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THE SPANISH ECONOMY

Monthly Report

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RESEARCH DEPARTMENT

"la Caixa"

Forecast

% change over same period year before unless otherwise noted

	2006	2007	2008	2007				2008	
				1Q	2Q	3Q	4Q	1Q	2Q
INTERNATIONAL ECONOMY			Forecast						Forecast
Gross domestic product									
United States	2.9	2.2	1.4	1.5	1.9	2.8	2.5	2.5	1.8
Japan	2.4	2.0	1.8	3.1	1.7	1.8	1.4	1.3	2.2
United Kingdom	2.9	3.1	1.9	3.1	3.3	3.1	2.8	2.3	2.0
Euro area	2.9	2.6	1.7	3.2	2.6	2.7	2.1	2.2	1.9
Germany	*3.1*	*2.6*	*1.9*	*3.7*	*2.6*	*2.5*	*1.8*	*2.6*	*2.0*
France	*2.4*	*2.1*	*1.6*	*2.2*	*1.7*	*2.4*	*2.2*	*2.0*	*1.7*
Consumer prices									
United States	3.3	2.8	3.9	2.5	2.5	2.4	4.0	4.2	4.0
Japan	0.2	0.1	0.5	–0.1	–0.1	–0.1	0.5	1.0	0.4
United Kingdom	2.3	2.3	3.3	2.9	2.6	1.8	2.1	2.4	3.3
Euro area	2.2	2.1	3.5	1.9	1.9	1.9	2.9	3.4	3.6
Germany	*1.6*	*2.3*	*2.8*	*1.8*	*2.0*	*2.3*	*3.1*	*2.9*	*3.0*
France	*1.7*	*1.5*	*2.9*	*1.2*	*1.2*	*1.3*	*2.3*	*2.9*	*3.2*
SPANISH ECONOMY			Forecast						Forecast
Macroeconomic figures									
Household consumption	3.7	3.1	1.7	3.5	3.4	3.1	2.7	1.8	1.7
Government consumption	4.8	5.1	4.9	6.1	5.0	5.1	4.4	4.7	4.8
Gross fixed capital formation	6.8	5.9	0.3	6.3	6.7	5.8	4.8	3.2	0.3
Capital goods	*10.4*	*11.6*	*2.3*	*13.1*	*13.1*	*11.6*	*8.6*	*6.3*	*2.9*
Construction	*6.0*	*4.0*	*–1.5*	*4.9*	*4.6*	*3.8*	*2.9*	*1.3*	*–1.8*
Domestic demand (contribution to GDP growth)	5.1	4.6	2.0	5.1	4.9	4.5	3.9	3.0	1.9
Exports of goods and services	5.1	5.3	3.6	3.6	4.7	7.7	5.1	5.0	3.9
Imports of goods and services	8.3	6.6	2.8	6.0	6.7	8.4	5.4	5.0	3.0
Gross domestic product	**3.9**	**3.8**	**2.0**	**4.1**	**4.0**	**3.8**	**3.5**	**2.7**	**2.0**
Other variables									
Employment	3.2	3.0	0.9	3.3	3.1	3.0	2.5	1.7	0.9
Unemployment (% labour force)	8.5	8.3	9.9	8.5	8.0	8.0	8.6	9.6	9.7
Consumer price index	3.5	2.8	4.6	2.4	2.4	2.4	4.0	4.4	4.6
Unit labour costs	2.3	2.7	3.0	2.6	2.6	2.7	2.8		
Current account balance (% GDP)	–8.8	–10.0	–10.3	–10.1	–9.0	–10.2	–10.7	–12.1	
Net lending or net borrowing rest of the world (% GDP)	–8.1	–9.5	–9.9	–9.5	–8.7	–10.1	–9.8	–11.3	
Government balance (% GDP)	1.8	2.2	0.2						
FINANCIAL MARKETS			Forecast						Forecast
Interest rates									
Federal Funds	5.0	5.0	2.2	5.3	5.3	5.1	4.5	2.8	2.0
ECB repo	2.8	3.9	4.2	3.6	3.8	4.0	4.0	4.0	4.0
10-year US bonds	4.8	4.6	4.0	4.7	4.8	4.6	4.1	3.5	4.0
10-year German bonds	3.8	4.2	4.4	4.0	4.4	4.3	4.2	3.9	4.4
Exchange rate									
$/Euro	1.26	1.38	1.56	1.32	1.35	1.39	1.46	1.53	1.55

Contents

Sport: both competition and business

It is now only a few weeks before the start of the XXIX Olympic Games, the world's most important sporting event. Some 16,000 athletes will meet in China's capital with the hope of bathing in the glory of the winners' podium after years of effort and rigorous training. This is the big festival of sport, the only event capable of bringing together and uniting, if only for a few weeks, nearly all countries of the globe.

But sport cannot be seen only as a noble activity of body and spirit. Today, Baron de Coubertin's Olympic ideals involve multi-million-dollar contracts for television coverage rights, vast investment in infrastructures and major commercial interests. Modern sport, that arose with the Industrial Revolution to become a product of today's society, has evolved from an amateur activity into an economic sector that, in the developed countries, if we add together sports centres and clubs, facilities and equipment, materials and management, rights and marketing, involves between 3% and 5% of gross domestic product.

This Monthly Report gathers together some aspects of the relationship between sport and economic activity. For example, the debate about the cost and benefits of organizing the Olympic Games. Does it work out financially to act as the site of the Summer Games? To judge by the many candidates that every four years opt for selection (now including the city of Madrid) the reply must be in the affirmative. Following its experience in 1992, very few citizens of Barcelona would state otherwise. The people of Montreal, however, still look back bitterly at the financial costs left behind after the 1976 Games. The fact is that the city hosting the Games must provide the facilities for holding 30 different contests as well as lodging the huge group of participants, support personnel, journalists and tourists. All of this requires investment in pavilions, competition areas, lodging, highway and transportation improvements, among other factors. The spectacular Olympic stadium in Beijing, where they plan to hold the opening and closing ceremonies, cost 500 million dollars. Many people feel very positive about such investments as they generate new jobs and drive the country's economy, even if this increases government debt. Nevertheless, sooner or later, this increased debt must be faced and it is therefore fundamental that such investment not only provide benefits during the Games but subsequently can be made profitable.

All this money becomes involved because sport today has become a mass spectacle and this is largely due to the fact that the results are unpredictable. Will it be Nadal or Federer? Ferrari or MacLaren? Man Utd or Liverpool? This Monthly Report makes no attempt to predict the final allotment of Olympic medals but rather to point out that there is some relationship between success in sport and economic development, although here we must make some provisos. Other aspects dealt with in boxes are television coverage rights (who sells what to whom?) and the payment of the athletes (why should the winner take all?), two distinct questions but ones that again underline the close interdependence of sport and business. In spite of the fact that the dynamic of sporting activity often depends on the logic of the economy, sport still remains something apart, an individual or team activity that brings many people together, a symbol of health, a means of education and an instrument of social integration.

EXECUTIVE SUMMARY

World prospects becoming more complicated

Inflation joins problems dragging since start of year...

At the beginning of the year, *Monthly Report* drew attention to the double challenge facing the world economy in 2008: bringing the financial crisis to bay and overcoming the slowdown in the US economy. The upsets arising from the subprime mortgages, that broke out in the summer of 2007, and the scenario of a temporary crisis followed by a rapid recovery had to be finally ditched. What is more, the effects of the stagnation or recession expected in the United States on the rest of the world economy were considerable. The role to be played by the emerging countries in unfolding this scenario, as a counterweight to the decline in the United State, also turned out to be uncertain.

...making central bank measures more difficult.

Six months later, the world economic situation, far from getting back on track, has become still more complicated. Inflation, a risk that was given less importance in view of the challenges presented by the financial upsets and the worsening of the US economy, ascended into first place while the other two risks remain unresolved. An initial upward episode in oil last Autumn and the Winter of 2007 along with the performance in food and metals had set off some alarm bells. The prospect of a world slowdown, however, put the problem of inflation into second place.

Can economies handle more restrictive monetary policies?

What we were not counting on was an unstoppable rise in the per barrel price of oil and an unprecedented increase in food commodities. Inflation indices in practically all key economies have climbed to levels not seen for many years. While some metals have corrected the excesses noted in 2007, food and energy continue to move upward. The new highs for oil (an increase of 50% so far this year) and the difficulty of controlling its growth trend (apart from statements by the G-8 and meetings of producer and consumer countries) does not hold out much hope for any easing over the short term. In some economies, such as the Euro Area, underlying inflation (discounting volatile energy and food components) is beginning to rise, which suggests that the inflation problem may be beginning to spread to the whole economy.

This new situation has obliged the central banks to modify their views. The statements by Ben Bernanke, chairman of the Federal Reserve, and Jean-Claude Trichet, head of the European Central Bank, have explicitly mentioned the risk of inflation. The tone of their statements, which have been stronger than usual in recent times, have caused the markets to begin to anticipate a tightening of monetary policy on both sides of the Atlantic, a perception that has brought about interest rate increases for all terms.

Can the economies deal with a tighter monetary policy? Most of the European economies and the US economy have undergone higher than expected growth in the first half of this year. In Europe, economic activity is holding up well, largely thanks to exports to the dynamic emerging economies and to those that are exporters of commodities. The United States does not yet seem to have hit bottom in the real estate recession

while the weakness of household consumption remains disturbing. Rapid action by the central bank authorities in lowering interest rates and the application of a decidedly expansionist fiscal policy (such as issuing tax rebate cheques to households) seem to have halted the blows of the recession.

We still expect that in the second half of the year the economies will move within a stage of weakness both in the Euro Area and in the United States although the alarmist tone showing up in many economic reports some months back has now somewhat eased. This explains why the International Monetary Fund, for example, has revised upward its growth forecasts for the United States and the Euro Area for 2008. Another international body that recently expressed its views on this was the Organization for Economic Cooperation and Development (OECD). Its latest economic prospects confirm that in the industrialized countries the scenario will be one of weak growth and high inflation. The growth rate, however, will be better than foreseen some months ago but at the same time the increase in prices will be higher than expected. Specifically, the OECD foresees modest growth in the United States for 2008 (barely above 1%) with an outbreak of inflation to more than 3%. The Euro Area will grow more than the United States in 2008 (1.7%) but here again inflation will be higher going close to 3.5%. Looking farther ahead, in 2009 both economies will grow slightly less and inflation will ease.

What about the financial upsets? The OECD indicates that the worst may have already emerged. While the worst would be a system crisis, that is to say, a collapse of the banking system, this may be true. The Federal Reserve make it clear in March at the time of the BearStearns crisis that it would not allow such a thing to happen. But, after looking at the course of the stock markets in the developed countries in June, the continuing high risk premiums in the interbank market, the differentials on corporate bonds and the tightening of credit terms in retail markets, we could conclude that the end of the financial crisis was not near at hand. Furthermore, a rise in official interest rates will not help to normalize those upsets, at least at an early date. As we move into summer the big economic question of the moment will likely be how to fight inflation in a context of decreasing economic activity and a financial front still not entirely normal. This is the challenge.

While subprime mortgage crisis far from ended, OECD suggests worst is over...

Spain's economy: a triple shock

If we now look at the results for the first half-year in Spain's economy, the most notable feature of the present economic situation is the sharpness of the adjustment process. While it was expected that 2008 would be a year of lower growth, the speed of the slowdown has been well above that being forecast some months ago. Why is that so?

...but pressures in money markets, private sector borrowing and retail credit indicate tempest still not brought to bay.

The present course of Spain's economy is the result of the coming together of three impacts at the same time – the slump in the real estate sector, the hardening of borrowing terms and the rise of inflation. Any one of these bumps alone would have been able to end the long period of growth that began in the mid-Nineties. The three at once make for a very difficult situation.

Following growth of 3.8% in 2007, Spain's economy moved ahead by 2.7% in the first quarter of 2008, a period when some 75,000 jobs were lost, approximately twice the number of jobs lost in the fourth quarter of 2007. The unemployment rate rose sharply and consumer confidence began to collapse.

Spain's economy caught in three impacts at once: real estate slump, credit market and rise in commodity prices.

Economic activity indicators for second quarter suggest sharper slowdown.

Figures for the second quarter are still not available but it would not be hazardous to anticipate substantial worsening of the situation.

The most recent economic indicators confirm a loss of growth and a drop in key variables such as consumer confidence (with consumers seeing their situation as the worst since 1993), sales of consumer durables and housing construction. In this case, figures confirm the adjustment taking place in the housing sector. In the first quarter, approvals for new housing were down by 59.8% compared with the same period in 2007, although this is partly due to a distortion resulting from the coming into force of the new Building Code. Another early indicator of construction investment, cement consumption, was down 18.7% in May compared with the same month last year. Nevertheless, government tendering recovered strongly in the first quarter with an increase of 27.7% compared with the same period last year, which indicates increased activity in public works.

Prices and wages rising at rate of 5%.

The labour market is also indicating a weaker tone with a limited increase in registrations with Social Security and an increase in the number of unemployed as of May. We also note an increase in labour costs which are beginning to reflect the increase in inflation last year. Company labour costs rose by 5.1% in the first quarter compared with the same period last year, according to the National Institute of Statistics. This was the highest rise since the first quarter of 2003. Non-wage costs, made up mainly of contributions to Social Security, were up 4.5%.

Central government announces measures to ease effects of slowdown.

Nevertheless, the increase in nominal wages did not mean greater purchasing power due to the rise in inflation. By June, the year-on-year change in the consumer price index was above 5% which hurt the purchasing power of incomes and set off fears of an inflationary spiral. Protests and demonstrations by those groups most affected by the increased fuel costs (especially road transport) were a clear sign of the delicate situation now being seen in prices and company margins. Furthermore, the rise in oil prices has an effect on the foreign deficit and is interfering with its correction. In the first four months of the year the trade deficit rose by 16.3%. If the price of oil had held at the same level as in January-April 2007, the trade imbalance would have dropped by 3.3%.

The complicated combination of economic activity losing drive and rising inflation has become more real and it is difficult to see any improvement over the short term. What is to be done? The central government has announced a series of measures aimed at dealing with the impact of the slowdown by trying to generate confidence of both companies and consumers with an initial group of palliative moves of a fiscal character applying to both companies and households as well as pushing ahead certain reforms overdue. The Bank of Spain has also stepped in with the governor reminding one and all that its margin for manoeuvre on demand policy is limited and that this was a good time to improve the operation of markets that are still not fully efficient. The inflation threat, it noted, deserved special attention. There was the risk that price increases might be seen as being permanent which, along with wage revision practices quite unsuited to situations such as the present one, could end up generating a spiral of wage increases and higher inflation that could even further complicate the economic scene.

June 27, 2008

CHRONOLOGY

2007

June	**6**	**European Central Bank** raises official interest rate to 4.00%.
	14	Parliament approves new **Law on Safeguarding Competition** with creation of National Competition Commission.
	21	EU Council of Ministers approves **adoption of euro as national currency for Malta and Cyprus** as of January 1, 2008.
August	**9**	European Central Bank injects extraordinary liquidity into interbank market as early emergency move to ease pressures set off by **subprime mortgage crisis** in United States.
	13	US Federal Reserve reduces discount interest rate from 6.25% to 5.75% in order to relieve effects of **subprime mortgage crisis**.
September	**18**	**Federal Reserve** reduces reference rate to 4.75%.
October	**9**	Dow Jones index for **New York stock exchange** marks up all-time record (14,164.5), a rise of 13.7% compared with end of 2006.
	19	European Council agrees to adopt the **Treaty of Lisbon** in place of the European Constitution.
	31	**Federal Reserve** cuts reference rate to 4.50%.
November	**8**	IBEX 35 index for **Spanish stock market** marks up all-time high (15,945.7) with cumulative gains of 12.7% compared with end of December 2006.
December	**11**	**Federal Reserve** cuts reference rate to 4.25%.
	13	Central banks in United States, Euro Area, United Kingdom, Switzerland and Canada announce plan for **coordinated measures to relieve difficulties in monetary markets** brought about by financial upsets.

2008

January	**1**	Further enlargement of **Euro Area** with entry of Cyprus and Malta, making 15 member states.
	22	**Federal Reserve** reduces reference rate to 3.50%.
	30	**Federal Reserve** reduces reference rate to 3.00%.
March	**9**	Spanish Socialist Workers Party wins **general elections**.
	18	**Federal Reserve** cuts reference rate to 2.25%.
April	**18**	Government approves a **Plan for measures to stimulate the economy**.
	23	**Euro** exchange rate at 1.594 to dollar, highest figure since launching of single currency at beginning of 1999.
	30	**Federal Reserve** reduces reference rate to 2.00%.
June	**27**	One-month forward price of Brent quality **oil** rises to all-time high of 140.3 dollars a barrel.

AGENDA

July

- **2** Registrations with Social Security and registered unemployment (June).
- **3** Governing Council of European Central Bank.
- **4** Industrial production index (May).
- **11** CPI (June).
- **16** Harmonized CPI (HICP) for EU (June).
- **22** Central government revenues and spending (June).
- **23** Producer prices (June).
- **24** Labour Force Survey (2nd Quarter). Foreign trade (May).
- **25** US GDP (2nd Quarter).
- **31** Balance of payments (May). HICP flash estimated (July).

