growth still below last year.

Exports, in turn, grew by 12.7% nominal in July, thus consolidating the improvement recorded in June. In any case, the cumulative figure for the first seven months (86.3 billion euros) meant an increase of 5.9%, equivalent to 6.1% real (7.8% in the same period in 2003). The continuing improvement in exports in July may be seen in some countries of the euro area but more sharply in Latin America, some newly industrialized Asian countries and those of the former USSR. Exports to third countries as a whole showed a relatively more favourable cumulative balance with growth of 11.0% real as against 4.6% in the case of shipments to the former EU-15.

Exports of non-food consumer goods weak.

By product, the best situation showed up in capital goods with a cumulative real increase of 15.4% as of July with notable foreign sales in transportation equipment, mainly ships and aircraft. Exports of consumer goods were much weaker with an increase of 3.1% real (3.3% in the case of non-food products), there being a notable drop in sales of certain consumer manufactures (footwear and furniture) in nominal terms and a modest increase in motor vehicle exports at 3.5%. Finally, exports of intermediate goods showed a somewhat more positive performance than in previous months with a real increase of 5.4%, partly brought about by strong foreign demand for iron and steel as well as energy products.

Current account balance shows increased deficit in July

Current account deficit continues to rise.

The current account balance showed a deficit of 3.7 billion euros in July, practically twice that for the same month last year. The worsening of the current account balance put the cumulative deficit for the last 12 months at 29.8 billion euros, a figure equivalent to 3.8% of the gross domestic product estimated for 2004.

All headings of current account balance worsen in July.

The worsening of the situation in July was due to the poor performance in the various headings of the balance, especially the trade balance which considerably increased its negative figure, along with the services balance which showed a reduction in surplus. The transfers balance was also more negative than in July last year as was the case in the incomes balance. In the first case, however, the cumulative balance for the year shows a surplus in contrast to that for the incomes balance.

Surplus in tourist balance drops under pressure from increase in payments.

The worsening of the services surplus may be attributed to the various services heading and, to a lesser extent, to the tourist balance. In this case, the opposing trends in receipts and payments, downward and upward respectively, brought about the drop in the surplus. In the period between July 2003 and July 2004 the tourist balance showed a positive figure of 28.6 billion euros, 2.2% lower than in the same period one year earlier. Receipts, in turn, were 1.2% higher as against an increase of 15.2% in payments.

BALANCE OF PAYMENTS

Cumulative figure for last 12 months in million euros

	July 2003	July 2004	% change
Current account balance			
Trade balance	–36,044	–44,946	24.7
Services			
Tourism	*29,266*	*28,635*	*–2.2*
Other services	*–2,049*	*–3,155*	*53.9*
Total	27,217	25,480	–6.4
Income	*–11,481*	*–11,026*	*–4.0*
Transfers	1,017	734	–27.9
Total	**–19,291**	**–29,758**	**54.3**
Capital account	**7,875**	**8,925**	**13.3**
Financial balance			
Direct investment	2,585	–7,461	–
Portfolio investment	–9,143	27,482	–
Other investment	26,682	16,751	–37.2
Total	**20,124**	**36,772**	**82.7**
Errors and omissions	–5,461	–4,550	–16.7
Change in assets of Bank of Spain	–3,247	–11,389	250.8

NOTES: The figure resulting from the sum of current account balance, capital account balance and financial balance is compensated by the change in assets of Bank of Spain plus errors and omissions.
SOURCE: Bank of Spain and internal figures.

Sharp increase in net world borrowing.

Capital account, in turn, showed a surplus of 623 million euros in July, well above the figure for the same month last year. As a result, the balance for the last 12 months was 13.3% above that for the previous year.

Spanish direct investment abroad down 40% while foreign investment in Spain drops by more than 65%.

In the last 12 months ending July 2004, financial account, excluding Bank of Spain transactions, showed total net entries of 36.8 billion euros, 82.7% more than in the same period last year. Spanish direct investment abroad remained weak, particularly in the field of corporate investment, given that fixed asset investment showed substantial increases. In spite of everything, the total volume was 40.0% lower than in the same period last year. Direct foreign investment continued to drop with a decrease of 65.3% compared with last year. Under direct foreign investment the decrease was concentrated in corporate investment while that going into real estate purchases was still slightly higher than in the same period the year before. Portfolio investment from abroad, on the other hand, was up by nearly 80%.

PUBLIC SECTOR

Sharp drop in Treasury deficit as of September

Tax collections up 6% as of September.

Central government non-financial revenues rose by 4.0% in the first nine months of 2004 to reach 79.6 billion euros. This figure does not include those segments of tax collections for personal income tax and the greater part of indirect taxes ceded to autonomous communities and municipalities, with the result that it is of little significance as an indicator of the revenue capacity of the central government through general taxes. If we include the revenue segments thus ceded, collections amounted to 108.1 billion euros which meant an increase of 6.1% compared with the same period in 2003.

Tax on corporate income shows biggest increase under direct taxes.

The main source of collections was direct taxes amounting to 50.6 billion euros, 6.5% more than in the same period in 2003. The biggest increase showed up in corporate income tax (17.2%) which may partly be explained by the decrease in rebates. Revenue from personal income tax showed very modest growth at 1.5% compared with the same period the year before.

CENTRAL GOVERNMENT BUDGET IMPLEMENTATION

September 2004

	Month		Cumulative for year	
	Million euros	% change over same month year before	Million euros	% change over same month year before
Non-financial revenue	**8,807**	**14.6**	**79,592**	**4.0**
Non-financial revenue adjusted (*)				
Personal income tax	4,362	6.6	34,033	1.5
Corporate tax	217	–	14,907	17.2
VAT	4,441	16.7	33,086	8.5
Special taxes	1,446	3.0	13,106	4.3
Other	1,512	26.5	12,992	3.1
Total	**11,978**	**14.0**	**108,124**	**6.1**
Non-financial spending	**7,383**	**–8.9**	**82,105**	**–1.0**
Treasury balance	**1,424**	**–**	**–2,513**	**–60.9**
Surplus (+) or deficit (–) (**)	***409***	**–**	***845***	***294.9***

NOTES: (*) Includes tax segments ceded to autonomous communities under financing system in operation as of 2002.
(**) In terms of National Accounting.
SOURCE: Ministry of Finance and internal figures.

Collections for indirect taxes up by 8% with VAT in the lead.

Collections for indirect taxes, in turn, amounted to 48 billion euros, 7.6% more than in 2003 with value added tax (VAT) in the lead. The amount obtained under this tax heading as of September was 33.1 billion euros, 8.5% more than in the same period in 2003. Under special taxes, most headings advanced at a rate well above inflation. In the case of petroleum products, collections rose to a lesser extent (3.4%) probably reflecting the effect of the increased price of fuels. In contrast to 2003, the figures for 2004 do not include tax on certain modes of transport which is considered as revenue proper to the autonomous communities. On the other hand, there was a quite notable increase in revenues obtained from the tax on insurance premiums (10.0%), related to the increase in the motor vehicle market, and to revenue arising from foreign trade thanks to the sharp increase in imports from third countries.