August

- **4** Registrations with Social Security and registered unemployment (July).
- **5** Federal Reserve Open Market Committee.
- **6** Industrial production index (June).
- **7** Governing Council of European Central Bank.
- **13** CPI (July).
- **14** Advance GDP (2nd Quarter). Harmonized CPI for EU (July).
- **21** Foreign trade (June).
- **25** Producer prices (July).
- **27** Quarterly National Accounts (2nd Quarter).
- **28** Advance HCPI (August).
- **29** Balance of payments (June). Central government revenues and spending (July).

INTERNATIONAL REVIEW

OECD foresees lower growth and higher inflation

OECD lowers growth forecast to 1.8% for 2008 and 1.7% for 2009.

In its Spring report, the Organization for Economic Cooperation and Development (OECD) lowered its growth forecasts for gross domestic product (GDP) in 2008 for all its member states as a whole to 1.8%. Recovery will not come early given that growth in 2009 was also revised downward to 1.7%. At the same time, price pressures are not weakening and inflation expected for 2008 and 2009 has been raised to 3.0%.

United States will not recover in 2009 but inflation to drop.

The risk of higher price rises and lower growth has increased due to higher energy costs, the tightening of credit, the rise in inflation expectations and the effects further upsets in financial markets could have on growth and prices. On top of these uncertainties we must add the growing influence of economies outside the OECD. According to the OECD, examples in one direction or another are the pressure these countries are putting on commodity prices and their capacity for vigorous growth and ability to act as a cushion in view of the economic slowdown by stimulating world demand.

Euro Area to grow 1.7% in 2008 and 1.4% in 2009.

The biggest downward revisions are related more to 2009 than 2008, especially in the United States, Italy, Spain and the United Kingdom. In the United States an advance of 1.2% is expected in 2008 with 1.1% in 2009 so that, according to the OECD, recovery will have to wait for later when the real estate correction is complete and credit terms go back to normal. As a result of lesser aggregate demand, the lower use of production capacity will mean that inflation will moderate significantly in 2009 while the weak dollar and the strength of exports will significantly ease the trade deficit putting it at 4.5% of GDP in 2009.

In the Euro Area in general, all forecasts have been revised downward, especially those for 2009. The GDP of the monetary union as a whole will rise by 1.7% in 2008 and drop to 1.4% in 2009. Tougher credit terms, greater difficulties for exports and a drop in residential investment, according to the OECD, will act as a brake on growth. Despite this scenario of weakness, inflation will not drop until the end of 2009 moving down toward 2%. By country, Germany shows lower growth prospects in 2008 and 2009 to 1.9% and 1.1% respectively. France is expecting advances of 1.8% and 1.5% in the same period while for Spain the forecast is down to 1.6% in 2008 and 1.1% in 2009 when the biggest downward revision is to take place. Among the large countries of the Euro Area, Italy will continue as that showing least growth in this period at 0.5% and 0.9% respectively.

Under macroeconomic policy, there are some major uncertainties. Globalization and structural reforms should keep adding to growth potential but the increase in energy prices and higher capital costs could work in the opposite direction. At the same time, while

OECD: ECONOMIC OUTLOOK (1)

	2005	2006	2007	2008	2009
GDP (2)					
United States	3.1	2.9	2.2	1.2	1.1
Japan	1.9	2.4	2.1	1.7	1.5
Germany	1.0	3.1	2.6	1.9	1.1
France	1.9	2.4	2.1	1.8	1.5
Italy	0.7	1.9	1.4	0.5	0.9
United Kingdom	1.8	2.9	3.0	1.8	1.4
Spain	3.6	3.9	3.8	1.6	1.1
Euro area	**1.7**	**2.9**	**2.6**	**1.7**	**1.4**
OECD	**2.7**	**3.1**	**2.7**	**1.8**	**1.7**
Inflation (3)					
United States	3.4	3.2	2.9	3.9	2.2
Japan	–0.6	0.2	0.1	0.9	0.4
Germany	1.9	1.8	2.3	2.9	3.1
France	1.9	1.9	1.6	3.5	2.4
Italy	2.2	2.2	2.0	3.6	2.1
United Kingdom	2.0	2.3	2.3	3.0	2.5
Spain	3.4	3.6	2.8	4.6	3.0
Euro area	**2.2**	**2.2**	**2.1**	**3.4**	**2.4**
OECD	**2.0**	**2.2**	**2.2**	**3.0**	**2.1**
Unemployment (4)					
United States	5.1	4.6	4.6	5.4	6.1
Japan	4.4	4.1	3.9	3.8	3.8
Germany	10.5	9.7	8.3	7.4	7.4
France	8.8	8.8	7.9	7.5	7.6
Italy	7.8	6.8	6.1	6.2	6.5
United Kingdom	4.8	5.5	5.4	5.5	5.8
Spain	9.2	8.5	8.3	9.7	10.7
Euro area	**8.8**	**8.2**	**7.4**	**7.2**	**7.4**
OECD	**6.5**	**6.0**	**5.6**	**5.7**	**6.0**
Current account balance (5)					
United States	–6.1	–6.2	–5.3	–5.0	–4.4
Japan	3.7	3.9	4.8	4.4	4.4
Germany	5.2	6.1	7.7	7.9	7.7
France	–0.9	–1.2	–1.2	–1.8	–1.6
Italy	–1.7	–2.7	–2.6	–2.4	–2.6
United Kingdom	–2.5	–3.9	–4.2	–3.3	–3.1
Spain	–7.4	–8.6	–10.1	–10.1	–9.8
Euro area	**0.4**	**0.2**	**0.2**	**0.1**	**0.0**
OECD	**–1.5**	**–1.7**	**–1.4**	**–1.3**	**–1.1**
World trade (6)	**7.5**	**9.6**	**7.1**	**6.3**	**6.6**

NOTES: (1) Starting hypothesis: a) Fiscal policies in force or announced will not change; b) Exchange rates will not change from level on May 13, 2008 (1 dollar = 104.44 yen = 0.640 euros); c) Closing date of publication and for including figures was May 23, 2008.
(2) All percentage change rates in real tems.
(3) Percentage change rates in GDP deflator.
(4) As percentage of labour force.
(5) As percentage of GDP.
(6) Arithmetical average of percentage annual growth rates of world imports and exports by volume.
SOURCE: Organization for Economic Cooperation and Development.

OECD: FINANCIAL OUTLOOK (1)

	2005	2006	2007	2008	2009
Government deficit (–) or surplus (+) (2)					
United States	–3.6	–2.6	–3.0	–5.5	–5.2
Japan	–6.7	–1.4	–2.4	–1.4	–2.2
Germany	–3.4	–1.6	0.0	–0.5	–0.2
France	–3.0	–2.4	–2.7	–3.0	–2.9
Italy	–4.4	–3.4	–1.9	–2.5	–2.7
United Kingdom	–3.5	–2.8	–3.0	–3.8	–3.7
Spain	1.0	1.8	2.2	0.7	–0.3
Euro area	**–2.6**	**–1.3**	**–0.6**	**–1.1**	**–1.2**
OECD	**–3.0**	**–1.5**	**–1.5**	**–2.5**	**–2.6**
Short-term interest rates (3)					
United States	3.5	5.2	5.3	2.7	3.1
Japan	0.0	0.2	0.7	0.8	0.7
United Kingdom	4.7	4.8	6.0	5.6	4.4
Euro area	**2.2**	**3.1**	**4.3**	**4.5**	**4.1**
Long-term interest rates (4)					
United States	4.3	4.8	4.6	3.9	4.4
Japan	1.4	1.7	1.7	1.7	2.1
Germany	3.4	3.8	4.2	4.2	4.3
France	3.4	3.8	4.3	4.2	4.3
Italy	3.6	4.0	4.5	4.5	4.6
United Kingdom	4.4	4.5	5.0	4.7	4.8
Spain	3.4	3.8	4.3	4.2	4.3
Euro area	**3.4**	**3.8**	**4.3**	**4.3**	**4.4**

NOTES: (1) Starting hypothesis: a) Fiscal policies in force or announced will not change; b) Exchange rates will not change from level on May 13, 2008 (1 dollar = 104.44 yen = 0.640 euros); c) Closing date of publication and for including figures was May 23, 2008.
(2) As percentage of GDP.
(3) 3-month interest rates on national money markets.
(4) Government bond interest rates on most representative issues in each country.
SOURCE: Organization for Economic Cooperation and Development.

Increasing energy cost, higher capital costs and financial uncertainty limiting growth.

expectations of more moderate inflation seem well founded, the trend in prices is making the central banks cautious. Finally, increased uncertainty in financial markets could be a drag on world growth. In this respect, it is essential to apply monetary policies that will ensure symmetrical responses to deal with periods of strong growth or tightening credit.

US GDP grows by 2.5% thanks to private consumption and exports.

With regard to public finances, the OECD believes that the temporary tax cuts in the United States are opportune. Nevertheless, their application in other OECD economies is more doubtful and current inflationary trends must be taken into account. In Japan, the state of the public finances leaves no room for tax changes.

United States: inflation arrives before recovery

Fears of an immediate recession are diminishing although the biggest risk to the economy (a continuation of the current period of low growth) has not been brought to bay and inflation has

now turned into the main hurdle to overcome. Most of this inflation is imported but this makes the monetary policy decisions of the Federal Reserve difficult. After a first revision, the gross domestic product (GDP) grew by 2.5% year-on-year, which was higher than expected. In year-on-year terms annualized, the increase was 0.9% thus showing better than the 0.6% seen in the previous period. The main contributors to growth (in equal parts) were private consumption, a key component that, while slowing down, is showing greater than expected strength, and the foreign sector because of the increase in exports and especially because of the drop in imports. Housing investment continued to be a burden on the economy while investment in capital goods and infrastructures was stagnant showing neither gains nor losses.

Returning to private consumption, in spite of the gradual nature of the slowdown, there are some clouds on the horizon. In May, the consumer confidence index of the Conference Board went down from 62.8 points to 57.2 points, a level similar to that in 1992, a year after the 1990-1991 recession. The extreme weakness of expectations, now at all-time lows, continues to give off the perception of the present situation with an index that has dropped from 114.3 points to the 74.4 points level in four months. Showing more vitality than expected, retail sales (excluding the fluctuating figures for cars and petrol consumption) were up 3.4% year-on-year in May which, discounting price variations, translates into an increase of 1.1%. This was a rise that, more than a change in trend, underlines the resistance of the US consumer to reduce spending levels.

Consumer confidence drops more sharply but retail sales move up.

UNITED STATES: MAIN ECONOMIC INDICATORS

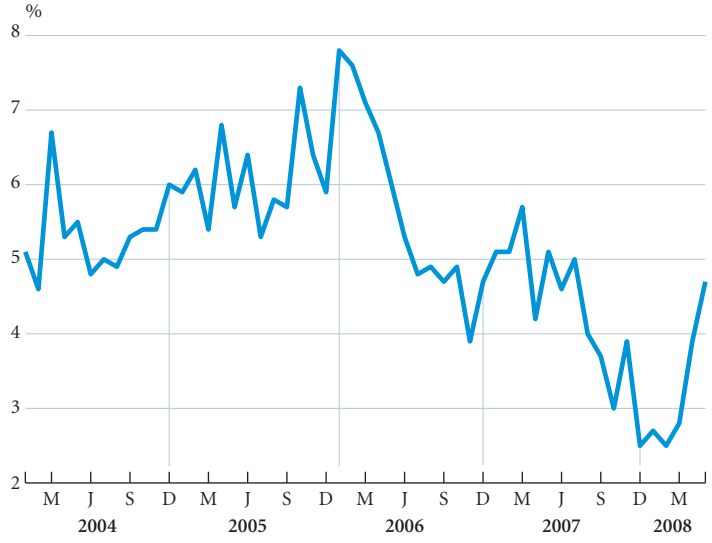
Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
Real GDP	2.9	2.2	1.9	2.8	2.5	2.5	–	...
Retail sales	5.8	4.0	4.0	3.9	4.7	3.0	3.0	2.5
Consumer confidence (1)	105.9	103.4	106.7	105.7	91.2	76.5	62.8	57.2
Industrial production	2.2	1.7	1.4	1.8	2.1	1.7	0.1	–0.1
Industrial activity index (ISM) (1)	53.1	51.1	53.0	51.3	49.6	49.2	48.6	49.6
Sales of single-family homes	–18.0	–26.8	–22.1	–27.3	–33.7	–33.3	–42.0	...
Unemployment rate (2)	4.6	4.6	4.5	4.7	4.8	4.9	5.0	5.5
Consumer prices	3.2	2.9	2.6	2.4	4.0	4.2	3.9	4.1
Trade balance (3)	–753.3	–700.3	–730.7	–701.4	–700.3	–695.6	–696.3	...
3-month interbank interest rate (1)	5.2	5.3	5.4	5.4	4.9	3.0	2.9	2.7
Nominal effective exchange rate (4)	82.5	77.9	79.3	77.0	73.3	72.0	70.5	70.8

NOTES: (1) Value.
(2) Percentage of labour force.
(3) Cumulative figure for 12 months in goods and services balance. Billion dollars.
(4) Change weighted for foreign trade movements. Higher values imply currency appreciation.
SOURCE: OECD, national statistical bodies and own calculations.

UNITED STATES: CONSUMPTION HOLDS UP BETTER THAN EXPECTED

Year-on-year change annualized in retail sales excluding cars and petrol (*)



NOTES: (*) Trend series.
SOURCE: Department of Commerce and own calculations.

Housing still fails to hit bottom with prices showing total loss of 18% from high levels.

A change in trend is still wanting in the housing sector. On the supply side, the bottom of the crisis has not yet arrived. There were 975,000 housing starts in May, showing a downward revision of figures over previous months. This indicator has thus piled up a loss of 57% compared with the high in January 2006. Pointing in the same direction, building permits that have been an early indicator of starts were down 36.3% year-on-year. On the demand side, the decreases were sharper. The variable that has most effect on the economy, because of the wealth effect, is the price of real estate. In March, the most representative index, the Case-Shiller figure, was down 1.0% from the month before. This meant a cumulative drop of 17.8% over the high in June 2006, a decrease that, if we add the rise in CPI, comes to 22.2%. In turn, existing home sales were down 17.5% year-on-year in March while new housing, which is always more volatile, was down by 42.0%.

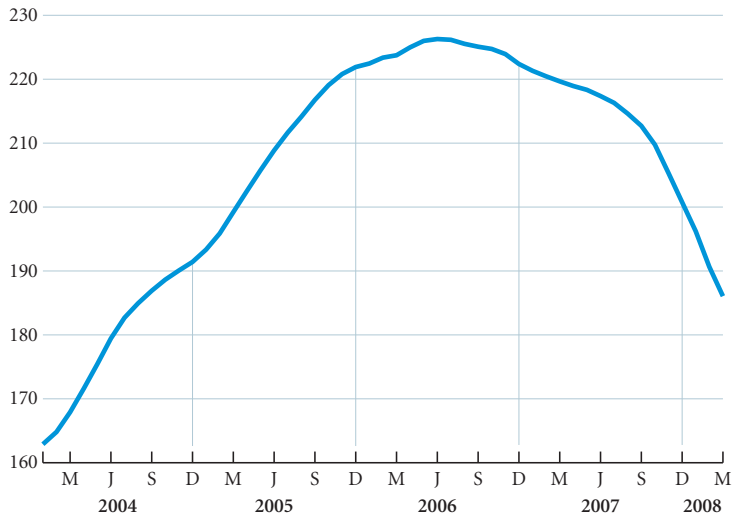
Labour market showing gradual drop and unemployment hits 5.5%.

The labour market, which also has a lot of influence on consumers, continued its downward trend. Some 49,000 jobs were lost in May putting the cumulative drop at 324,000 jobs since the end of 2007. As a result, in the total economy, non-farm jobs stood at a mere 0.2% above the same period last year. Along similar lines, the unemployment rate showed a drastic increase in May going from 5.0% to 5.5% of the labour force.

On the business side, the prospects of decreases are more moderate than in the case of consumers and the dominant risk is inflation. Confirming this is the trend in the May index for business activity published by the Institute for Supply Management. In the services sector the index went up from 50.9 points to 53.6 points. This was a level that, being above 50, indicates that optimistic responses won over those that were pessimistic. The manufacturing index also rose but just to 49.6 points,

UNITED STATES: FURTHER DECREASES IN REAL ESTATE PRICES

Case-Shiller index of housing prices. January 2000 = 100



SOURCE: Standard & Poor's and own calculations.

slightly below a balance. In both cases, the biggest dangers lie in price increases and, to a lesser extent, to the weakness in employment. The greatest strengths were still in new export orders which were close to 60 points in manufactures.

The manufacturing industry remains in a state of weakness. Since the first quarter of 2006, when the GDP was still growing close to potential, capital goods investment in real terms (ignoring price increases) had gained a mere 3.3% while investment in transportation equipment was down 21.8%, the biggest loss in a GDP component, except in the case of residential investment. Along the same lines, industrial production in May remained slack with a drop of 0.6% compared with the same period the year before. That the same month, industrial production of capital goods was also at a low ebb with a slim advance of 2.2% year-on-year. Filling out this picture of weakness in manufacturing industry, the utilization of production capacity continued to drop going to 79.4%, the lowest level in the past three years.

While the economy continues to gradually cool down, prices are showing a higher temperature. The May consumer price index (CPI) rose to a growth rate of 4.1% year-on-year. The underlying component (the general rate less energy and food) held at 2.3%, showing the little influence energy prices are having on other components of the CPI. Since the end of 2003, the energy prices component has appreciated by 75.6% and energy commodities by 111.9% whereas the underlying CPI has risen by a more than reasonable 10.6%. Nevertheless, while there has been no pressure on costs in the labour market, the persistence of expensive energy and food and the effects of Asian inflation could have important effects on the pocket of the average US citizen.