Drop in government property earnings, revenue from fees and public service charges and current transfers.

Apart from tax resources, fees and public service charges showed an appreciable decrease but less than that recorded for government property earnings and current transfers, 10.4% and 6.1% respectively. On the other hand, capital transfers rose by 19.3% compared with the same period last year while funds arising from disposal of public investment property was of little significance.

Central government non-financial spending down slightly because of lower interest payments and decrease in real investment.

Central government non-financial spending, in turn, was down by 1.0% with a total amount of 82.1 billion euros. This figure does not include the balancing entry for revenue corresponding to those segments of tax ceded to the autonomous communities. The drop in spending showed up in current operations as a result of the decrease in interest payments (15.5%) as well as lower real investments. Spending related to public consumption, on the other hand, showed a notable increase, 4.4% in the case of staff and 21.2% in the case of purchases of goods and services.

Treasury deficit drops substantially in contrast to surplus in National Accounting.

The central government Treasury balance as of September, that is to say, the difference between non-financial revenues and spending, was negative for an amount of 2.5 billion euros, some 60.9% lower than in the same period last year. The deficit, in turn, was up practically four times to reach 8 billion euros, mainly because of the sharp rise in financial assets related to movements of central government deposits in financial institutions. Property allocations (1.6 billion euros in total) were also up sharply (24.3%), their main destination being Gestor de Infraestructuras Ferroviarias. In terms of National Accounting, on the other hand, the budgetary balance was positive to the amount of 845 million euros, although certain adjustments related to debt in the case of Andalusia and RENFE are still outstanding.

SAVINGS AND FINANCING

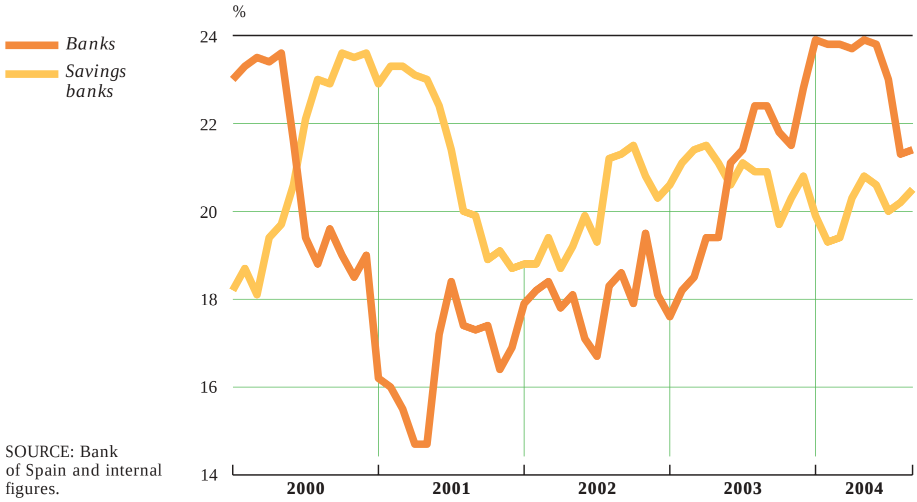
Slight slowdown in bank credit to private sector

Bank credit to companies and households increases more than twice that in euro area.

Bank credit to companies and households rose by 15.5% in August compared with the same month last year. This rate is 8 decimals lower than that recorded the previous month but, in any case, it is still a high growth rate, more than twice that in the euro area as a whole. Demand for bank credit by the private sector continues to be fostered by the good economic situation and favourable financing terms, with very low interest rates.

MORTGAGE LOANS SHOW STRONG GROWTH RATE

Year-to-year change in mortgage loans by institution



SOURCE: Bank of Spain and internal figures.

Savings banks grant more loans to private sector than banks.

In the past twelve months, total loans granted by savings banks to companies and households rose by 17.5%, some 4 decimals more than the annual change rate in December 2003. In the same period, loans granted by banks increased by 13.7%, some 9 decimals more than in December. As a result, total loans granted by savings banks to the private sector stood at 403.1 billion euros at the end of August, 4.2 billion euros more than by banks. Savings banks thus held a higher balance than banks in this segment after reaching this point for the first time in June.

Total amount of mortgage loans up 25% in last 12 months.

The biggest advance in loans to companies and households continued to show up in mortgage loans. Mortgage loans granted by banks and savings banks rose by 20.9% in August compared with the same month in 2003, some 2 decimals more than in the previous month. If we include securitizations and other lending institutions this rate goes up to 24.8%, according to the Spanish Mortgage Association. As a result, mortgage loans for the moment are showing no sign of a slowdown. Growth in household incomes, demographic factors and low interest rates remain an incentive.

Slowdown in commercial credit to companies.

On the other hand, commercial credit, which goes to finance working capital of companies, rose by only 5.0% in August compared with 12 months earlier, as against a year-to-year rate of 12.5% in July. Leasing, which goes to finance the purchase of capital goods and real estate by companies and self-employed professionals, rose by 9.8% over August 2003, a similar rate to that recorded the previous month.

CREDIT TO COMPANIES AND HOUSEHOLDS

August 2004

	Total	Change this year		Change over 12 months		% share
	Million euros	Million euros	%	Million euros	%	
Trade credit	55,214	–317	–0.6	2,648	5.0	6.2
Secured loans (*)	505,424	63,299	14.3	87,416	20.9	56.8
Other term loans	272,469	21,570	8.6	26,031	10.6	30.6
On-demand loans	20,633	–290	–1.4	1,170	6.0	2.3
Leasing	28,008	2,939	11.7	2,497	9.8	3.2
Doubtful loans	7,364	–302	–3.9	–319	–4.2	0.8
TOTAL	**889,112**	**86,900**	**10.8**	**119,443**	**15.5**	**100.0**

NOTES: (*) For most part made up of mortgage security.
SOURCE: Bank of Spain and internal figures.

Slight rise in default rate.

On the other hand, doubtful loans broke away from the downward path in absolute figures begun last March to stand at 7.4 billion euros. This figure meant a default rate of 0.83%, a very slight increase of one-hundredth of a point compared with the lowest level in recent years recorded the previous month. The rate for banks and savings banks (excluding other credit institutions) also rose very slightly to 0.69%, one-hundredth of a point above the all-time low recorded the month before.

Loan rate for companies records low in August.

Bank loan rates generally increased slightly in August. As a result, the composite interest rate for loans by credit institutions rose to 3.97%, some 9 basis points more than in the previous month and 12 basis points above the all-time low in June. In fact, this increase was due to the household component for which the composite interest rate rose to 4.44% to thus stand 10 basis points below 12 months earlier. The composite interest rate for non-financial companies marked up a new all-time low of 3.46% to stand at 45 basis points below one year earlier.

Slight decrease in home-purchase interest rate for all institutions in September.

On the other hand, the interest rate on mortgage loans for more than a 3-year term for acquisition of non-subsidized housing at credit institutions as a whole in September dropped slightly by 3 basis points to 3.37%. In any case, it showed an increase of 11 basis points over the all-time low in May 2004 although it stood some 6 basis points below the same month in 2003.

Major increase in time-deposits for more than 2-year term

Discrepancy between growth of deposits and loans.

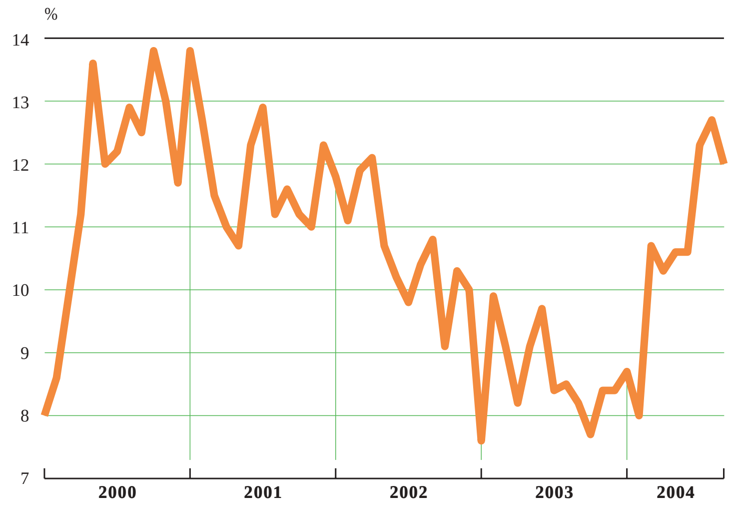
Total deposits of the resident private sector in euros and foreign currency rose by 12.0% in August 2004 compared with the same month last year, 0.8 points less than in July. In the last twelve months, these deposits rose by 72 billion euros. This figure was considerably lower than the increase in loans so that credit institutions had to carry out security issues and securitizations and have recourse to the foreign interbank market to compensate for this imbalance.

Savings banks attract more deposits than banks.

The rate of attracting deposits dropped in August both for banks and savings banks. Nevertheless, the change rate in the case of the latter was more than double that for banks showing 14.2% as against 6.6% respectively.

SLOWDOWN IN RECOVERY OF BANK DEPOSITS

Year-to-year change



SOURCE: Bank of Spain and internal figures.

Deposits for more than 2-year term up 63% in past 12 months.

By type of deposit, time-deposits for more than a 2-year term showed a spectacular rise of 63.3%, some 1.3 points more than in July. Deposits in currencies other than the euro also showed a notable year-to-year increase of 18.8%, although this was substantially lower than in preceding months. Term deposits for less than a 2-year term, in turn, were down by 2.7% over the course of the past year.

DEPOSITS BY COMPANIES AND HOUSEHOLDS AT CREDIT INSTITUTIONS

August 2004

	Total	Change this year		Change over 12 months		% share
	Million euros	Million euros	%	Million euros	%	
On-demand	175,597	6,693	4.0	17,048	10.8	26.0
Savings (*)	153,010	7,801	5.4	13,336	9.5	22.7
2-year term	155,601	–625	–0.4	–4,253	–2.7	23.1
More than 2-year term	106,761	29,399	38.0	41,395	63.3	15.8
Repos	78,025	224	0.3	3,672	4.9	11.6
Total	**668,995**	**43,493**	**7.0**	**71,201**	**11.9**	**99.2**
Deposits in currencies other than euro	**5,135**	**984**	**23.7**	**812**	**18.8**	**0.8**
TOTAL	**674,130**	**44,477**	**7.1**	**72,013**	**12.0**	**100.0**

NOTES: (*) Deposits redeemable at notice, according to ECB definition.
SOURCE: Bank of Spain and internal figures.

Preference of those participating in mutual funds on one hand lean toward global funds and, on other hand, toward short-term bond-based funds.

The assets of mutual funds showed a small increase of 82 million euros in September to reach 212.8 billion euros, if we eliminate duplications in funds of funds, an increase of 7.5% over December, according to figures provided by Inverco, the sector organization. The September increase may be attributable to capital gains, given that there were net withdrawals that month amounting to 594 million euros. Nevertheless, in the course of the first three quarters, net purchases of participations, discounting sales, amounted to 12.7 billion euros with the biggest increases showing up in global funds, short-term bond-based funds and guaranteed bond-based funds in a context of volatility in financial markets.

Number of persons participating up 4% over December.

The total number of persons participating in funds at the end of September was 8,072,435, some 5,993 more than one month earlier. The increase over December was 338,411 participants, an increase of 4.4%. The biggest increase in participants so far this year showed up in the global funds category with an increase of 155%.

Average annual yield on mutual funds stands at 3%.

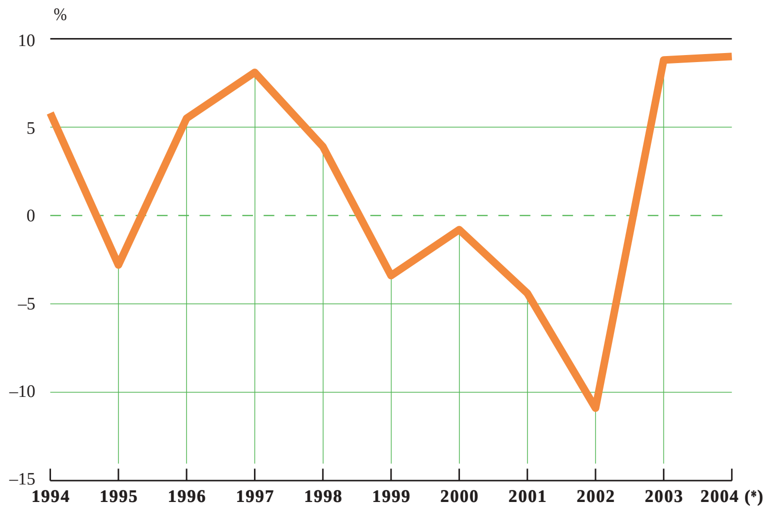
The weighted average yield on mutual funds in the past twelve months was 2.9% in September. All types of mutual funds obtained positive annual yields, thanks to the recovery in the stock markets. The biggest annual gains showed up in national share-based funds, with an extraordinary 20.7% increase, and by share-based funds in emerging countries, with 20.0%.

Argentina leaves recession behind

Argentina overcomes worst recession since 1914 thanks to sound economic policy.

The Argentine economy has brilliantly overcome one of the worst recessions in its history. We should have to go back to 1914 to find a slump in gross domestic product (GDP) of a magnitude such as the 10.9% drop which took place in 2002. This was a drop which, furthermore, came after three years of decrease in the GDP. Starting out from this difficult situation, between the first quarter of 2002 (when the recession hit bottom) and the second quarter of 2004, the economy recorded growth of 31%. While factors outside the Argentine economy contributed to the recovery (especially the favourable international economic scene in 2003 and 2004), the basic element behind this notable recovery was the sound management of economic policy. The main highlights in this process are set out below.