Business executives fear for prices and, to lesser extent, for employment while industry remains at low levels.

In turn, the trade balance in goods and services showed a deficit of 60.90 billion

Inflation hits 4.1% because of increased oil prices.

UNITED STATES: TRADE DEFICIT GETS CORRECTION IN SPITE OF OIL PRICES

Monthly figure for goods and services balance

SOURCE: Department of Comnmerce and own calculations.

Trade deficit puts off correction in spite of weak dollar.

dollars in April, an increase of 7.7% year-on-year. Net oil imports represent 57% of this imbalance. If we exclude the impact of higher cost oil, things are going somewhat better but to any excess given that, following some major drops, the non-oil trade deficit has been stagnant at above 26 billion dollars for five months. In April, exports remained strong with an increase of 19.2% year-on-year but the increase in imports, largely due to price increases with growth of 13.5%, made it difficult to correct a trade deficit that has not been able to benefit from a weak dollar.

Japan: hoping for good winds from the rest of Asia

Japan's GDP grows by 1.3% with improvement in capital goods investment.

The GDP for the first quarter of 2008 was revised upward from an increase of 1.1% to 1.3% year-on-year, a robust 4.0% compared with the last quarter of 2007, in annual terms. The main matter of interest was the upward correction of investment in capital goods which had been the component causing the most disappointment before the revision. This came on top of the relatively good state of private consumption and exports in the first quarter. As part of the general situation, dominated by rising inflation in the emerging economies and the worsening of the relation between growth and inflation in the developed economies, Japan is an exception on the positive side. Its weaknesses continue to lie in the poor state of domestic demand and its dependence on foreign sales.

In the real estate market, housing starts in April continued the recovery of previous months with a year-on-year decrease of 8.7% as against 15.6% in March. Nevertheless, on the demand side, sales in the Tokyo area were down 22.7% year-on-year in May which meant two consecutive years of decreases with prices

JAPAN: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
Real GDP	2.4	2.0	1.7	1.8	1.4	1.3	–	…
Industrial production	4.2	2.9	2.4	3.1	2.7	2.5	0.7	…
Tankan company Index (1)	22.5	22.0	23.0	23.0	19.0	11.0	–	…
Housing construction	4.5	–17.2	–2.8	–36.9	–27.1	–8.9	–8.7	…
Unemployment rate (2)	4.1	3.9	3.8	3.8	3.8	3.8	4.0	…
Consumer prices	0.2	0.1	–0.1	–0.1	0.5	1.0	0.8	…
Trade balance (3)	9.4	12.5	11.1	12.3	12.5	11.7	11.3	…
3-month interbank interest rate (1)	0.3	0.7	0.7	0.8	0.9	0.8	0.8	0.8
Nominal effective exchange rate (4)	81.1	77.1	75.7	76.9	78.4	83.4	83.9	83.0

NOTES: (1) Value.
(2) Percentage of labour force.
(3) Cumulative balance for 12 months. Billion yen.
(4) Change weighted for foreign trade movements. Higher values imply currency appreciation. Average in 2000 = 100.
SOURCE: OECD, national statistical bodies and own calculations.

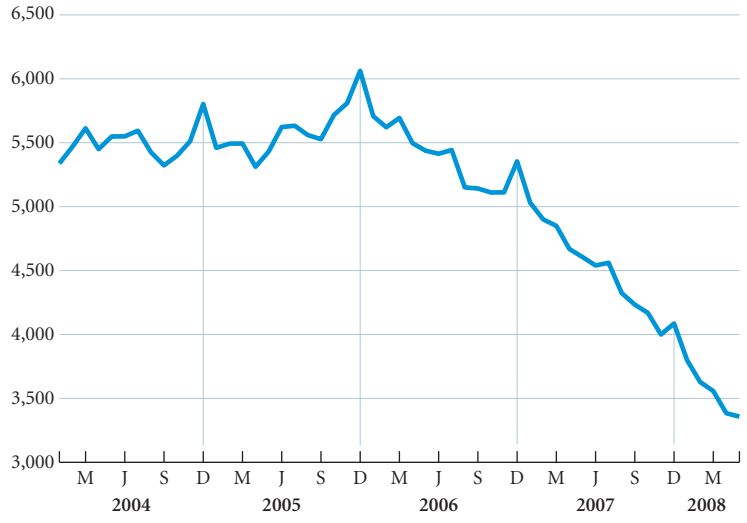
stagnant in that period after having previously shown an upward trend.

In addition, we should point out that, in spite of the slight improvement in the national accounts, the prospects for capital goods investment are not bright. Machinery orders, a good early indicator of investment demand, slipped down by 2.1% year-on-year in April although

Construction recovers but real estate market remains weak.

JAPAN: HOUSING STAGNANT BUT PRICES RISING

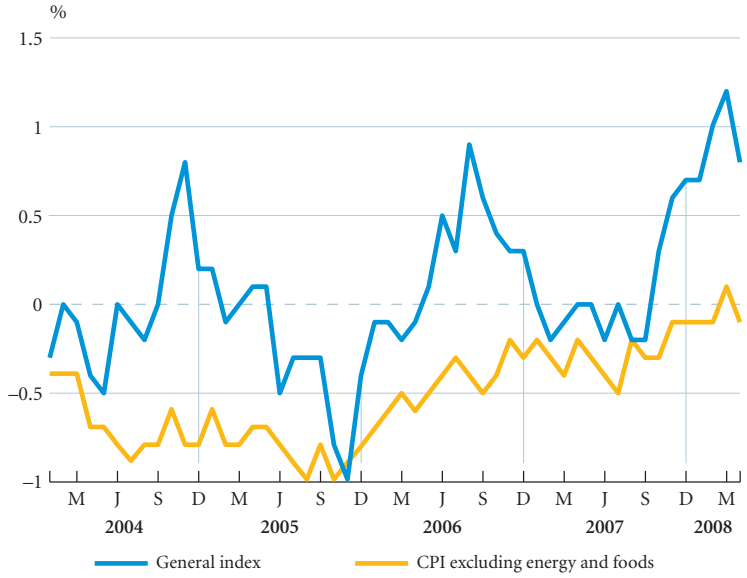
Monthly housing sales in Tokyo area



NOTES: Trend series.
SOURCE: Japan Real Estate Institute and own calculations.

JAPAN: MORE THAN MODERATE INFLATION

Year-on-year change in consumer price index



SOURCE: Japanese Ministry of Communications, National Statistics Office and own calculations.

Prices excluding energy and food down 0.1% while unemployment hits 4%.

there was a slight recovery of orders aimed at the export industry. Confirming this slack situation, industrial production in the same period grew by a slim 0.7% year-on-year.

On the inflation front, the April CPI rose by 0.8% year-on-year, showing some moderation (if this were possible) of the 1.2% figure for the month before. The traditionally followed index that excludes fresh foods was also down showing an increase of 0.9%. Nevertheless, the underlying inflation index (the general index excluding energy and food) returned to negative ground with a drop of 0.1% year-on-year that made Japan an exception to the general increase in inflation. In turn, the unemployment rate rose from 3.8% of the labour force to 4.0% in April while the trade balance showed a cumulative surplus for the 12 months ending April of 11,300 billion yen. This was a slight drop due to a slowdown in exports.

Brazil growing by 5.8% as result of private consumption and investment but foreign sector getting weaker.

Brazil: growth with risk of inflation

Brazil's GDP continued its robust progress with an increase of 5.8% year-on-year in the first quarter, above the average in recent years. The main player in economic activity was domestic demand. Private consumption rose by 7.1% while investment, which held up well, rose by 15.2%. Nevertheless, the foreign sector (quite strong until very recently) continued to show a poor profile because of the weakness of exports, which in the first quarter reported a drop of 2.1% year-on-year. Imports, however, were up by a considerable 18.9%. The other aspect of growth was public consumption, which in the first quarter went up to an increase of 5.2% compared with the year before, a rate nearly twice the norm in recent times.

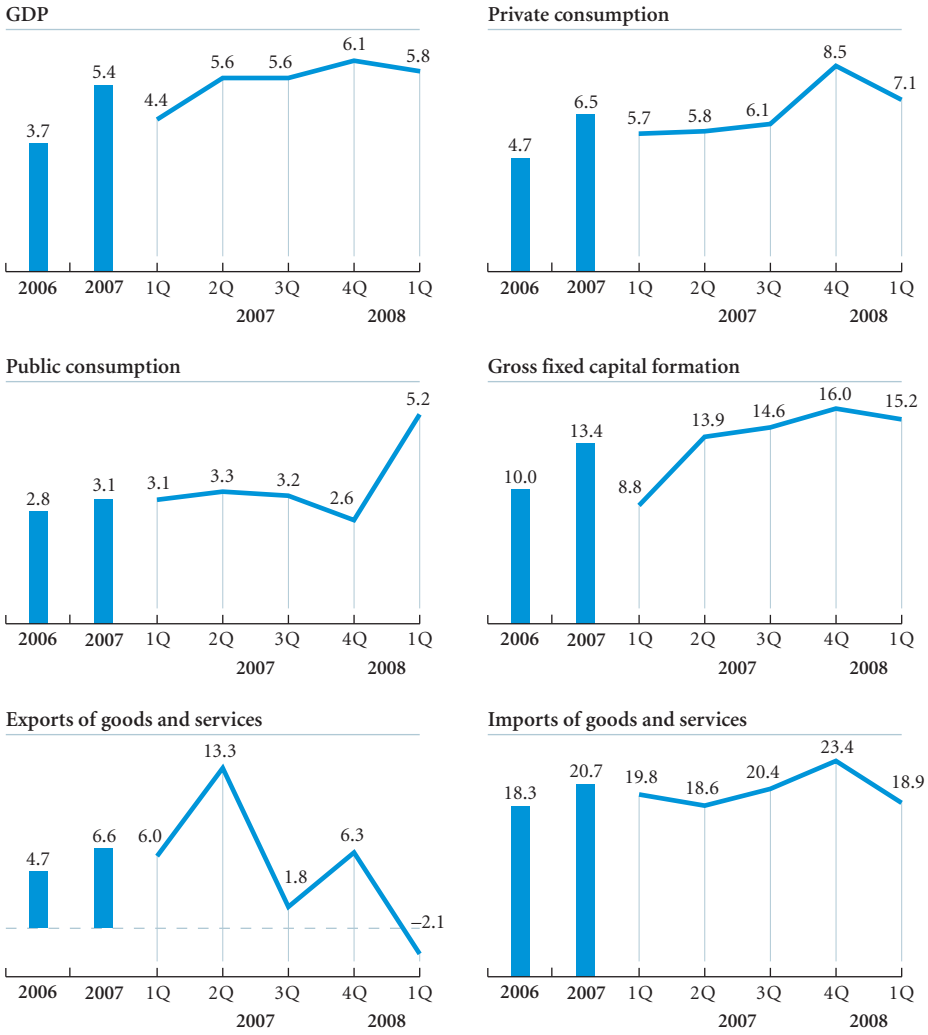
Among latest economic activity indicators, industrial production in April

recovered the levels at the beginning of the year with a rise of 10.1% year-on-year. In turn, industrial production of capital goods continued two-digit growth to record a gain of 30.0% year-on-year, which confirms the present increase in private investment. Utilization of production capacity has ended up reflecting the strong pace of industry and in March rose to 82.9%, a high level that, nevertheless, was below the figures most predominant in the second half of 2007. On the demand side, retail sales grew by 8.7% year-on-year in March, slightly below the robust level in recent months. Car sales, in spite of a slight dip in May, continued to show a picture of strength with a level in the first five months of 2008 38.3% higher than that for the same period last year.

Industry continues to move ahead strongly, especially in capital goods.

TREND IN BRAZIL'S GDP BY COMPONENT

Percentage year-on-year change in real terms



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

BRAZIL: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
Real GDP	3.7	5.4	5.6	5.6	6.1	5.8	–	…
Industrial production	2.8	6.0	5.8	6.3	7.9	6.4	10.1	…
Unemployment rate São Paulo (*)	15.9	15.0	15.6	15.0	14.0	13.8	14.2	…
Consumer prices	4.2	3.6	3.3	4.0	4.3	4.6	5.0	5.6
Trade balance (**)	46.3	40.0	47.4	43.1	40.0	34.1	31.7	31.9
Central bank SELIC rate (***)	15.1	12.0	12.3	11.4	11.3	11.3	11.8	11.8
Reales to dollar	2.2	1.9	2.0	1.9	1.8	1.7	1.7	1.6

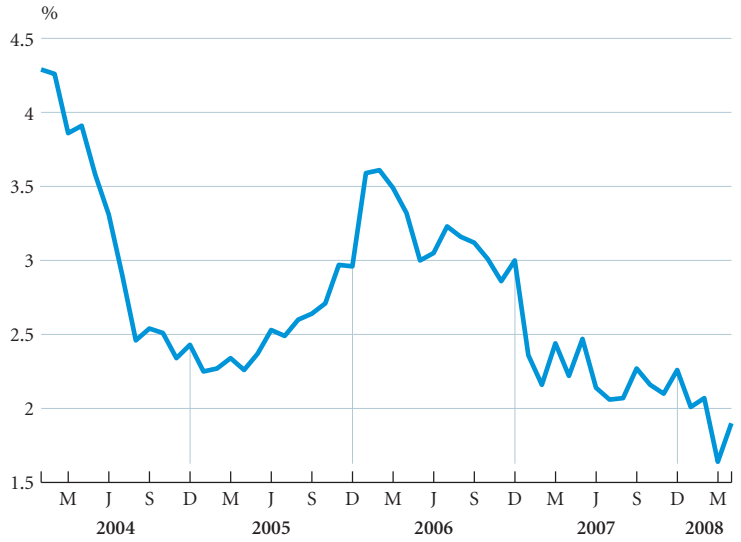
NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion dollars.
(***) Value of central bank rate from the Sistema Especial de Liquidação e Custodia (SELIC).
SOURCE: Brazilian Institute of Geography and Statistics, Central Bank of Brazil and own calculations.

Inflation rises to 5.8% and tax and monetary measures will have difficulty getting it below 5% in 2008.

The strength of domestic demand, along with the world increases in energy and food prices, is bringing about an incipient return of inflationary pressures. In May the CPI rose by 5.6% year-on-year, thus sharpening the upward trend that began in June 2007. The bad news comes on the side of wholesale prices which were up 15.4% and suggest bigger price increases that will make it difficult to go back to levels of 5% at the end of 2008. In order to ease the increase in prices, the central bank raised the SELIC reference rate to 11.8% in April. The government is also trying to apply fiscal austerity measures

BRAZIL: PUBLIC DEFICIT DOWN IN SPITE OF VERY HIGH INTEREST PAYMENTS

Public deficit in past 12 months in terms of GDP



SOURCE: Instituto da Pesquisa Economica Aplicada and own calculations.

but, as shown under public consumption in the national accounts, these come more on the side of higher revenues than lower spending, which limits their anti-inflationary effects.

In this respect, in the past 12 months ending in April the fiscal surplus before public debt interest was 4.2% of GDP, thanks to revenues resulting from the strong economic activity, repatriation of profits obtained from abroad and delays in public investment. Help has also come from credit rating agencies (Fitch and Standard Poor's) which raised ratings for Brazilian government bonds in May. This brought decreases in interest rates thus helping to reduce the total public deficit which, for the 12 months ending in April, stood at 6.1% of GDP.

In turn, unemployment continued to rise in spite of the strength of demand and the increase in prices. In April, the unemployment rate in the São Paulo district reached 14.2% of the labour force. In the foreign sector, the appreciation of the real, brought about by the higher rating of foreign debt, contributed to the rapid worsening of the trade deficit, which in the past 12 months ending in May amounted to 31.92 billion dollars, some 15.75 billion dollars less than in the same period last year.

Argentina: long period of growth in grip of prices

The growth of Argentina's economy is losing strength but even so the GDP in the first quarter of 2008 grew by a notable 8.4% year-on-year. Economic activity continues to be dominated by domestic demand with private consumption that, in keeping with the pattern for the economy as a whole, has slowed to the rate of 8.2%. Definitely following a more upward move, investment showed sharper growth going up by 20.5%, thus contributing to half of all economic growth in absolute terms. The foreign sector continued to cut back the strength of growth, a quarter of the total, with imports full steam ahead and exports sliding down.

The big danger for Argentina's economy continues to be inflation. The May CPI continued to move up from already high levels to growth of 9.1% year-on-year. This is a high figure that, nevertheless, may be underestimating real inflation. Prospects are not good seeing that, first of all, wholesale prices for national goods rose by 14.2% while imported goods were up a more striking 19.6%. Secondly, the conflict with farmers over export taxes is creating bottlenecks that could end up causing further price increases.

Recent demand indicators confirm the inflation problem to some extent but without breaking the continuity of the growth cycle. Retail sales in the Buenos Aires region were up by 17.8% year-on-year in April and for department stores as a whole they rose by 32.3%, which indicates a clear slowdown in growth rates which were blown up by price increases. Car sales in the past 12 months ending in May were down although they showed respectable growth of 17.5% year-on-year to stand 13% below the all-time high. On the supply side, industrial production also lost some of the increase begun back in October to show a rise of 6.7% year-on-year.