ARGENTINE ECONOMY OVERCOMES ONE OF WORST RECESSIONS IN ITS HISTORY
Annual real change in gross domestic product



NOTES: (*) First half of 2004.
SOURCE: National Institute of Statistics and Census, Republic of Argentina (INDEC) and internal figures.

From 2001 to start of 2002: urgent measures adopted

Measures adopted at end of 2001 aimed at stopping flight of capital.

As is well-known, the recession, which began in the final years of the Nineties, by the end of 2001 had brought about a complicated financial situation which undermined citizen and corporate confidence, the most obvious result being the increase in withdrawals of bank deposits. In response to this situation, in November of that year the Argentine government was obliged to set up a system of restricting cash withdrawals (a mechanism became known as the «corralito»). Not long after, the government adopted a series of measures limiting the movement of capital. Finally, at the end of that year it proceeded to put a moratorium on its external debt.

Legislative framework finalized at beginning of 2002.

At the beginning of 2002, the Argentine government broadened legislation aimed at halting the economic collapse. Its two key decisions were to abandon the system of convertibility of the peso and the dollar, going to a system of flexible exchange rate, along with reorganization of the financial system, with essential factors being a start to making the «corralito» more flexible and conversion of all assets and liabilities in the economy to pesos. At the same time, taking an initiative which would later turn out to be a key move, it modified the legal framework covering the operations of the Republic of Argentina Central Bank (BCRA) allowing it to follow an independent monetary policy.

Broad range of institutional reform.

The full impact of the broad reforms in the institutional framework of the economy had to wait until the second quarter of 2002 before showing the first signs of any improvement in the economy. In the first three months of the year, the GDP fell by 16.3% year-to-year putting it at a level similar to the beginning of 1993 in absolute terms. Many other indicators show the difficulties of the time. On quarterly average, inflation rose by 4.2% year-to-year (the previous quarter there was a situation of deflation) and the peso depreciated by 60% against the U.S. dollar between January and March.

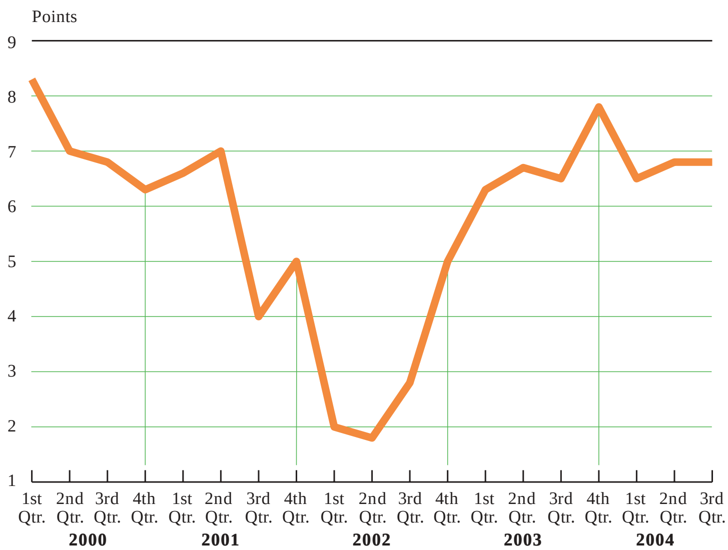
Confidence recovers in 2002

Economic recovery as of second quarter makes it possible to remove exceptional measures.

As of the second quarter of 2002, the economy stopped growing worse, stabilizing and then opening the way to a new stage. As the economic improvement became confirmed, the government was able to remove most of the exceptional measures previously adopted. In this respect, of special significance was the opening up of the «corralito»

GOVERNMENT ACTION AIDS RECOVERY OF CONFIDENCE

IFO indicator of future expectations (*) in Argentine economy



NOTES: (*) Economic performance expected over next six months.
SOURCE: IFO Institute.

which, after an initial increase in the limit on withdrawals decided on in October, became fully applicable in November.

Notable steps on fiscal consolidation in 2002.

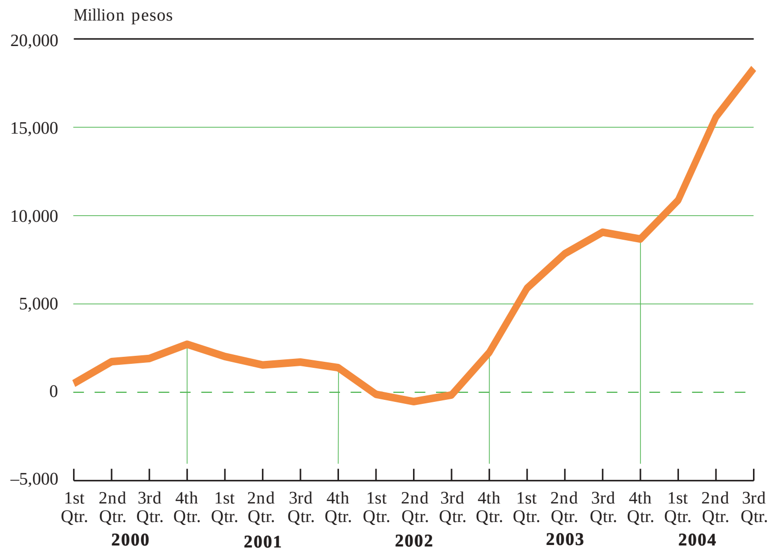
Also of note is the effort made to improve the public accounts, both national and provincial. In 2002, the national public deficit was 50% less than one year earlier and amounted to 4.6 billion pesos. In spite of the fact that part of this consolidation came from the reduction in payments to service the public debt, it was the recovery in tax revenues together with lower growth in spending which brought about this positive result. In fact, in 2002 the primary balance, that is to say, discounting interest on the public debt, stood at a surplus equivalent to 0.7% of the GDP. Provincial public finances followed along similar lines although the adjustment in spending was greater.

Major contribution from tax on exports.

The partly exceptional nature of 2002 was also reflected in the government budget. The tax heading making the biggest contribution to the recovery in revenue collections was the tax on exports. This tax is of a nature which the Ministry of Economy itself has recognized as not being traditional when compared with other more normal headings, such as the value added tax and tax on profits.

EXCELLENT RESULT IN MATTERS OF FISCAL CONSOLIDATION

Cumulative primary balance of national public sector (*) for four quarters



NOTES: (*) Non-financial national public sector balance excluding interest on public debt and revenue from privatizations.
SOURCE: Finance Secretariat of Ministry of Economy and internal figures.

Argentine Central Bank shows brilliant results in controlling inflation.