By sector, the automotive industry recovered with strength regained following a brief lull to show an increase of 33.7% year-on-year in April. The mining industry, both metal and non-metal, also showed growth of more than

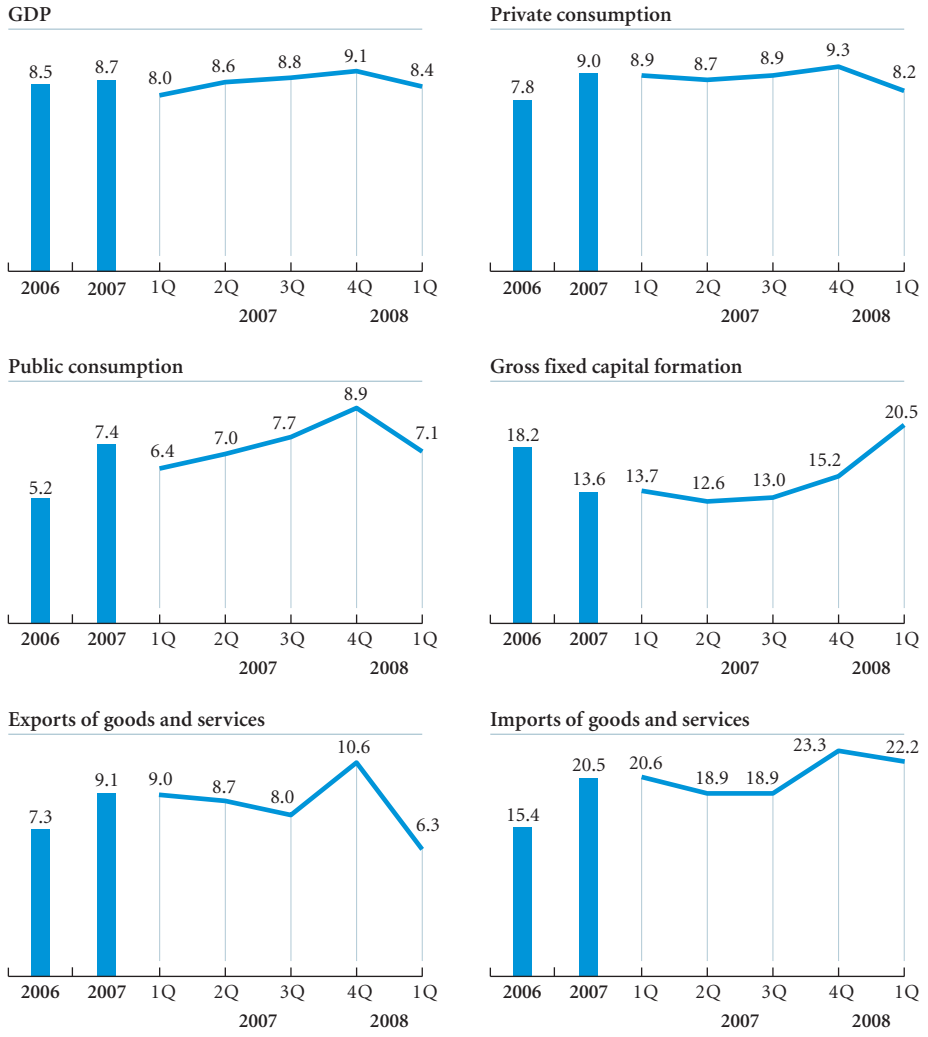
Trade surplus dropping rapidly.

Argentina grows by 8.4%, thanks to domestic demand, while foreign sector keeps dropping.

Inflation above 9% and still going up.

TREND IN ARGENTINE GDP BY COMPONENT

Percentage year-on-year change in real terms



SOURCE: National Institute of Statistics and Census, Republic of Argentina (INDEC) and own calculations.

Retail consumption and industrial production slowing down but construction recovering.

20% while the chemical and food industries continued to drop. In April, the Synthetic Indicator for Construction Activity sharpened the rise seen in previous months to show an increase of 22.7% while the Industrial Activity Indicator moved up by a more discreet 8.5%.

In the labour market, the strength of demand did not stop unemployment in the first quarter from rising to 8.4% of the labour force. In turn, the trade surplus for 12 months ending in April was down to 11.7 billion dollars whereas interest on the foreign debt continued to rise.

ARGENTINA: INFLATION MOVING UP

Year-on-year change in CPI

SOURCE: INDEC and own calculations.

ARGENTINA: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
Real GDP	8.5	8.7	8.6	8.8	9.1	8.4	–	…
Industrial production	7.7	5.6	4.7	2.7	8.6	8.1	6.7	…
Unemployment rate (*)	10.2	8.5	8.5	8.1	7.5	8.4	–	…
Consumer prices	10.9	8.8	8.8	8.6	8.5	8.5	8.9	9.1
Trade balance (**)	12.3	11.1	11.5	10.4	11.1	12.0	11.7	…
3-month interbank interest rate (***)	9.9	11.3	9.4	12.6	13.7	10.7	11.1	15.1
Pesos to dollar	3.1	3.1	3.1	3.1	3.1	3.2	3.2	3.1

NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion dollars.
(***) Value.
SOURCE: National Institute of Statistics and Census, Republic of Argentina (INDEC) and own calculations.

Commodities: oil goes to new highs

Month after month, all-time high after all-time high, oil continues to surprise. At the beginning of June, oil broke with a path of some downward correction shot up in barely two sessions from 123 dollars a barrel (one-month forward price for Brent quality) to 136 dollars. At the session on June 6, the rise was 9% in a single day, the highest recorded in more than a decade. Later on, the price of oil swung considerably but always within a narrow range, between 134-137 dollars a

Unemployment rate at 8.4% and trade surplus dropping.

Oil breaks barrier of 130 dollars a barrel and stays in that range.

barrel. At the end of June, however, the price went to levels of the order of 140 dollars.

Apart from the atypical session on June 6, said to be sparked by certain Israeli statements about a hypothetical war with Iran, the persistent maintenance of oil at levels above 130 dollars a barrel is due to an unfortunate combination of still strong world demand and supply having difficulty to expand. While four key countries of the Organization of Petroleum Exporting Countries (OPEC), including the leading world producer, Saudi Arabia, reached their highest production level for six years in May, inventories of oil and distilled products stand at low levels. It should be remembered that inventories normally recover in the second quarter due to the end of the winter season. This has not happened in the current year.

Lack of additional production capacity while demand remains strong.

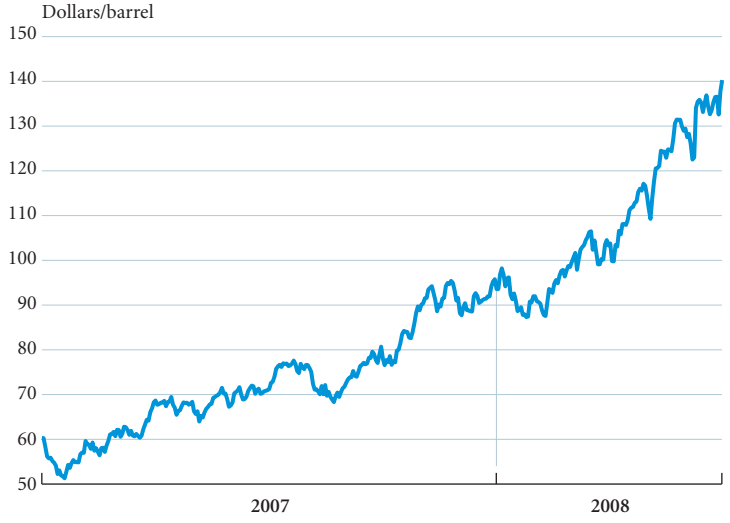
The narrow gap between supply and demand reduces the margin available for correcting the situation. In spite of the joint meeting of producer and consumer countries held in the Saudi Arabian city of Jeddah on June 22, Saudi Arabia merely repeated its willingness to increase production by another 550,000 barrels as of July, a figure considered insufficient to turn around the upward trend in prices, especially taking into account that production problems in Nigeria could end up counterbalancing the extra efforts by Saudi Arabia.

Metals show correction while food commodities continue upward.

Other commodities are following uneven lines. In overall terms, according to *The Economist* commodities index, commodities have grown by around 22% so far in 2008, a result of the sharp rise in food commodities which showed an increase of 28% during the year. By contrast, industrial commodities, especially metals, have risen at a more moderate rate (13% in the latter case). These trends continued in June. Food commodities showed an increase of 10% while metals were down by 3%.

NEW HIGHS: ARE THEY JUST FOR NOW?

Per barrel one-month forward price for Brent quality oil



SOURCE: Thomson Financial Datastream.

Wealth and Olympic gold

According to legend, the first Olympic Games were held in Ancient Greece in 775 B.C. and the first champion was Pelops. The games were held at intervals of four years and only freemen who spoke Greek could participate. Competitions were between individuals and not between countries. The year 1896 saw the beginning of the Modern Era games and since then the competitors have essentially been countries. Does the size and prosperity of a country have any relation to its Olympic success? Sport is not a basic necessity of the individual and usually is more developed in advanced societies. Taking part in international sporting events requires an investment in means and human resources that a less developed society might prefer to devote to more immediate needs. We may therefore expect that success in sports might be gained as the result of enjoying a higher economic level. On the other hand, Olympic success is often taken as a measure of the good state of a country. In addition, it would seem logical to expect that, with a similar per capita income, a large country in terms of population would be able to win more Olympic medals than a small one.

Following this reasoning, gross domestic product (GDP) would be a good indication of the number of medals a country would win in the Olympic Games. A rich, highly populated country such as the United States, would always get to the winners' podium more often than a poor, sparsely populated one such as Albania or Gambia. In 1997, Bernard and Busse[1] made forecasts about the medals that would be won in Sydney 2000 and showed that the GDP had a greater influence than population.

Nevertheless, the correspondence between GDP and Olympic medals is by no means perfect, although there are various reasons that largely account for the deviations observed. To simplify the calculations we may speak of medal points. An Olympic gold would thus be the equivalent of three points, a silver would equal two points and a bronze just one point.

A logical deviation from any correspondence between GDP and Olympic medals would include boycotts that inevitably distort the results. The clearest deviation from the GDP/Olympic success pattern, however, is the site effect. Being the host of the Olympic Games stimulates efforts to play a bigger than normal role. For example, Greece that organized the 2004 Games won 1.9% of all the medals whereas its historic average was 0.8%. In 1992, Spain won 3.4% of the medal points whereas its average in the previous 30 years had been 1.5%.

At the country level, we may state that the trend in Olympic results reflects the development tendency of economies. Since the days of Baron Coubertin, the Olympic club has thus become less and less more exclusive. In 1896 in Athens only 12 countries won medals whereas at Athens 2004 there were 74 countries winning medals. Since then, the traditionally rich countries (Western Europe, United States, Canada, Japan, Australia, New Zealand and Israel) have seen how their proportion of total medal points has been slipping. It went from 94.3% at the 1900 Paris games to 46.7% in 2004. Nevertheless, this decline was not uniform. First of all, the long downward trend disappeared as of the games in Mexico City in 1968. Secondly, there are sharp differences between countries. Continental Europe suffered a serious decline between 1920 and 1968 when its proportion of all medals won went from 50% to 15%. In the same period, the United States maintained a level of more

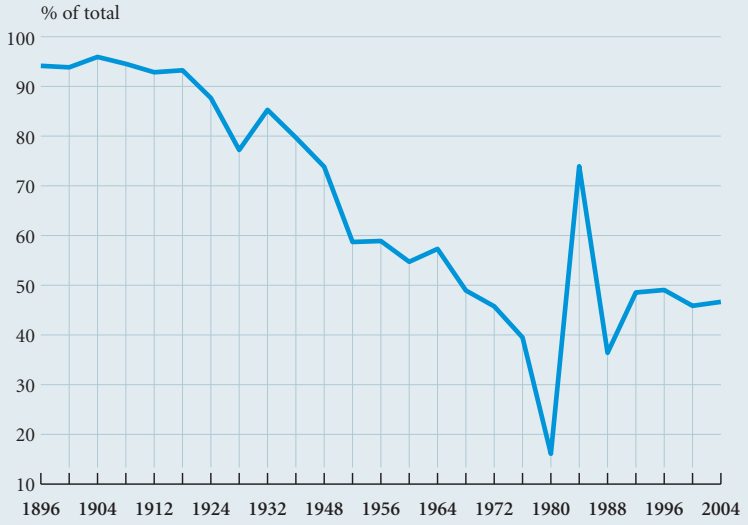
(1) Andrew B. Bernard, Meagan R. Busse, «Who wins the Olympic Games: Economic Resources and Medal Totals». August 28, 2000.

than 20% without showing downward trends. Since then, Continental Europe's quota has risen above 19% whereas that of the United States was cut in half going below 11% in a decline that does not seem to have yet ended. These performances do not correspond with the trend in the GDP shares held by Europe and United States out of the world total.

A remarkable trend, consistent with a strong GDP/Olympic success ratio, is the vigorous arrival of Oriental Asia, apart from Japan, as of the end of the Seventies. If we distinguish between China and the other countries of the region, this ratio holds up in both cases. The countries of Latin America, although in a much more paced manner and with less overall weight, have seen their quota of medals and their GDP quota move upward over the past 20 years. In the case of Africa, the drop in Olympic success corresponds with the difficulties of that continent in joining in the dynamic of economic growth.

ARE RICH COUNTRIES ON THE DECLINE?

Medal points won by developed countries (*)



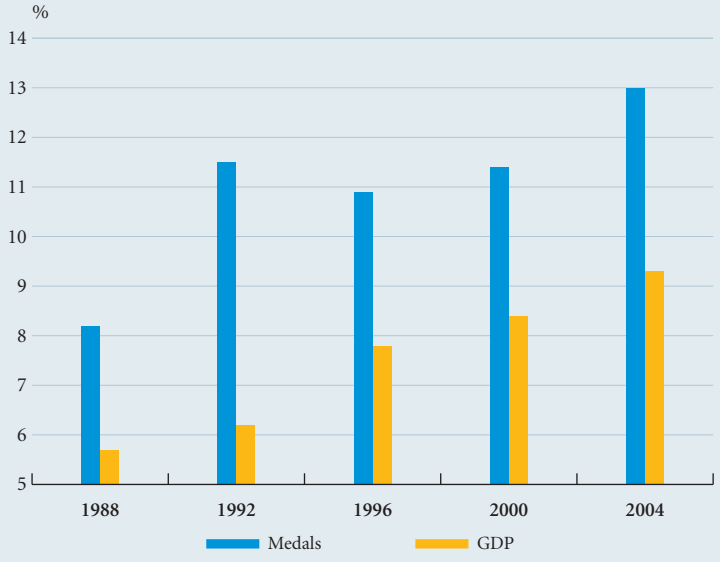
NOTES: (*) United States, Canada, Western Europe, Japan, Australia, New Zealand and Israel.
SOURCE: International Olympic Committee and own calculations.

The failures observed in the GDP/Olympic success ratio may be largely attributed to factors of a cultural, political or even religious nature. Here we may speak of a propensity to a sport as this varies according to geographical area. While among the traditionally rich countries and the Far East we see no big differences, in North Africa and the rest of Asia, including the Indian giant, the economic and population variables would make us expect bigger Olympic harvests than those garnered in the past five Games. Perhaps we could put this down to a lower involvement in sport in those regions.

On the other side of the coin are the former Communist countries which have had much more participation in Olympic glory than their population and GDP would suggest. This intense interest in sport came as part of the propaganda effort of these countries in Iron Curtain times but the fall of the Berlin Wall scarcely reduced their competitive capacity given that the structures then established have been well maintained.

FAR EAST BURSTS INTO GLOBAL WORLD

Quota of medals and nominal GDP quota in Far East, excluding Japan, in terms of world total



SOURCE: International Monetary Fund, Olympic Committee and own calculations.

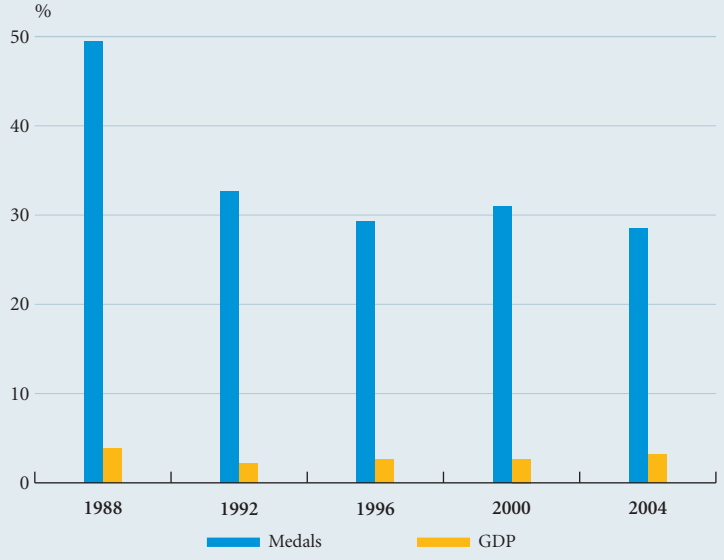
These countries reached a peak at the Montreal Games in 1976 when they picked up 57% of the medals. Their quota later dropped to 33% in Barcelona and has since stabilized just below 30%, a high level that indicates that government policies have established a strong institutional momentum or that among the general population there exists a great degree of interest in sports. Other investigations[(2)] that have looked at cultural and demographic factors conclude that an early marrying age and ethnic diversity have a positive contribution on Olympic success, the former perhaps raising a sense of responsibility and the latter helping to find highly specialized individuals.