Another result of the effective management of economic policy was the success achieved in the monetary programmes of the BCRA in its efforts to deal with inflationary pressures. There was the fear that, as a factor partly brought about by the depreciation of the Argentine peso, the consumer price index (CPI) would shoot sky-high as had happened in the devaluation crises in the Eighties. Nevertheless, the CPI rose by only 25.9% on average in 2002, well below previous occasions. This result came largely because of the fact that, as of the second quarter of 2002, the BCRA began to institute an active monetary policy, something not possible before adoption of the legal framework at the beginning of that year.

Central bank concentrates on control of money supply and limited intervention in foreign exchange markets…

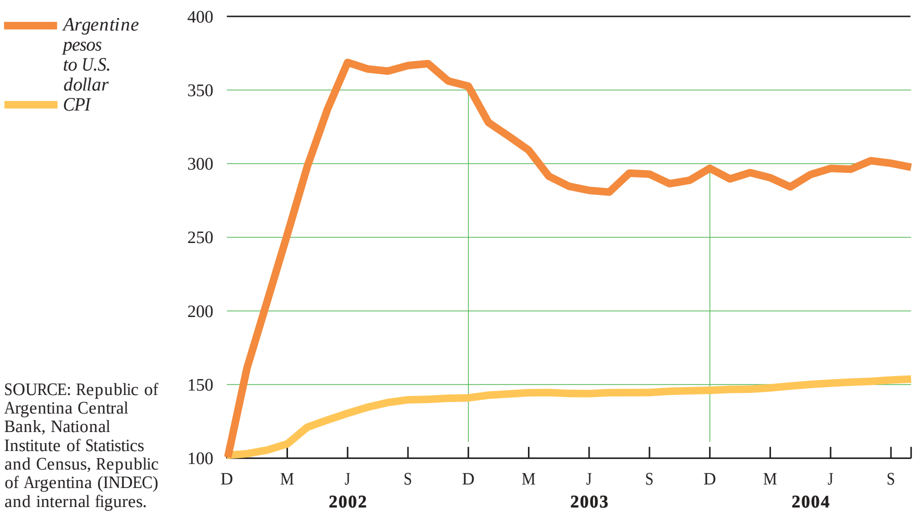
The BCRA established two main areas of action. Firstly, it wanted to ensure proper control over the money supply which would make it possible to limit inflationary pressures and at the same time provide sufficient liquidity to ensure that the financial institutions could meet their demands. With the aim of controlling the money supply it began to issue Central Bank Treasury Bills (known as LEBAC). Secondly, it would intervene in foreign exchange markets in order to at least partly stabilize the exchange rate. Such stabilization was also aimed at by strengthening controls over movement of capital.

…measures which make for easing prices and stabilization of exchange rate.

It was as of the second half of 2002 that these measures began to yield fruit, by stabilizing the exchange rate, improving the development of the LEBAC market and beginning to contain inflation. It should be pointed out that two other basic measures for avoiding an inflationary spiral were refraining from returning to practices of indexing wages as had been done in the Eighties and the freezing of privatized public services. At the end of 2002, the improvement in the key financial variables of the economy (such as interest rates, private sector deposits, credit to the private sector and the money supply) along with stabilization of prices were a sign of the success of the monetary policy followed.

MEASURES TAKEN BY ARGENTINE CENTRAL BANK PREVENTS DEPRECIATION OF PESO SHIFTING TO INFLATION

December 2001 = 100, in monthly averages



SOURCE: Republic of Argentina Central Bank, National Institute of Statistics and Census, Republic of Argentina (INDEC) and internal figures.

As 2002 advances, government measures help start of economic recovery.

As the above measures began to take effect, the economy showed notable recovery. In spite of the fact that for the year as a whole the GDP dropped by 10.9%, as mentioned earlier, the rate of year-to-year decrease moderated from 16.3% in the first quarter to 3.4% in the last quarter of 2002. A similar improved trend showed up in other significant economic indicators as the year advanced. Industrial production went from a drop of 16.1% year-to-year in February to end the year with growth of 11.3% year-to-year in December. After dipping by 1.6% year-to-year in real terms in the second quarter, exports of goods and services rose by 5.8% year-to-year in the fourth quarter. The year 2002 was thus characterized by a sharp worsening of the economy in the early months followed by a rapid turnaround of that drop in economic activity in the later part of the year.

From 2003 to 2004: economic recovery grows stronger

2003 and 2004 bring consolidation of recovery.

Following the exceptional situation reigning in 2001 and 2002, as of 2003 and so far in 2004 there has been a move into a stage of consolidation and normalization of the cycle. At the beginning of 2003, the main challenge was to consolidate the incipient improvement in the economic indicators recorded in the second half of the previous year. The political period beginning with the national elections in April 2003, which confirmed the new president elected by popular suffrage, represented what the Argentine Ministry of Economy itself called the normalization of the country's political institutions. This normalization came out the much-needed continuity and progress of economic policy.

Public finances greatly improve in 2003 with primary surplus of more than 2% of GDP…

Perhaps the area most sharply reflecting the depth of the government's political commitment was continuation of the disciplined management of the public finances. In 2003, compared with the deficit of 4.6 billion pesos the year before, the budget for the national public sector showed a surplus of 1.8 billion pesos. As in 2002, the positive turnaround in the public finances was largely brought about through an improvement in tax revenues and a readjustment of spending. The primary surplus in 2003 came to 2.3% of the GDP, a notable figure. The budget of the provinces, in turn, showed a primary surplus of 0.9% of the GDP. As a sign of the normalization of the economic situation, the tax headings which may be considered as traditional (value added tax and corporate tax) raised their contribution compared with non-traditional taxes (tax on exports and tax on financial transactions).

…which could be twice that in 2004.

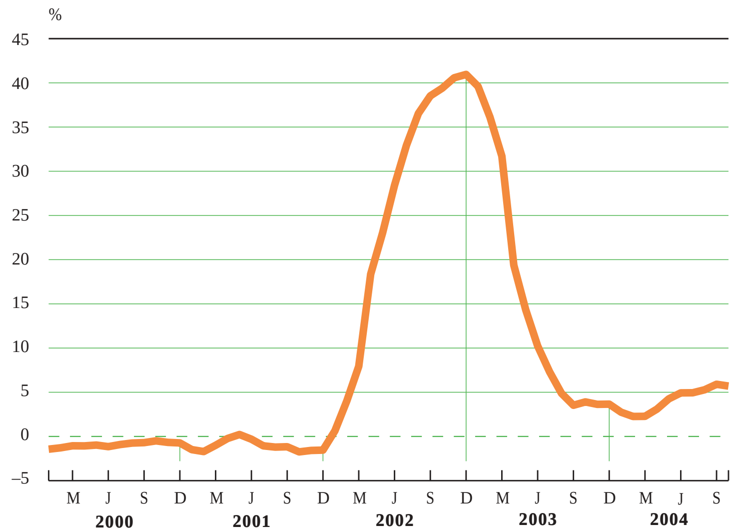
Figures for budgetary implementation in 2004 would indicate a sharpening of these trends. According to available estimates, the government's primary surplus could come to 4.4% of the GDP, while that for the provinces could stand at 2.2% of the GDP. The proposed law on fiscal responsibility presented in 2004, and the new system of co-participation of the State and provinces in tax collections now under discussion, would substantially improve fiscal coordination between the various levels of government.