To sum up, the imperfect relationship between the economic potential of a country and its Olympic successes should not make us forget that, after all, it is individuals who are competing and pushing themselves to the limit on the track or in the stadium, just as in the Classical Olympics, only now they speak many more languages than Greek and that inevitably standing behind them are their countries.

(2) Alexander Matros, Soiliou Daw Namoro, «Economic Incentives of the Olympic Games». January 21, 2004.

MANY MEDALS STILL GOING TO EASTERN EUROPE

Quota of medals and quota of nominal GDP of former Communist countries in terms of world total



SOURCE: International Monetary Fund, Olympic Committee and own calculations.

EUROPEAN UNION

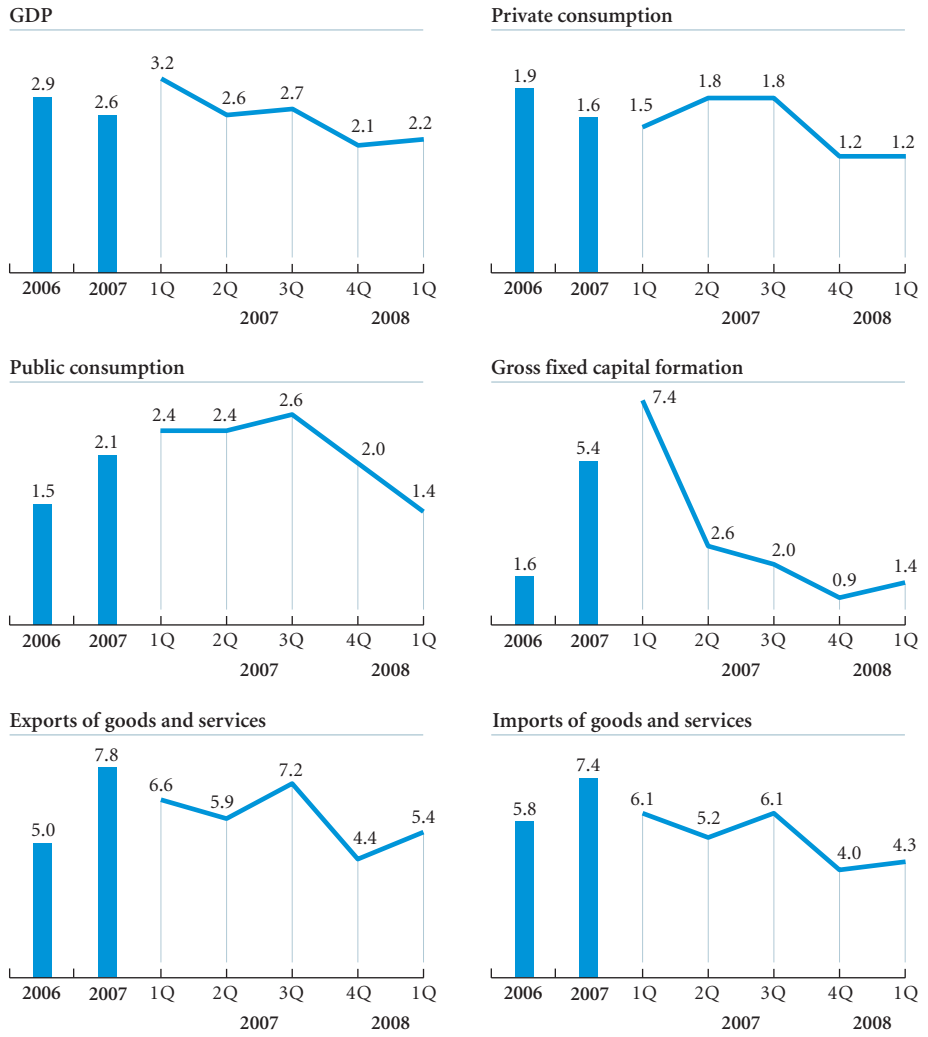
Euro Area: inflation sets off alarm bells

Halfway through 2008, it may be worth weighing where the Euro Area economy is headed. Just a few months ago at the start of 2008, the scenario showed that attention should be paid to what was felt to be a rapid slowdown in economic activity with other fronts such as

Economic activity holds up in Euro Area in first quarter thanks to consumption and investment.

TREND IN EURO AREA GDP BY COMPONENT

Percentage year-on-year change



SOURCE: Eurostat and own calculations.

EURO AREA: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
GDP	2.9	2.6	2.6	2.7	2.1	2.2	–	…
Retail sales	1.6	0.9	1.0	1.4	–0.4	–0.1	–2.7	…
Consumer confidence (*)	–9.1	–4.9	–2.6	–3.9	–7.7	–11.9	–12.4	–14.7
Industrial production	4.0	3.5	2.9	4.0	3.1	2.7	3.9	…
Economic sentiment indicator (*)	106.3	108.4	111.0	108.7	104.3	100.5	97.1	97.1
Unemployment rate (**)	8.3	7.4	7.5	7.4	7.2	7.1	7.1	…
Consumer prices	2.2	2.1	1.9	1.9	2.9	3.4	3.3	3.7
Trade balance (***)	–10.4	20.1	15.6	31.4	34.3	23.5	17.9	…
3-month Euribor interest rate	3.1	4.3	4.1	4.5	4.7	4.5	4.7	4.9
Nominal effective euro exchange rate	103.6	107.7	107.1	107.7	110.6	112.8	116.0	115.5

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

Second-quarter slowdown still contained.

inflation of less concern. Only halfway into the year the situation has completely turned around. Now we know that there is a slowdown but one that is very gradual, thus reinforcing the idea that the Euro Area is benefiting from notable growth momentum while, on the other hand, inflation is serious.

Most recent figures for national accounting in the first quarter show an economy maintaining its growth rate (2.2% year-on-year, slightly higher than in the fourth quarter of 2007) largely thanks to two components, consumption and investment. With regard to domestic demand, the maintenance of the private consumption rate and the increase in investment makes it possible to more than compensate the drop in public consumption. The foreign sector, on the other hand, while contributing positive growth to the change in gross domestic product (GDP), is doing so at a rate two-thirds below the first quarter. As against a contribution of six decimals in the fourth quarter, the contribution of foreign demand amounted to just two decimals in the first quarter.

The situation was only slightly different in the second quarter. While it is true that the rate of economic activity will end up below the first three months of the year, the various indicators suggest that the slowdown trend is not very strong. The economic sentiment indicator, that tries to gauge the level of activity overall, was down to 97.1 points in April but late held at this level in May. In spite of the fact that it again moved down in June, both maintenance of the level for two consecutive months and the gradualness of the decrease confirm that the European economy is showing a notable fund of resistance.

Inflation emerging as worst problem of current economic situation...

On the demand side, this is due to the fact that investment is holding up at an appreciable rate. On the supply side, the

indicator reflecting the good state of economic activity is industrial production. Another front showing positive developments is the foreign sector. In April, the trade surplus as a cumulative figure for 12 months stood at 17.9 billion euros, showing no change over March.

In spite of this overall positive situation, this was not enough to bring about reductions in the unemployment rate since last February, which partly explains the continued weakness in consumption indicators in the second quarter. In any case, if the economic indicators are taken together, we can expect that the three months April-June will end up showing a very little drop in economic activity.

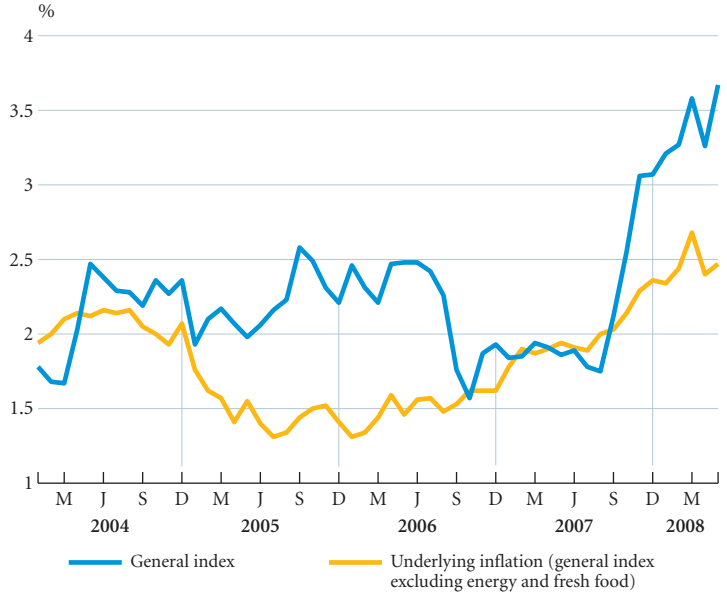
In the face of this reality (economic activity is holding up better than expected a few months ago), there appears another that is less satisfying. The growth rate in consumer prices has practically doubled in one year. In May 2007 the harmonized consumer price index (HCPI) was growing at 1.9% year-on-year. In May one year later the rate of increase was 3.7% year-on-year. This figure is doubly negative both because of the level reached and its make-up. To start off, it is far from the medium-term objective of the European Central Bank (2.0%) which is indicative of an abnormally high level of inflation. In fact, this is the highest figure in the practical 10-year existence of the single currency.

But it is also the fact that this rate arises not only from the poor performance of the volatile components but also from the non-volatile components. The sharp increase in energy and unprocessed food costs largely explains the rise in inflation. But, even if we discount these headings,

...given that it is affecting both energy and fresh foods and other less volatile headings.

ENERGY AND FOODS ARE NOT ONLY SOURCES OF INFLATION IN EURO AREA

Year-on-year change in CPI



SOURCE: Eurostat.

German economy maintaining overall positive tone.

resulting inflation suggests an upward trend. This is a thus a situation that is hard to correct and one that today has become the prime concern of European economic policy. The sensitiveness of the situation is to be seen in the various demonstrations taking place in different parts of Europe demanding compensation for the sharp increase in fuels and other products.

Germany: economy holding up thanks to prices

If we take all available indicators it would be difficult to conclude that the German economy was suffering badly from the world economic shock. Consumption, a relatively weak component of Germany's present economic situation, is holding up in the second quarter, as indicated by the year-on-year decrease of only 1.0% in April (in March the drop was 7% year-on-year). Investment is showing an even better state.

Both domestic demand and foreign demand seem to be riding out subprime storm.

On the supply side, the battery of positive figures is repeated. Industrial production increased in April in contrast to the forecasts (year-on-year increase of 4.8%). Along the same lines, the rise in the IFO industrial activity index in May (putting it at 103.5 points) reinforces the view of an economy well withstanding the blows, an impression only partly changed by the correction in the June indicator which showed 101.3 points.

This was largely due to the good trend in the foreign sector. In the 12 months ending in April, the trade surplus amounted to 203.2 billion euros, a figure some 34% higher than one year earlier. This trend has been aided by the notable progress in exports which (as a cumulative figure for 12 months) has been growing at rates of 7.5%-8.5% year-on-year since the beginning of the year.

In this situation, the main blemish in the German economy is inflation. In May, Germany's inflation stood at 3.0% year-on-year which meant that it was holding at high levels. The worst feature is that prospects are not good. The Bundesbank recognizes that the country cannot wait until the end of 2008 for the growth rate of prices to drop substantially below that now being recorded.

GERMANY: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
GDP	3.1	2.6	2.6	2.5	1.8	2.6	–	…
Retail sales	6.1	–7.6	–7.7	–7.4	–8.8	–0.7	–1.0	…
Industrial production	6.0	5.9	5.4	5.6	5.0	5.4	4.8	…
Industrial activity index (IFO) (*)	105.5	106.2	108.0	105.5	103.7	104.0	102.4	103.5
Unemployment rate (**)	10.7	9.0	9.2	8.9	8.5	8.0	7.9	7.9
Consumer prices	1.6	2.3	2.1	2.3	3.1	2.9	2.5	3.0
Trade balance (***)	151.5	183.5	178.3	192.0	198.1	201.1	203.2	…

NOTES: (*) Value.
(**) Percentage of labour force.
(***) Cumulative balance for 12 months. Billion euros.
SOURCE: Eurostat, European Central Bank, European Commission, national statistical bodies and own calculations.

France: an economy slowing down?

The growth of the French economy in the first quarter was an unexpected relief. The figure was 2.2% year-on-year, equivalent to a quarter-to-quarter increase in GDP of 0.6%, more than expected. Now, the Bank of France feels that in the second quarter the economy could grow by a low 0.3% quarter-to-quarter. This represents a situation of sharp slowdown in growth.

Latest available indicators suggest the weak points in the French economy. The biggest problem is consumption. Given the relatively unsatisfactory state of France's foreign demand, growth of the economy largely depends on household consumption. And consumer are proving reluctant. For example, domestic consumption grew by a me re 1.7% year-on-year as the April-May average as against 2.3% in the first quarter. This is partly a basic problem and partly the result of a lack of confidence.

Two key determining factors of consumption, unemployment and inflation, are thus working against it. The decrease in the unemployment rate, which had given strength to private consumption, has just not happened over three consecutive months (between February and April the unemployment rate has been stuck at 7.8% of the labour force). The increase in inflation, that put the CPI at 3.3% year-on-year in May, brings about a notable loss of purchasing power at a time when its maintenance would be important. Apart from these factors, consumer confidence was down 3.4 points in March and April, a serious drop to have taken place in only two months.

Bundesbank warns of difficulties in correcting high inflation.

In this context, the improvement in industrial activity in April (growth of 3.2% year-on-year as against 0.7% in March) seems to be an isolated positive figure, especially if we take into account that industrial orders were down notably in March and April. Nor do other supply indicators offer signs of recovery. Confidence in the tertiary sector and various construction indicators confirm the downward trend in services and construction.

In spite of good growth figure in first quarter, French economy may show practically no growth in second quarter.

Finally, in contrast to other key economies in the Euro Area, the trade deficit continues to worsen month after month. In April, the trade deficit increased to 42.7 billion euros (in cumulative figure for 12 months), far

Private consumption weakening sharply.

FRANCE: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
GDP	2.4	2.1	1.7	2.4	2.2	2.2	–	…
Domestic consumption	3.3	4.4	4.3	4.9	3.7	2.3	0.2	3.1
Industrial production	1.1	1.5	0.2	2.1	2.5	1.9	3.2	…
Unemployment rate (*)	9.2	8.3	8.4	8.2	8.0	7.8	7.8	…
Consumer prices	1.7	1.5	1.2	1.3	2.3	2.9	3.0	3.3
Trade balance (**)	–26.9	–32.2	–30.2	–32.8	–37.3	–40.5	–42.7	…

NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion euros.
SOURCE: OECD, Eurostat, INSEE, European Commission and own calculations.

Inflation and trade deficit are two pressing imbalances.

from the average of 40.5 billion euros in the first quarter. Sharp growth of imports, along with stagnation in exports, was behind this poor performance.

Italy: a poor first quarter

Italy scarcely grows in first quarter.

The Italian economy continues to be going through a difficult time. Compared with the generally more positive first-quarter figures in most the Euro Area economies, in the first quarter Italy grew by a mere 0.3% year-on-year, a figure certainly better than the 0.1% seen in the fourth quarter but one indicating a notable weakness in the economy. The growth problems arise from the poor state of private consumption. The drain from change in inventories also added a negative contribution. On the other hand, investment and public consumption showed no change over the previous quarter. In this context, the only factor that made it possible to beat the figure for growth in the fourth quarter as the contribution from foreign demand.

Situation on way to becoming stable.

From this point on, the figures indicate some stabilization of the situation. Breaking with recent trends, consumer confidence recovered in April and May and ended the latter month at the –19.5 points level, its best figure since September 2007. Figures for industrial activity were also slightly better. In April, industrial production grew by 0.2% year-on-year thus improving on the March figure when the indicator had dropped by 1.2% year-on-year. As an overall summing up of the situation in economic activity, the economic sentiment indicator rose by three points in May. This relative containment of economic weakness stands in contrast to the poor state of inflation. In May, the CPI grew by 3.6% year-on-year, a figure not reached since 1996.

In another sphere, we should mention that the new government led by prime minister Silvio Berlusconi has begun to take its first decisions on economic matters. The Italian government has decided to abolish the tax on real estate in the case of a main residence and to reduce taxes on overtime in private companies. To prevent these tax cuts from having a negative effect on the delicate state of public finances the Minister of Economy, Giulio Tremonti, has announced that some 70 spending headings are to be eliminated.

ITALY: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
GDP	1.9	1.4	1.6	1.6	0.1	0.3	–	…
Retail sales	1.2	0.5	0.1	0.2	0.5	0.9	…	…
Industrial production	2.4	0.0	0.7	0.8	–3.0	–1.2	0.2	…
Unemployment rate (*)	6.8	6.1	6.1	6.2	6.2	6.5	–	…
Consumer prices	2.1	1.8	1.6	1.6	2.4	3.1	3.3	3.6
Trade balance (**)	–17.6	–13.7	–15.4	–11.3	–8.9	–9.1	–8.6	…

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

United Kingdom: priority is to save growth

The recent dilemma of the Bank of England exemplifies the present situation of the British economy. Should it support a weakening economy or, on the other hand, would it be better to contain inflation expectations in view of rising prices? Central bank governor Mervyn King explained in his letter to parliament (which he legally must write when inflation goes above 3% year-on-year) that he felt the situation in the United Kingdom was the biggest economic challenge in the past 20 years. At the same time, he foresaw that inflation could go above 4% (in May it was 3.3% year-on-year) and seemed to suggest that monetary policy would not be made any tighter. In fact, the priority seemed to be to salvage economic activity.

Nevertheless, the economy is showing the odd positive surprise along with some figures that are quite poor. The sector most clearly reflecting the economic difficulties is real estate. Figures show a drop in prices and sales and no one is expecting that the situation will improve quickly. The trend in other supply indicators (and here we may cite the slack in industrial production that grew by a mere 0.2% year-on-year in May) also suggests an economy going through a slowdown.

New government introduces tax cuts while controlling public spending.

This is in contrast to another traditional support of the past British economic cycle, namely household consumption. If we look at the most representative indicator, retail sales, in the first quarter these provided a surprise by moving ahead of the last three months in 2007. But the fact is that in May the figure reached (an increase of 8.1% year-on year) was the highest since 2002. The fact that consumer confidence, while not giving up its gradual downward tendency, has halted its drop also suggests that households are bearing up. While it is true that the low level of unemployment may be helping (the unemployment rate was again 2.5% in May), the resilience of consumer demand cannot fail to be surprising.

British economy showing high inflation and slowdown trend.

Caught between both difficulties economic policy seems aimed at rescuing growth.

UNITED KINGDOM: MAIN ECONOMIC INDICATORS

Percentage change over same period year before unless otherwise indicated

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
GDP	2.9	3.0	3.2	3.1	2.8	2.5	–	…
Retail sales	3.2	4.3	4.0	4.8	3.9	5.5	3.9	8.1
Industrial production	0.3	0.3	0.8	0.1	0.7	0.4	0.2	…
Unemployment rate (*)	2.9	2.7	2.7	2.6	2.5	2.5	2.5	2.5
Consumer prices	2.3	2.3	2.6	1.8	2.1	2.4	3.0	3.3
Trade balance (**)	–74.1	–82.9	–80.5	–84.0	–88.4	–90.9	–91.9	…
3-month Libor interest rate (***)	4.6	5.3	5.6	6.0	6.3	6.0	6.0	5.8
Nominal effective pound exchange rate	98.0	103.9	104.0	104.3	102.2	97.6	92.6	93.1

NOTES: (*) Percentage of labour force.
(**) Cumulative balance for 12 months. Billion pounds.
SOURCE: OECD, Bank of England, ONS, European Commission and own calculations.

Private consumption figures offer some relief although this could be temporary.

The fact is the erosion of purchasing power is undeniable. As mentioned earlier, inflation in May was surprising (with growth of 3.3% year-on-year) as it beat the already troubling 3.0% recorded in April. Both the situation in energy and foods and the trend in inflation expectations would confirm the Bank of England's views. Its warning that the process of price increases will not be soon corrected looks very real.

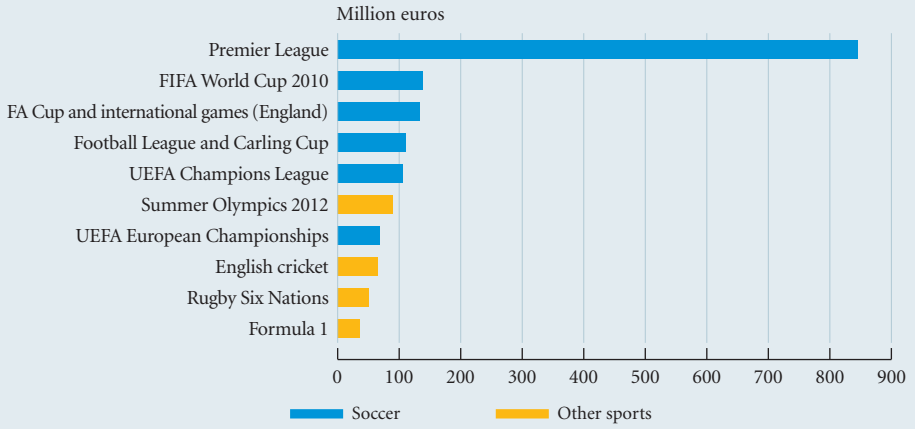
Television rights... going once... twice... sold!

A man in a black suit scans the audience in search of the slightest change in their gestures. When he perceives it he raises his voice calling out a figure, somewhat higher each time. At a certain moment, suddenly, everything stops, no one makes a move and the sound of a hammer echoes through the room. A Picasso has just been sold. This is a familiar enough scene and, yet, it seems a bit strange to imagine the man in black striking the gavel for the rights to the Champions League. Nevertheless, the mechanisms that determine the price of those rights closely resemble those that set the figure for a Picasso at Christie's or Sotheby's. When the exchange of a good is negotiated directly between a small number of buyers and a single seller, the different competition theories give way to auction theory. In this box we will see how auction theory applies to the market for television broadcasting rights and whether this allocation method explains the differences in value observed among the rights of the various sports events (see following graph).

First, we have to know who the seller is. Ownership of television broadcasting rights may fall directly on the teams competing in the championship (as is the case with soccer in most countries) or on the body organizing the competition (as happens in the Formula 1 or with the soccer league in France). Nevertheless, given the complementary nature of the rights of the various teams, it is common to negotiate the sale of such rights collectively through the championship organizer. The British Premier League negotiates the joint sale of the rights of the teams competing each year and divides the profits according to a predetermined formula.

SOCCER: REIGNS ALSO ON TELEVISION

Amount per season for the latest rights negotiated in the United Kingdom



SOURCE: Ofcom.

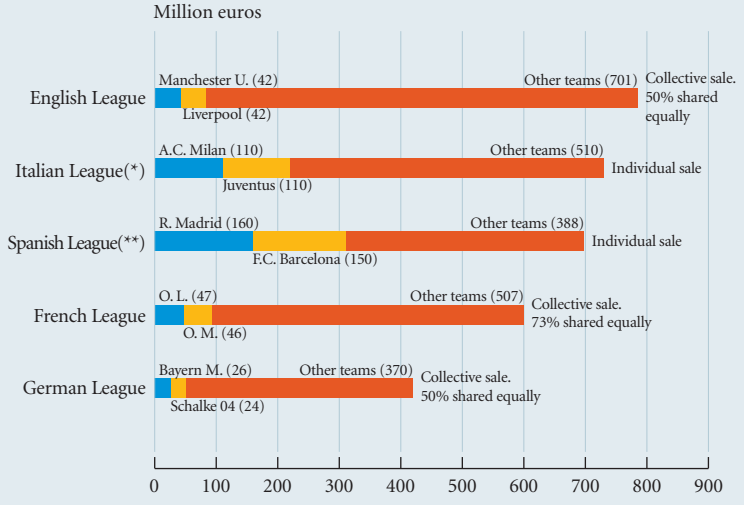
In Spain, on the other hand, teams negotiate the sale of their rights directly and the buyers are the ones who afterwards must come to an agreement on how these rights are shared. Individual sale favours the bigger teams bringing in more income than under joint sale (see following graph). Nevertheless, earnings by the championship as a whole are usually lower than under joint sale (given the attractiveness of the League and the purchasing power of the consumer) and the resulting big inequality between clubs' income may distort too much the competitive balance, thus reducing its attractiveness.

Television network operators are the main bidders for sports broadcasting rights. Sports programmes provide another type of content to shape an attractive programming (or TV channel) to viewers. It is important, however, to distinguish between two types of operators according to their business model. On the one hand, the traditional free-to-air television channel operators «sell» viewers to companies wanting to advertise their products. To some extent, these operators act as go-betweens who match advertisers with their targeted audience. To obtain the biggest possible audience, the viewers get the service for free and all the earnings arise from the value of that audience to the advertisers. Hence, these operators' willingness to pay for the rights is the potential income from advertising during the broadcasting of the event.

The alternative model is one followed by pay-tv operators. These operators group content into different channels that are offered to the final consumer in a single bundle in exchange for a subscription fee. In this case, broadcasting rights of certain competitions are used to attract new subscribers. It is precisely this power of attraction, along with that of keeping existing customers, what determines how much operators are willing to pay for the rights. In some cases, competitions may be so attractive to the public that offers by pay-tv operators can exceed those from free-to air operators.

SOCCER RIGHTS: NATIONAL CHAMPIONS OR A BALANCED COMPETITION?

Amount of rights for the 2006/07 season



NOTES: (*) 2007/08 season. The rights for the 2010 season and onwards will be negotiated collectively.
(**) Total amount estimated assuming the two leading clubs-rights weight a 44% of the total. (Ofcom).
SOURCE: Sports Business Group, Deloitte, Football Money League; La Gazetta dello Sport, October 10, 2007 and Falconeri, S., J. Sákovics and F. Palomino (2004), «Collective versus individual sale of television rights in league sports», Journal of the European Economic Association, Vol. 2 (5).

According to figures from the European Commission, 65% of subscribers in the United Kingdom mention sports programmes as the main reason for subscribing. In Spain, the figure reaches 85%. In addition, according to the Spanish competition authority, 17 out of the 20 sports events most viewed in Spain in 2005 were soccer matches. It is therefore not surprising that soccer manages to sell its television rights at a much higher price.

Once we know the players, we must define the elements comprising an offer for television transmission rights. For the owners, these rights are just one more source of income along with the sale of tickets to the event, advertising placed around the stadium and sponsorship obtained by the competitors. Television coverage of the event may affect these other revenues so that the seller must take this into account in analyzing the offers received. These offers must be weighed not only by their price but also keeping in mind the effect on ticket sales and the value of the television audience for advertisers and sponsors. Although pay-tv operators are able to make more attractive monetary bids, their audience is not as large and this reduces the value of sponsorships and advertising on the ground. This explains why, for example, Mr. Ecclestone prefers to sell Formula 1 broadcasting rights to free-to-air operators.

Keeping in mind this wider definition of an offer: what determines the final price of rights? Let us imagine that the auction is organized like the aforementioned Picasso example. The bidder with the second highest valuation for the rights will stay in the bidding process until it reaches the limit of his/her valuation. He/she will retire on the next bidding increment thus leaving alone the bidder with the highest valuation. The latter wins but only has to pay an amount slightly higher than the second bidder's valuation. Auction theory formalizes this idea and tells us that the winner will have to pay approximately the value of the rights for the second highest bidder. Given the marked differences between the two types of operator, in terms of willingness to pay and potential audiences, what largely determines the final price of the rights is the two leading bidders being of the same type.

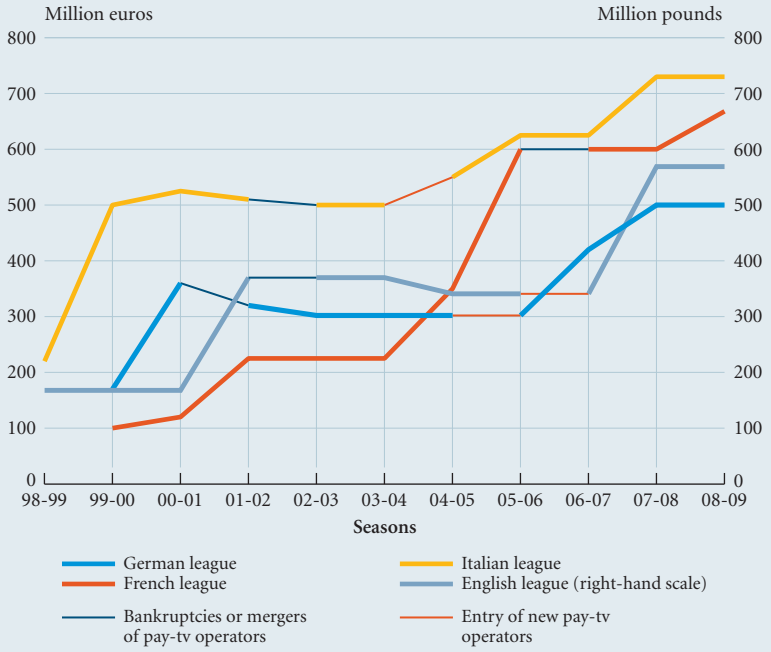
The importance of the identity of the second bidder can be seen in the evolution of prices paid for the rights to the main football leagues. The collapse of various pay-tv operators at the beginning of the decade halted the upward trend in the price of rights for the immediately following seasons (see following graph). Later on, a wider adoption of pay-tv and technological advances such as digital terrestrial television and television via ADSL, have enabled the surge of credible competition in the sector and the price of rights has risen again. In a word, given that their value is similar for all pay-tv operators, competition means that the price finally paid by the winner is very close to its own valuation.

Nevertheless, this is not the only reason why competition in the pay-tv market increases the price of rights. Another reason is based on the effect that winning the rights may have on the degree of future competition between operators. At the early stages of the pay-tv market, losing soccer rights could mean not gaining a sufficient customer base to remain in the market. The possibility of excluding rivals meant that operators became more aggressive in their bidding. The case of France is a perfect example. In 2005, CanalSat doubled the bid made by its rival TPS in order to obtain in exclusivity the rights they had shared until that moment. Having lost the rights, TPS accepted a merger with CanalSat. Cases like this have led competition authorities to keep an eye on the sale of rights. The authorities may modify the auction rules or the nature of rights in order to avoid, for example, that collective sale leads to an excessive increase in prices or that the exclusivity of rights drives competitors out of the market.

To sum up, when the auction rules are well designed, they offer a very efficient method of selling a good at the highest possible price. For this reason, we should not be surprised if one day television broadcast rights are auctioned at Christie's. Nor should we be surprised if, along with the keen eye of the man in black, we find the alert eye of the regulator.

COMPETITION IN PAY-TV MARKET CONDITIONS THE PRICE FOR THE TV RIGHTS

Trend in soccer rights



SOURCE: Ofcom and own calculations.

FINANCIAL MARKETS

Monetary and capital markets

Inflation complicates monetary policies

Central banks ease monetary policy in order to deal with financial crisis...

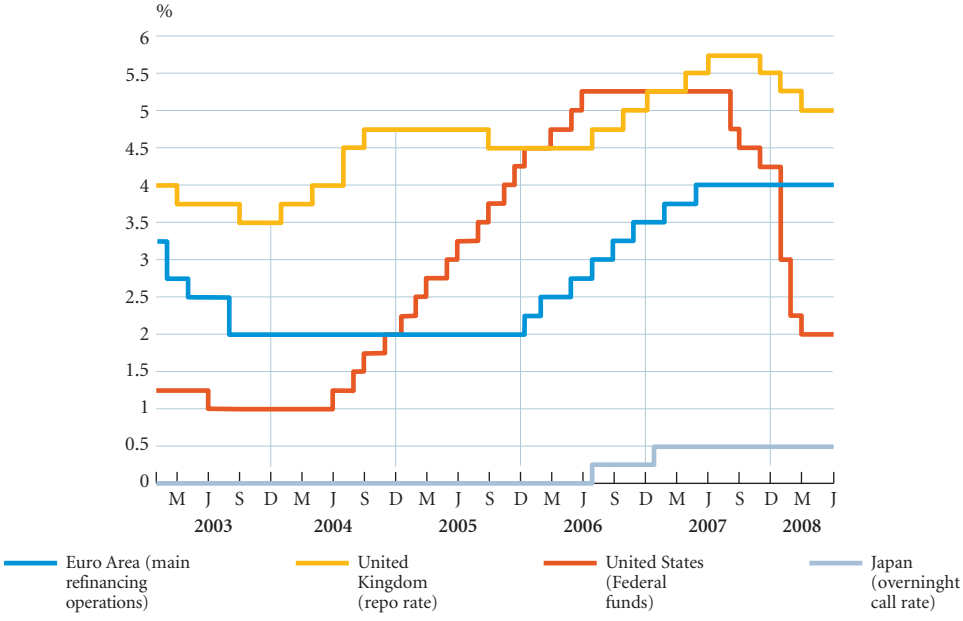
The subprime mortgage financial crisis that began in August last year drove the central banks in the United States and Europe to inject the necessary liquidity to avoid the collapse of loan markets. The central banks of the United States and the United Kingdom lowered their reference rates while the European Central Bank did not follow this move but sharply halted the series of increases it began in December 2005. It even cancelled the rise earlier announced for last August due to the upsets in financial markets.

As well as providing the necessary liquidity, the priority of the central banks and monetary authorities was to avoid a system crisis in the banking sector. That is to say, to avoid the risk of a chain of failures in lending institutions that would bring about a collapse of the financial system that, as happens in bank crises, would inevitably hurt the real economy.

But now it is inflation that seems to have taken first place among the concerns of the central banks. The sharp rise in oil prices combined with the increase in food commodity prices has pushed up inflation indicators. In order to meet this

IS THIS THE TIME FOR A RISE?

Central bank reference rates



SOURCE: Central banks.

risk, the prescription is the opposite of that applied up to now, namely, to contain excess liquidity and even raise interest rates.

The central banks must therefore normalize an extraordinary situation in official interest rates brought about by the special circumstances of sharp pressures in financial markets. At what moment and how strongly should the monetary authorities take action? If the central banks move too soon they could bring about a relapse of the pressures on liquidity and if they delay, as an undesired effect, they could set off new bubbles in other markets and an increased risk of higher inflation.