Argentine Central Bank concentrates efforts on stabilizing inflation and obtains positive results.

In its monetary programmes for 2003 and 2004, the BCRA presented price stability as it main objective. In both years, the Argentine Central Bank has concentrated its efforts on controlling the money supply as the nominal anchor of monetary policy. Following growth of the broad monetary base figure (which includes notes and coin in circulation and Central Bank reserves plus so-called quasi-money issued by the provinces and municipalities until completion of its total withdrawal), by approximately 110% in 2002, the increase in 2003 eased to 30%. For 2004, the BCRA's monetary programme foresees growth of the monetary base in a band from 11% to 22% annual. Maintenance of the broad monetary base at the margins established since June 2003 is indicative of how well the system is operating. As a result, the trend in prices has remained stable, apart from temporary factors such as the rise in oil prices, thus consolidating the disinflation taking place since the beginning of 2003. At the same time, this situation is helping to bring about a notable easing of interest rates.

NOTABLE DROP IN INFLATION NOW STABILIZING AT MODERATE LEVELS

Year-to-year change in consumer price index



SOURCE: National Institute of Statistics and Census, Republic of Argentina (INDEC) and internal figures.

Agreement between government and IMF in September 2003.

In another sphere, we should point out that the Argentine government and the International Monetary Fund (IMF) reached agreement on September 20, 2003 regarding the restructuring of government debt held in private hands. According to the terms of this agreement, some 21 billion pesos was refinanced for the period 2004-2006 which represented a partial acquittance of 75% of the total amount of the debt under consideration (that issued before December 2001 together with accrued interest). The IMF agreement includes a series of demanding quantitative objectives, mainly in matters of fiscal discipline and price stability. For 2004, for example, it established the requirement of a primary government surplus of more than 3% of the GDP and average annual inflation of between 7% and 11%. As noted above, available figures indicate that these limits will be fully met.

Economic indicators up sharply in 2003 with this trend consolidating in 2004.

The Argentine economy has notably benefited from the sound economic policy followed in 2003 and so far in 2004. In 2003, GDP growth came to 8.8% year-to-year, a rate which continued into the first half of 2004 when the GDP rose by 9.0% compared with the year before. Average annual inflation was 13.4% year-to-year in 2003 and 4.1% year-to-year on average in the January-October period of 2004. Following an increase of 12.6% in 2003, industrial production held at very acceptable rates in 2004, of the order of 7.5% on average between January and September. Finally, since the end of 2003 the unemployment rate has stabilized at levels under 15% of the labour force, a reduction of five percentage points compared with the end of 2002.

Worst recession in Argentina's history overcome first by adopting urgent measures...

To sum up, after going through the worst recession in recent decades, Argentina's economy has recovered rapidly and convincingly. Behind this good performance, along with other factors such as the growth of the world economy, lies the good management of economic policy during these complicated years. In the measures taken by the Argentine government three stages stand out. To begin with, between the end of 2001 and the beginning of 2002, measures taken were of an urgent nature aimed at halting the flight of national assets due to the drop in corporate and citizen confidence.

...then through economic programme bringing back corporate and citizen confidence.

As of the second quarter of 2002, and more strongly so in 2003, the government and the Argentine Central Bank introduced a series of measures aimed at improving confidence and relieving the less positive effects of the 2001-2002 readjustment, especially the threat of inflation. The improvement in the economy and stabilization of the financial variables of the economy meant that most of the urgent measures adopted in the previous stage could be dropped. Finally, in economic terms, the years 2003 and 2004 may be considered as being marked by normalcy as opposed to the exceptional state of previous years, along with the beginnings of a new stage characterized by positive prospects.

2005 Central Government Budget

Macroeconomic scenario for 2005 Budget aimed at recovery of economic growth based on increased domestic demand.

The 2005 Budget bill has been presented to the House of Deputies for discussion and approval. The macroeconomic scenario of the Budget is aimed at a slight increase in growth of the gross domestic product (GDP) putting it at 3.0%, based on growth of domestic demand, particularly on investment in capital goods while taking into account a slight moderation in construction which, however, will continue at positive levels. Private consumption will maintain sustained growth while public consumption will moderate slightly from current high levels. The foreign sector will make a negative contribution to growth in spite of the gradual recovery in exports.

MACROECONOMIC SCENARIO FOR 2003-2005

	2003	2004	2005
GDP and figures (% real change)			
Spending – final national consumption	3.1	3.4	3.3
Spending – final national household consumption (*)	*2.9*	*3.2*	*3.2*
Spending – final general government consumption	*3.9*	*4.0*	*3.5*
Gross capital formation	3.4	3.8	4.0
Gross fixed capital formation	3.2	3.3	4.0
Capital goods and other products	*1.7*	*2.2*	*5.1*
Construction	*4.3*	*4.2*	*3.2*
Change in inventories (contribution to GDP growth)	0.1	0.1	0.0
Domestic demand	3.2	3.5	3.4
Exports of good and services	2.6	4.8	6.4
Imports of good and services	4.8	6.9	7.3
Foreign balance (contribution to GDP growth)	–0.8	–0.9	–0.6
Gross domestic product	**2.5**	**2.8**	**3.0**
GDP at current prices (billion euros)	744.8	791.3	841.0
GDP at current prices (% change)	6.6	6.3	6.3
Prices and costs (% change)			
GDP deflator	4.0	3.4	3.2
Real terms of trade	0.8	–3.0	–0.4
Compensation (labour cost) per employee	4.2	3.9	4.1
Labour market			
Employment (change as %)	1.8	2.0	2.0
Employment (change in thousands)	278.9	326.1	331.9
Unemployment: percentage of labour force (EPA)	11.3	11.1	10.8

NOTES: (*) Includes non-profit institutions serving households.
SOURCE: Ministry of Economy.

Spending

Consolidated spending of central government public sector amounts to 249.5 billion euros with growth of 7.8%.

Consolidated spending forecast in the 2005 Budget for the non-corporate central government public sector, excluding the change in financial liabilities, will amount to 249.5 billion euros in consolidated terms, that is to say, 29.7% of the GDP, a half-point more than in 2004. This means an increase of 7.8% compared with the figure initially budgeted for 2004, one and a half points more than estimated nominal growth of the economy.

CONSOLIDATED BUDGET ESTIMATES FOR CENTRAL GOVERNMENT, AUTONOMOUS BODIES, SOCIAL SECURITY AND PUBLIC CORPORATIONS FOR 2005

SPENDING

Million euros

	Central government	Autonomous bodies	Social Security	Public corporations	Consolidated total	% change over initial budget
Current operations						
Staff costs	20,439	1,915	1,975	1,015	25,343	4.7
Current goods and services	2,924	1,922	1,580	369	6,796	4.4
Financial costs	19,293	12	28	0	19,334	1.0
Current transfers	63,709	28,168	80,100	5	162,597	7.9
Total	**106,365**	**32,017**	**83,684**	**1,389**	**214,070**	**6.7**
Contingency fund	**2,491**	**–**	**–**	**–**	**2,491**	**6.2**
Capital operations						
Real investment	8,771	2,199	419	268	11,657	10.8
Capital transfers	6,900	1,307	28	3	6,698	–4.9
Total	**15,671**	**3,505**	**447**	**271**	**18,355**	**4.5**
Total non-financial operations	**124,526**	**35,523**	**84,130**	**1,660**	**234,915**	**6.5**
Financial assets	7,783	670	6,104	1	14,558	34.1
Financial liabilities	30,070	142	77	–	30,289	–9.8
Total financial operations	**37,853**	**812**	**6,181**	**1**	**44,847**	**0.9**
TOTAL	**162,379**	**36,335**	**90,311**	**1,661**	**279,763**	**5.6**

SOURCE: Central government budget and internal figures.

Figures do not include budgets of other corporate bodies in public sector, such as RTVE, AENA, Puertos del Estado and more than 60 public corporations and 40 government foundations.

The Budget does not include the budgets of other corporate public sector bodies. Among these public bodies are those concerned with the management of ports, airports and railway infrastructures, national regulatory commissions governing certain markets (energy, telecommunications, share markets), RENFE and FEVE railway companies, nearly 40 government foundations and somewhat more than 60 companies with a majority of government capital. Especially significant in this group is the case of Spanish Radio and Television, which expects losses, (after subsidies) of 643.1 million euros, (20 million euros more than initially forecast for 2004) which are financially covered by debt guaranteed by the government and which, in contrast to previous years, figures in the central government deficit. The text of the Budget bill foresees the concession of guarantees to a maximum of 1.7 billion euros for these purposes, of which 659 million applies to Spanish Radio and Television and 180 million euros to the RENFE railway company.

Pensions make up the biggest part of government spending.

From the point of view of purpose, the biggest part of total spending by the central government public sector is concentrated on pensions, which in 2005 will account for 79.2 billion euros, that is to say, 9.4% of the GDP. The increase in pension payments (6.8%) may be explained by increases (2.0%), the larger number of pensioners (0.8%) going up to 8.38 million beneficiaries, including State pensioners, the increase in certain pensions and, finally, from the effect of earlier pensions being replaced by others of larger amount.

2005 CENTRAL GOVERNMENT BUDGET: SUMMARY BY PROGRAMME POLICY

Million euros

	2005 budget	% of total	% annual change	% of estimated GDP	
				2005	2004
Pensions	79,221	31.8	6.8	9.42	9.37
Transfers to other levels of government	50,886	20.4	8.9	6.05	5.91
Public debt	19,272	7.7	1.4	2.29	2.40
Unemployment benefits	12,688	5.1	14.4	1.51	1.40
Infrastructures (4)	11,317	4.5	8.1	1.35	1.32
Other economic allocations	10,656	4.3	7.9	1.27	1.25
Agriculture, fishing and food	8,312	3.3	1.9	0.99	1.03
Management and administration of Social Security (1)	7,976	3.2	45.1	0.95	0.69
Services of general nature	6,967	2.8	3.2	0.83	0.85
Defence	6,794	2.7	4.5	0.81	0.82
Police and penitentiaries	6,499	2.6	7.7	0.77	0.76
Job promotion	6,233	2.5	7.0	0.74	0.74
Research, development and innovation	4,972	2.0	16.3	0.59	0.54
Health (2)	3,648	1.5	2.1	0.43	0.45
Industry and energy	1,743	0.7	4.4	0.21	0.21
Education	1,615	0.6	5.9	0.19	0.19
Financial and tax administration	1,425	0.6	2.8	0.17	0.18
Transportation subsidies (3)	1,309	0.5	–12.7	0.16	0.19
Social services and social programmes	1,197	0.5	5.7	0.14	0.14
Trade, tourism and small/medium business	1,195	0.5	2.7	0.14	0.15
Justice	1,185	0.5	8.6	0.14	0.14
Foreign policy	1,157	0.5	5.8	0.14	0.14
Culture	933	0.4	6.5	0.11	0.11
Housing aid and housing promotion	879	0.4	32.5	0.10	0.08
Other measures of economic nature	804	0.3	–1.1	0.10	0.10
Senior management	588	0.2	13.4	0.07	0.07
TOTAL (5)	**249,473**	**100.0**	**7.8**	**29.66**	**29.24**

NOTES: (1) Includes pension reserve fund for an amount of 5.35 billion euros in 2005.
(2) Figures not homogeneous because of certain agreements with public service health benefit societies and other factors.
(3) Assumption of RENFE debt by central government involves a reduction of transfers to this company so that transportation subsidies will grow by 0.7%.
(4) Transfer of Confederación Hidrográfica del Sur to Andalusia not included.
(5) Includes change in financial assets.

SOURCE: Central government budget and internal figures.

Financing of other levels of government, government debt and unemployment protection also take up a high proportion of spending.

The second biggest heading is made up of transfers to other levels of government, including the European Union, accounting for a total of 50.9 billion euros. Next, come payments for the government debt (7.7% of the total) which go up quite modestly thanks to the relative stability of interest payments. Fourth on the list is spending for unemployment benefits which are to grow by 14.4% nominal, mainly because of the increase in the number of those receiving job training income, given that beneficiaries of economic support decreased to a moderate extent.

Management and creation of infrastructures take up 11.3 billion euros with growth of 8% compared with initial 2004 budget.

The management and creation of infrastructures, in turn, is to take up 11.3 billion euros with growth of 8.1% compared with the year before. Programmes with the highest allocations are those involved in the construction and maintenance of highways (3.2 billion euros in total with growth of 6.5%) and port infrastructures, the latter for an amount of 1.96 billion euros, to be carried out by Puertos del Estado. In the area of railways, the new entity Administrador de Infraestructuras Ferroviarias (ADIF), brought about as a result of the merger of Gestor de Infraestructuras Ferroviarias and those business divisions of RENFE related to maintenance of the railway network, will invest 1.6 billion euros, 3.2% more than in 2004. Also of note are investments in waterworks and Aeropuertos Españoles y Navegación Aérea.

Revenue

Consolidated revenue of central government public sector for 2005 amounts to 216.8 billion euros.

Non-financial revenue of the central government public sector will amount to 235.5 billion euros in consolidated terms in 2005, that is to say, excluding the sum of internal transfers taking place between the various agencies of the central government administration, an increase of 6.5% over the initial budget the year before. The increase in revenue is to be met both by Social Security contributions and tax revenue, given that the other headings show decreases compared with the initial budget for the year before.