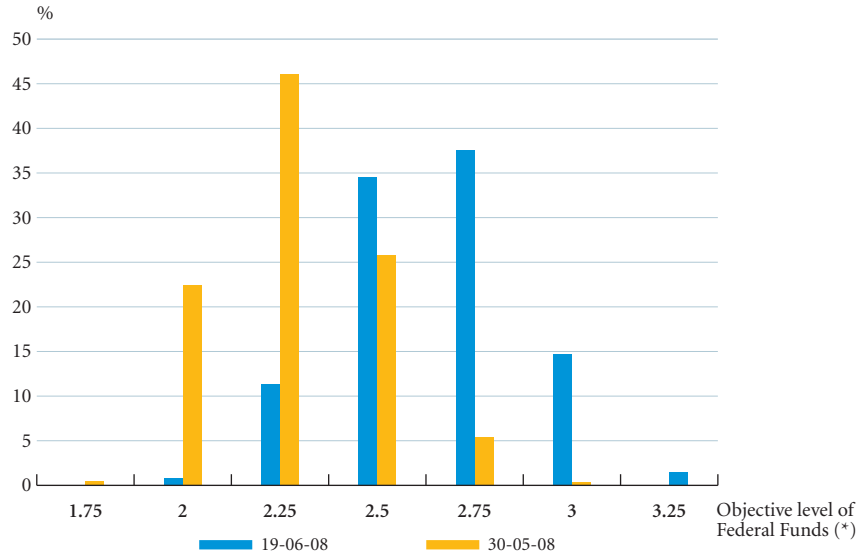
In this context, the chairman of the Fed, Ben Bernanke, admitted in a recent talk that the increase in commodity prices had still not been passed through to final prices of goods and services in the US market. The reason was that the weakness of consumer spending meant companies did not have sufficient incentive to change prices. That is to say, companies cannot pass through cost increases to final prices due to the weakness of domestic demand in the United States. Nevertheless, Bernanke added that he did not expect this situation to last much longer. These statements, on top of similar comments by other members of the Fed, have set off speculation about possible increases in the Fed's reference rate.

The accompanying graph shows how at the end of May the futures market assigned a 45% probability that at the end of this year, at its last meeting in December, the central bank system would raise the official rate from the present 2% to 2.25%. It was discounting that the worst of the financial crisis was over and therefore it could back off the previous interest rate cuts. On the other hand, following these latest statements

...but now they must decide when to normalize situation of extraordinarily low interest rates.

MARKETS FEEL THAT FED WILL SOON RAISE RATES

Probability of Fed reference rate in December 2008 discounted by futures market



NOTES: (*) Now standing at 2%.
SOURCE: Bloomberg.

Futures market discounting that Fed will raise official rate this year.

and economic figures, the futures market is discounting with a 38% probability that the official rate could go to 2.75%. It is clear that these figures are volatile and that a combination of weak economic figures or a worsening of the financial crisis could take us back to the first scenario for the futures market. But this does underline a sharp change in investor expectations from the month before brought about by astronomical oil prices which is being discounted as ending up forcing the central bank to act sooner than it was earlier believed.

ECB makes early announcement of rise at July 3 meeting.

In the Euro Area, the statements by Jean-Claude Trichet, governor of the European Central Bank, surprised the markets and the analysts when he stated that the ECB could announce a rise in the official rate, now at 4%, to deal with the highest inflation in the past 16 years. He also added that at the last meeting of the Governing Council several members had voted in favour of an increase in rates. This was in spite of the fact that the E had lowered its growth forecast for the Euro Area in 2008 by three decimals to 2%.

Governor of Bank of England recognizes gravity of economic situation.

The markets took careful note and took positions in the face of the expectations of an increase in reference rate at the next meeting on July 3. Should this rise be confirmed the analysts will show great interest in the official ECB press release following its next meeting. It is likely that the first questions at the press conference will be whether we are facing a new round of increases.

Bond yields incorporating prospects of rise in official rates.

In the United Kingdom, the central bank is not having things any easier. In fact, it would seem that since the beginning of the financial crisis everything has become distorted. The Bank of England has an inflation objective of 2% and, when this is off by more than one percentage point in any direction, the governor must write a letter to the Chancellor of the Exchequer setting out what he has in mind to bring inflation quickly back within the 1%-3% range. The latest inflation figure was 3.3% so that on June 16 governor King was obliged to write a letter in which he stated that inflation could even stay above 4% in the second half of this year. Furthermore, he expected that inflation would return to around 2% but that it would take around 24 months to bring this about. The problem is that with a slowdown in the economy the central bank's margin for manoeuvre is very limited. It recognizes that it could cut this time period to 12 months by raising the official interest rate but that this could bring a sharp increase in the volatility of the gross domestic product and employment in the United Kingdom. That is to say, it could cause a recession.

Asia too is feeling the inflationary phenomenon. China's central bank continued its tougher measures to fight an inflation figure that seems to be stuck at around 8% over the past four months. The central bank ordered a 100 basic points rise in bank cash ratios from 16.5% to 17.5%. This increase in cash ratio, the fifth since the beginning of the year, remains insufficient and the Chinese central bank will likely again raise the official interest rate.

Interest rates keep rising

Bond markets have had to incorporate the expectations of increases in official interest rates. Furthermore, they are still being affected by the financial upsets that began in the middle of last year. For this reason, it is difficult to distinguish in bond yields that part incorporating expectations of increases in the central

SHORT-TERM INTEREST RATES IN NATIONAL MARKETS

As annual percentage

	Euro area			United States		Japan	United Kingdom		Switzerland
	ECB auctions (2)	Euribor (5) 3-month	Euribor (5) 1-year	Federal Reserve Board target level (3)	3-month (5)	3-month (5)	Bank of England repo rate (4)	3-month (5)	3-month (5)
2007									
May	3.75	4.12	4.46	5.25	5.36	0.69	5.50	5.81	2.42
June	4.00	4.18	4.53	5.25	5.36	0.76	5.50	6.00	2.67
July	4.00	4.26	4.54	5.25	5.36	0.78	5.75	6.04	2.63
August	4.00	4.74	4.78	5.25	5.62	0.97	5.75	6.69	2.86
September	4.00	4.79	4.73	4.75	5.23	1.03	5.75	6.30	2.82
October	4.00	4.60	4.60	4.50	4.89	0.90	5.75	6.28	2.68
November	4.00	4.81	4.69	4.50	5.13	0.99	5.75	6.61	2.62
December	4.00	4.68	4.75	4.25	4.70	0.90	5.50	5.99	2.63
2008									
January	4.00	4.37	4.32	3.00	3.11	0.87	5.50	5.58	2.59
February	4.00	4.38	4.38	3.00	3.06	0.96	5.25	5.74	2.72
March	4.00	4.73	4.73	2.25	2.69	0.91	5.25	6.00	2.78
April	4.00	4.86	4.96	2.00	2.85	0.92	5.00	5.84	2.86
May	4.00	4.86	5.10	2.00	2.68	0.92	5.00	5.87	2.78
June (1)	4.00	4.96	5.43	2.00	2.80	0.92	5.00	5.95	2.93

NOTES: (1) June 19.

(2) Marginal interest rate. Latest dates showing change in minimum rate: 3-8-06 (3.00%), 5-10-06 (3.25%), 7-12-06 (3.50%), 8-03-07 (3.75%), 6-06-07 (4.00%).

(3) Latest dates showing change: 11-12-07 (4.25%), 22-01-08 (3.50%), 30-01-08 (3.00%), 18-03-08 (2.25%), 30-04-08 (2.00%).

(4) Latest dates showing change: 10-05-07 (5.50%), 5-07-07 (5.75%), 6-12-07 (5.50%), 7-02-08 (5.25%), 10-04-08 (5.00%).

(5) Interbank rate.

SOURCE: National central banks, Bloomberg and own calculations.

bank reference rate, the part that incorporates credit risk premium and that for liquidity premium.

Perhaps the most notable for its importance in the euro system is the 1-year Euribor reference rate. Following the statements by the ECB chairman regarding a possible increase in reference rate at the meeting of the central bank governing council on July 3, interest rate curves for the interbank market and the bond market rose. For example, following Trichet's comments the 1-year Euribor hit 5.43%, a level not seen since January 2000. Many credit, mortgage and commercial contracts in the Euro Area are pegged to this indicator. That is to say, in those contracts that are being renewed at this time the increased costs of financing is notable.

1-year Euribor hits 5.43%.

Historically, the differential between the ECB reference rate and the 1-year Euribor has been around 40-50 basis points (100 basis points equals 1%). At present, the differential is 143 basis points, the highest since the launching of the single currency in the Euro Area. We cannot expect the situation in this differential to normalize before the end of the year due to uncertainty about when it will be possible to state that the financial crisis is a thing of the past.

LONG-TERM INTEREST RATES IN NATIONAL MARKETS

10-year government bonds at end of period as annual percentage

	2005	2006	2007		2008	
			September	December	May	June (*)
United States	4.39	4.70	4.59	4.02	4.06	4.13
Japan	3.31	1.69	1.69	1.51	1.76	1.80
Euro Area	1.48	3.95	4.33	4.33	4.41	4.57
United Kingdom	4.10	4.74	5.01	4.51	4.99	5.14
Switzerland	1.97	2.52	3.01	3.05	3.19	3.37

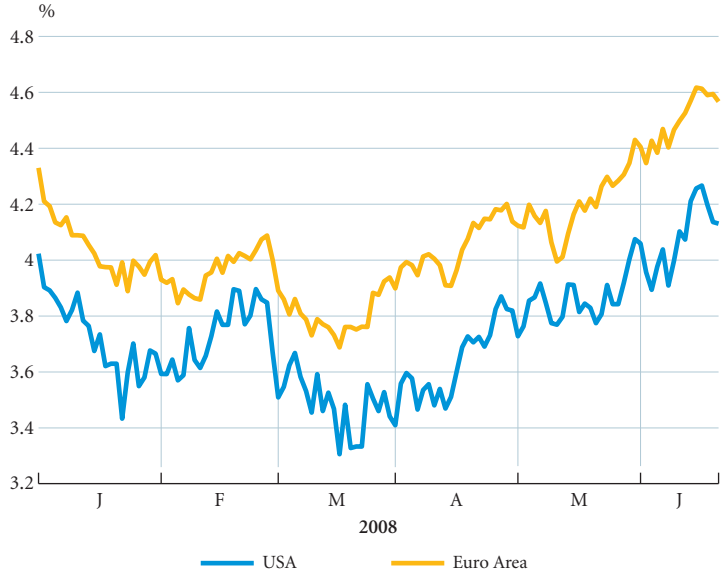
NOTES: (*) June 19.
SOURCE: Bloomberg.

Interest rate differentials in interbank market have not been so high since launching of euro.

Nor have government bonds been free of the latest events and the upward trend that began in mid-March is continuing, coinciding with the Fed's rescue of what was the fifth largest investment bank in the United States, namely Bear Stearns. From that moment on, fear of a system crisis in international banking began to wane. But, on the other hand, there was increased potential risk of higher inflation and investors have increased the risk premium demanded from bonds. The movement in bonds has been lively. As may be seen in the accompanying graph, US 10-year bonds, that reached a figure of 3.30% in mid-March, have gone above the psychological level of 4%, while government bonds for the same term in the Euro Area are now at 4.60%.

INCREASED YIELDS ON GOVERNMENT BONDS

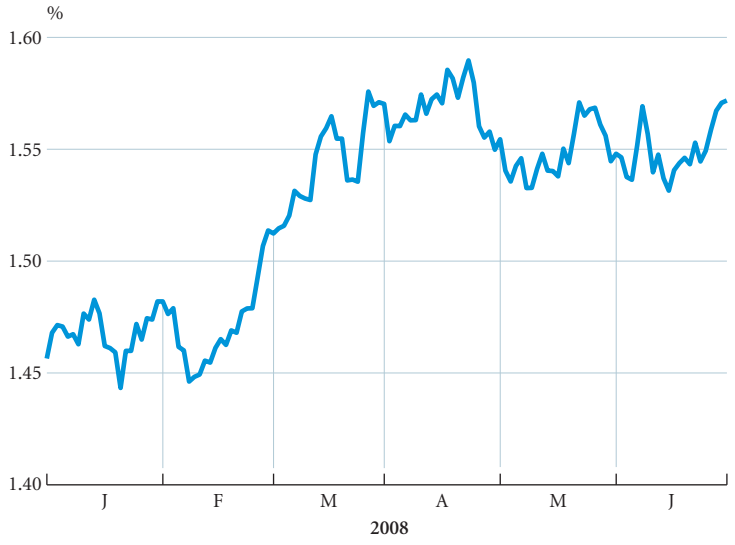
Interest rate on 10-year government bonds



SOURCE: Bloomberg.

EURO-DOLLAR EXCHANGE RATE AGAIN SNAPS AT 1.60 FIGURE

Euro-dollar exchange rate



SOURCE: Bloomberg.

Foreign exchange market watching interest rates

In the past month, the euro-dollar exchange rate has moved about a great deal but always hanging around 1.55. There are a number of factors behind the moves in either direction are if it were a situation of pulling and letting go. It is a bit like a game of tug-o-war with each team pulling with all is might to win the game. But for now, the winner has not been decided.

On the one hand, there are the statements by Bernanke, chairman of the Fed, who stated on June 3 that he was in favour of a strong dollar. That is to say, he was concerned that in the present situation any increase in the depreciation of the dollar could mean an increase in imported inflation and therefore risks for price stability. Historically it is the US Treasury that makes statements about the desirable level or movements in the currency while, on the other hand, the central bank comments on the interest rate. The fact that this tradition has been broken is indicative of the concern the trend to depreciation of the dollar represents for the Fed.

Following these comments, the euro-dollar exchange rate dropped to 1.53. On the other hand, differing positions are held by the central banks. While the European Central Bank advanced the possibility of a rise in reference rate at its meeting on July 3, at least for now it seems the Fed is not going to raise its official rate. This implies that the interest rate differential between the two areas will increase in favour of the Euro Area. This was the factor that pushed the euro-dollar exchange rate up to 1.58 at the end of June.

In addition, it is worth noting the movement of the yen against the dollar and the euro. The yen has firmed against

Government bonds raise yield because of inflation risk.

EXCHANGE RATES OF MAIN CURRENCIES

June 30, 2008

	Exchange rate	% change (*)		
		Monthly	Over December 2007	Annual
Against US dollar				
Japanese yen	105.3	0.8	–6.1	–16.3
Pound sterling	0.501	–1.4	–0.5	1.1
Swiss franc	1.017	–2.1	–11.5	–19.1
Canadian dollar	1.008	0.6	0.9	–4.8
Mexican peso	10.292	–0.4	–6.0	–4.5
Against euro				
US dollar	1.580	1.7	8.3	16.0
Japanese yen	166.4	2.5	2.1	–0.2
Swiss franc	1.606	–0.4	–2.9	–2.6
Pound sterling	0.792	0.3	7.8	17.3
Swedish krona	9.444	0.7	0.1	2.1
Danish krone	7.458	0.0	0.0	0.2
Polish zloty	3.356	–0.8	–6.9	–10.6
Czech crown	23.90	–4.0	–9.9	–17.0
Hungarian forint	237.5	–1.4	–6.1	–3.5

NOTES: (*) Plus sign indicates appreciation of dollar (first group) or euro (second group).
SOURCE: Bloomberg.

Two factors affecting euro-dollar exchange rate: interest rate differential between both areas and statements by Fed chairman.

both currencies since the beginning of the year due to the fact that in the early months of the year, in view of the worsening of the financial crisis, investors were divesting themselves of carry trade positions (operations involving borrowing in currencies with low interest rates and simultaneous investment in high-yield currency assets). As of March, the yen has depreciated against the euro and the dollar but recently it is against the European currency that it is more sharply depreciating. The reason is clear enough seeing that the Japanese would like to maintain the competitiveness of their exports and as many Asian currencies are being subject to official intervention to prevent them from appreciating more against the dollar.

Stock markets go back to lows reached in March

International stock markets seem to have moved into an *annus horribilis* seeing that they again had a poor month in view of the flood of bad economic news and the impact these had on their profit and loss accounts. Investors are discounting a situation of stagflation. That is to say, lower growth with higher inflation.

Driven by stagflation scenario, stock markets again drop sharply.