Direct taxes to grow at higher rate than indirect taxes although affected by moderation in collections for special taxes.

Under tax revenue, direct taxes show greater growth than indirect taxes (9.8% as against 7.3%) because of the increase in tax on corporate incomes (15.7%), because of higher corporate profits and personal incomes in spite of the drop in the tax rate. Under indirect taxes, collections for value added tax are expected to increase by 8.6%, 1.3 points above nominal growth of the economy, whereas special taxes will ease down to 4.9% in spite of the updating of tax rates on alcohol and tobacco (up 2%). Under non-tax revenue, we see a notable decrease in revenues on government property (26.7%) and a substantial drop in collections for fees (34.4%) which comes on top of a slight decrease in funds arising from current transfers. Only capital transfers showed a modest increase.

CONSOLIDATED BUDGET ESTIMATES FOR CENTRAL GOVERNMENT, AUTONOMOUS BODIES, SOCIAL SECURITY AND PUBLIC CORPORATIONS FOR 2005

REVENUE

Million euros

	Central government	Autonomous bodies	Social Security	Public corporations	Consolidated total	% change over initial budget
Current operations						
Direct taxes	63,689	20,840	83,220	–	167,750	9.4
Indirect taxes	43,051	–	–	–	43,051	8.1
Fees and other revenue	2,237	1,054	844	74	4,209	–4.6
Current transfers	5,353	10,041	4,933	1,271	12,213	–0.1
Government property earnings	1,767	297	1,064	13	3,141	–49.6
Total	**116,097**	**32,231**	**90,061**	**1,358**	**230,363**	**6.6**
Capital operations						
Disposal of real investments	94	473	0	–	567	6.1
Capital transfers	1,400	2,427	67	239	2,596	–8.7
Total	**1,494**	**2,900**	**68**	**239**	**3,163**	**–6.3**
Total non-financial operations	**117,592**	**35,131**	**90,129**	**1,598**	**233,526**	**6.4**
Financial assets	706	1,036	182	63	1,987	14.9
Total financial operations	**706**	**1,036**	**182**	**63**	**1,987**	**14.9**
TOTAL	**118,297**	**36,167**	**90,311**	**1,661**	**235,513**	**6.5**
Borrowing requirement	*–44,081*	*–168*	*0*	*0*	*–44,249*	*0.9*

SOURCE: Central government budget and internal figures.

Social Security contributions up 9% while tax load rises six decimals to 27.8% of GDP.

Social Security contributions, in turn, are to rise by 8.9% because of the increased number of persons registered and updating of contribution bases. As a result, taking into account collections forecast for direct taxes, indirect taxes and Social Security contributions, the tax load will stand at 27.8% of the GDP, six decimals above the estimated figure for 2004.

Budgetary balance

Consolidated Treasury budget deficit to be 0.2% of GDP, compatible with surplus (also 0.2%), according to National Accounting criteria.

As a result of the above transactions, the consolidated non-financial budget balance in Treasury terms for the central government, autonomous bodies, Social Security and other public corporations will be negative for an amount of –1.4 billion euros, that is to say, 0.2% of the GDP. On the other hand, in National Accounting terms, that is to say, applying accrual criteria, it is estimated that there will be a positive budget balance for an amount of 0.2% of the GDP, which comes about from compensation of a deficit in the central government and related bodies of 0.5% of the GDP (0.4% in the case of the central government plus 0.1% for Spanish Radio and Television), with a surplus of 0.7% in Social Security.

If change in financial assets is added, net deficit stands at 1.7% of GDP.

These figures do not take into account funds committed for net acquisition of financial assets, funds which, furthermore, are largely used to finance investment lying outside the budget through corporations such as ADIF, water corporations or for loans to motorway concessionaires. In consolidated terms, financial assets amount to 12.6 billion euros, that is to say, 1.5% of the GDP. These funds are not computed as spending so far as concerns the deficit in

National Accounting, given that they are considered as financial investments which are recoverable through the operation of the infrastructures being financed. Nevertheless, in any case, they constitute a deficit which, when added to the Treasury deficit, creates a net borrowing requirement for the central government and related bodies as a whole amounting to 13.96 billion euros, that is to say, 1.7% of the estimated GDP for 2005.

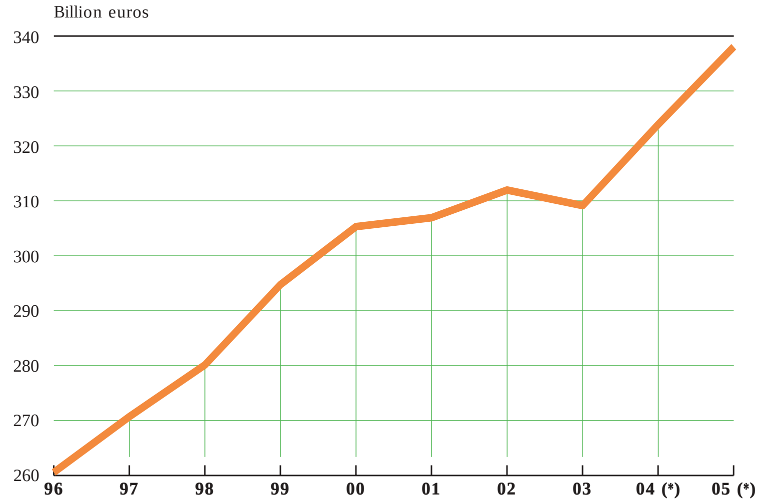
2005 BUDGET: NON-FINANCIAL DEFICIT AND BORROWING REQUIREMENT

	Million euros		As % of GDP	
	Central government	Consolidated	Central government	Consolidated
Non-financial revenues	117,592	233,526	14.0	27.8
Non-financial spending	124,526	234,915	14.8	27.9
Treasury deficit	**–6,934**	**–1,389**	**–0.8**	**–0.2**
Net change in financial assets	7,077	12,571	0.8	1.5
Net borrowing requirement	–14,011	–13,960	–1.7	–1.7
Change in financial liabilities	30,070	30,289	3.6	3.6
Borrowing requirement	**44,081**	**44,249**	**5.2**	**5.3**
Memo item: balance according to National Accounting	*–3,392*	*1,974*	*–0.4*	*0.2*

SOURCE: Central government budget and internal figures.

INCREASE IN GOVERNMENT DEBT

Government debt in circulation



NOTES: (*) Forecast.
SOURCE: Ministry of Economy and Finance.

Central government debt drops to 40.2% of GDP while debt of general government as a whole down to 47% of GDP.

Financing the borrowing requirement is to be carried out entirely through issues in euros of Treasury bills and bonds in balanced proportion. As a result, government debt in circulation, according to the Budget estimates, will amount to 338 billion euros at the end of 2005, a figure equal to 40.2% of the GDP and eight decimals lower than the year before. The debt balance for general government as a whole will stand at around 47% of the GDP in 2005, also down from the estimated level for the end of the current year.

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