This situation is the worst scenario for share prices. If, on the one hand, there is lower growth and sales drop and on the other hand the increase in energy and financial costs cannot be added to final prices due to the weakness of demand, if signifies that financial margins of

INDICES OF MAIN WORLD STOCK EXCHANGES

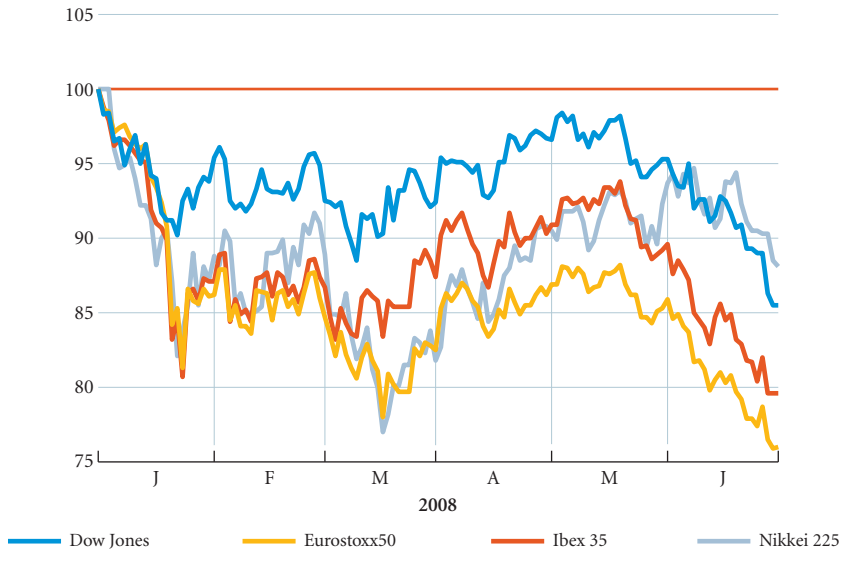
June 30, 2008

	Index (*)	% monthly change	% cumulative change	% annual change
New York				
Dow Jones	*11,346.5*	*–10.2*	*–14.5*	*–15.4*
Standard & Poor's	*1,278.4*	*–8.7*	*–12.9*	*–15.0*
Nasdaq	*2,315.6*	*–8.2*	*–12.7*	*–11.0*
Tokyo	*13,481.4*	*–6.0*	*–11.9*	*–25.7*
London	*5,558.0*	*–8.2*	*–13.9*	*–15.9*
Euro Area	*3,343.5*	*–11.5*	*–24.0*	*–25.5*
Frankfurt	*6,412.9*	*–9.6*	*–20.5*	*–19.9*
Paris	*4,398.3*	*–12.3*	*–21.7*	*–27.4*
Amsterdam	*423.0*	*–12.9*	*–18.0*	*–22.8*
Milan	*29,269.0*	*–11.9*	*–24.1*	*–30.2*
Madrid	*12,085.4*	*–11.1*	*–20.4*	*–18.8*
Zurich	*6,845.8*	*–8.9*	*–19.3*	*–25.7*
Hong Kong	*22,109.8*	*–9.9*	*–20.5*	*1.5*
Buenos Aires	*2,093.0*	*–5.1*	*–2.7*	*–4.5*
São Paulo	*64,321.1*	*–11.4*	*0.7*	*18.3*

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

PROOF OF MARCH LOWS

Stock market trends with base 1-1-2008 = 100



SOURCE: Bloomberg.

Until very recently emerging country stock markets were investor refuge but Chinese stock market has suffered sharp drop.

companies must grow worse. In a situation where companies have less ability to generate profits and where uncertainty about profits is on the increase, investors want to see higher risk premiums. For this reason, share prices must drop.

It may be seen how in the above graph the stock market indices for the Euro Area and the United States, along with the Spanish index, have gone below the lows reached in March this year. The first half of this year has been fateful for share prices. The main US markets are showing a cumulative drop of around 15% since the beginning of the year. The European indices have been worse with capital losses of between 18% and 24%.

Only the indices of the emerging countries have survived as, for example, Brazil, Mexico and Russia which have benefited from high commodity prices. The exception has been the Chinese stock market which has collected a drop of nearly 50% so far this year.

SPAIN: OVERALL ANALYSIS

Economic activity

Economic activity keeps losing strength

Available economic indicators for the second quarter generally point to a continuation of the trend to a sharp economic slowdown, mainly as a result of lower construction investment and the state of consumption. The economic upsets as a result of transport strikes at the beginning of June did nothing to improve the economic situation. Year-on-year economic growth will therefore go from the 2.7% recorded in the first quarter to a substantially lower level.

Consumption has continued to slow as a result of the drop in consumer confidence which has been affected by the rise in inflation and higher unemployment. The May consumer confidence index prepared by the European Commission went to its lowest level since the last recession in 1993. In April, retail sales in constant terms adjusted for the number of working days dropped by 3.4% compared with the same month last year. The biggest drop showed up in household appliances partly as a result of the drag effect from the housing market. This trend continued to increase in May judging by the year-on-year decreases in billing for white goods, according to the Anfel association.

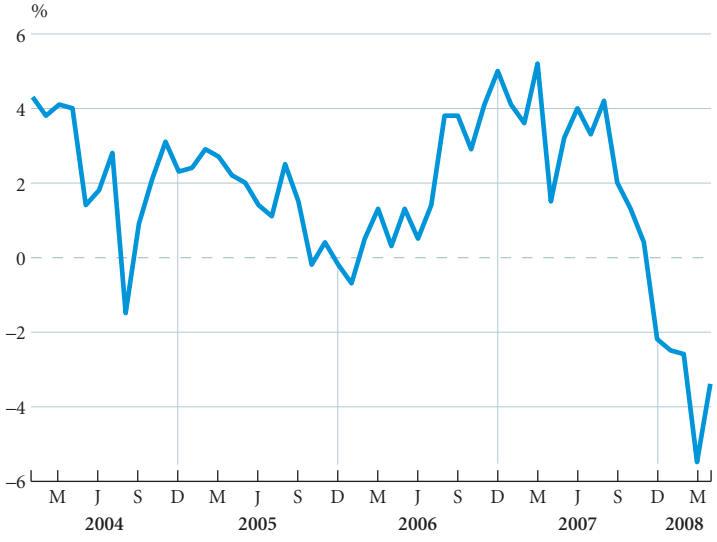
Other durable goods such as cars also recorded big drops in sales in May. On

Tendency to sharp economic slowdown continues with year-on-year growth in second quarter expected to be substantially lower than in first quarter.

Consumer confidence hits lowest level since last recession in 1993.

HOUSEHOLD CONSUMPTION WEAK

Year-on-year change in general retail sales index



NOTES: At constant prices and adjusted for number of working days.
SOURCE: National Institute of Statistics.

DEMAND INDICATORS

Percentage change over same period year before

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
Consumption								
Production of consumer goods (*)	2.3	1.2	2.1	0.9	–2.7	–0.6	0.5	...
Imports of consumer goods (**)	8.9	5.1	5.6	8.4	7.7	–1.2	...	...
Car registrations	–0.9	–1.2	–2.4	–2.9	1.3	–15.3	1.5	–24.3
Credit for consumer durables	14.5	10.0	9.6	6.9	9.9	8.8	–	...
Consumer confidence index (***)	–12.3	–13.3	–12.7	–12.3	–17.3	–20.0	–25.0	–31.0
Investment								
Capital goods production (*)	8.4	5.9	5.3	6.3	3.3	2.0	4.3	...
Imports of capital goods (**)	3.2	9.8	11.0	–0.6	9.0	–16.0	...	...
Commercial vehicle registrations	1.5	0.3	–2.2	–3.0	4.7	–29.5	–17.1	–37.9
Foreign trade (**)								
Non-energy imports	9.0	7.3	7.7	7.6	7.5	4.3	...	...
Exports	5.6	4.2	2.8	6.7	4.6	2.2	...	...

NOTES: (*) Adjusted 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 and Finance, European Commission and own calculations.

Slump in sales of durable goods such as appliances and cars.

top of the worsening economic picture came the rise in fuel prices and tougher financing terms. In this situation, the central government announced a new plan to help take old cars off the road as an aid to sales.

Domestic sales of large companies in April also proved weak. Figures supplied by the Taxation Office show a drop of 1.7% in constant terms and with correction for the number of working days in April. Exports by those companies showed up better with an annual increase of 3.3% as against a rise of 0.5% in imports.

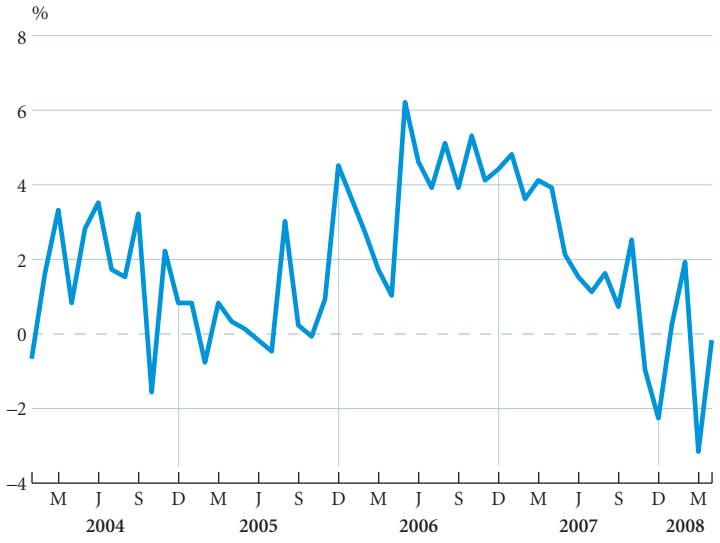
Capital goods investment is also undergoing a slowdown in view of prospects for consumption. Nevertheless, production of these goods in April showed a notable increase of 4.3% over the same month the year before, after adjustment for differences in number of working days. Nevertheless, registration of commercial vehicles showed sharp declines. This is only to be expected given the situation of the transport sector which has been affected by the drop in construction activity.

Sharp correction in housing construction continuing.

In fact, figures for this sector show the adjustment taking place in the residential building sector. In the first quarter, new housing go-aheads were down by 59.8% compared with the same period in 2007 although there is some distortion due to comparison with the final period before the coming into effect of the new building code. Another early indicator of construction investment, cement consumption, was down by 18.7% in May compared with the same month last year. Nevertheless, government tendering recovered strength in the first quarter with a rise of 27.7% compared with the

SLIGHT RECOVERY IN INDUSTRIAL PRODUCTION

Year-on-year change in general industrial production index



NOTES: Statistical series adjusted for differences in number of working days.
SOURCE: National Institute of Statistics and own calculations.

same period last year, which indicates an increase in the level public works.

With regard to industry, the general production index was down 0.2% in April compared with the same month last year in constant terms and adjusted for the number of working days, which shows a somewhat weak situation. Cumulative losses of competitiveness, made worse by the strength of the euro, are slowing recovery in industry. Nevertheless, we note a tendency to improvement in industrial production although the confidence index for industry is weakening.

In keeping with the trend in consumption and investment, capital goods production showed the biggest growth in April. Such branches as electronics and communications equipment, precision instruments, transportation equipment and machine building showed very strong. Under consumer goods, those sectors exhibiting increased growth were non-durable consumer goods sectors such as foods.

Capital goods branches of industry showing strong.

Services showed a somewhat more favourable trend. Sector billing rose by 7.7% in April compared with the same month last year. Tourism, however, showed a year-on-year drop of 3.3% partly due to the fact that this year Easter Week fell in March whereas in 2007 it took place in April.

A situation of lower sales and higher interest rates is resulting in a rise in default. The number of commercial bills unpaid rose by 24.4% in April compared with the same month in 2007. As a result, 4.2% of all due bills were unpaid.

At the same time, the current economic situation does not seem as favourable for entrepreneurs as it was some time back. The number of companies established in April (10,884) was down 12.0%

Increase in default while fewer companies being started.

SUPPLY INDICATORS

Percentage change over same period year before

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
Industry								
Electricity consumption (1)	3.9	4.1	4.4	2.2	4.5	3.3	3.2	1.7
Industrial production index (2)	3.9	1.9	2.5	1.1	–0.2	–0.5	–0.2	...
Confidence indicator for industry (3)	–2.7	–0.3	0.7	–0.7	–3.3	–7.0	–10.0	–14.0
Utilization of production capacity (4)	80.5	81.3	81.3	82.1	81.1	81.3	–	80.3
Imports of non-energy intermediate goods (5)	10.5	8.0	8.2	8.7	7.1	11.4	...	...
Construction								
Cement consumption	8.5	0.2	–1.4	–1.1	–1.9	–14.4	1.3	–18.7
Confidence indicator for construction (3)	14.2	9.3	15.7	12.0	–1.3	–14.7	–21.0	–14.0
Housing (new construction approvals)	18.6	–24.7	–15.0	–50.7	–33.6	–59.8	...	...
Government tendering	31.3	–14.9	–2.2	–30.0	–33.1	27.5	...	...
Services								
Retail sales (6)	2.1	2.4	2.9	3.1	–0.3	–3.6	–3.4	...
Foreign tourists	4.1	1.5	–0.1	1.4	1.6	5.3	–1.0	4.2
Tourist revenue inflows	5.6	3.6	1.6	3.3	4.5	5.0	...	...
Goods carried by rail (km-tonnes)	–1.2	–4.4	–6.5	–1.4	–5.3	–2.7	12.2	...
Air passenger traffic	6.8	9.0	7.2	10.5	8.6	7.9	–2.5	2.2
Motor vehicle diesel fuel consumption	5.5	4.6	3.3	4.2	4.7	–0.9	...	...

NOTES: (1) Adjusted for number of working days and temperature.
(2) Adjusted 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.
(6) Index deflated and corrected for calendar effects.
SOURCE: Red Eléctrica Española, OFICEMEN, AENA, National Institute of Statistics, Bank of Spain, European Commission, Ministry of Public Works, Ministry of Industry, Commerce and Tourism, Ministry of Economy and Finances and own calculations.

OECD makes downward revision in growth prospects for Spain's economy.

compared with the same month the year before. In addition, some 1,178 companies were closed down in April, a year-on-year increase of 32.8%.

In view of the current situation, the Organization for Economic Cooperation and Development (OECD) made a downward revision in its economic growth forecasts for Spain due to the worse economic situation. According to this body, the gross domestic product (GDP) is expected to grow by 1.6% in 2008 with a rise of 1.1% in 2009.

Labour market

Job creation losing steam

The sharp slowdown in the economy in recent months has left its mark on the labour market. The number of workers registered with Social Security rose by 132,647 in May to total 19,384,101. This figure meant an increase of 0.8% compared with the same month last year. This rate is similar to that recorded in recent months but represents a sharp slowdown from the year-on-year change rate of 3.2% marked up in May 2007.

In the past 12 months the number of workers registered with Social Security grew by 150,036 persons. This increase was mainly in services with an increase of 2.7%. In industry on the other hand employment was down by 1.1% in that period and there was loss of jobs especially in construction that is going through a sharp correction in the housing sector with a drop of 7.5% in the number of those registered.

Increase in employment over past 12 months mainly in services.

By nationality, the effect was also asymmetric. In the period May 2007-

Slight drop in Spanish nationals registered with Social Security in past year.

EMPLOYMENT INDICATORS

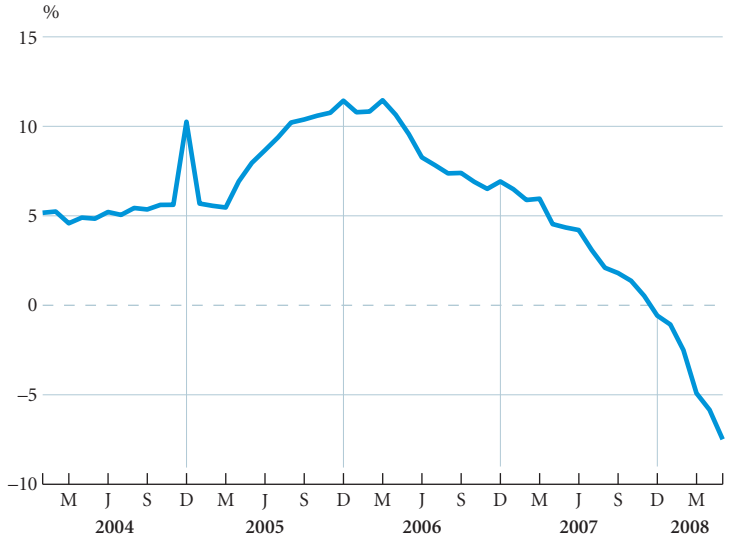
Percentage change over same period year before

	2006	2007	2007			2008		
			2Q	3Q	4Q	1Q	April	May
Persons registered with Social Security								
Sector								
Industry	*0.0*	*2.5*	*2.7*	*2.5*	*2.4*	*0.3*	*–0.8*	*–1.1*
Construction	*8.7*	*3.3*	*4.4*	*2.3*	*0.5*	*–2.8*	*–5.8*	*–7.5*
Services	*5.2*	*3.5*	*3.7*	*3.0*	*3.0*	*2.6*	*2.3*	*2.7*
Job situation								
Wage-earners	*4.7*	*3.0*	*3.5*	*2.6*	*2.2*	*1.2*	*0.6*	*0.7*
Non-wage-earners	*2.2*	*2.8*	*2.7*	*2.9*	*2.9*	*2.3*	*1.5*	*1.2*
Total	**4.3**	**3.0**	**3.3**	**2.7**	**2.4**	**1.4**	**0.7**	**0.8**
Persons employed (*)	**4.1**	**3.1**	**3.4**	**3.1**	**2.4**	**1.7**	**–**	**–**
Jobs (**)	**3.2**	**3.0**	**3.1**	**3.0**	**2.5**	**1.7**	**–**	**–**
Hiring contracts registered (***)								
Permanent	41.1	2.0	15.6	–1.6	–21.1	–11.8	12.0	–13.6
Temporary	4.7	0.3	–1.9	–0.5	1.2	–6.5	4.4	–15.0
Total	**7.9**	**0.5**	**–0.1**	**–0.7**	**–2.1**	**–7.2**	**5.3**	**–14.8**

NOTES: (*) Estimate from Labour Force Survey.
(**) Equivalent to full-time work. National Accounting estimate; figures adjusted for seasonal effects and number of working days.
(***) At INEM.
SOURCE: National Institute of Statistics, Ministry of Labour and Social Services, Employment Institute and own calculations.

LOSS OF JOBS IN CONSTRUCTION CONTINUES

Year-on-year change in number of construction workers registered with Social Security



SOURCE: Ministry of Labour and Social Affairs and own calculations.

Drop in employment in medium-sized companies.

May 2008 the number of persons registered grew by 7.6% in the past 12 months. Of these, workers coming from countries of the European Union rose by 14.8% while those from other countries were up by 4.2%. As a result, foreign workers registered represented 11.1% of the total at the end of May. Construction showed up as the sector giving work to most foreign workers (20.0%) followed by the hotel/restaurant trade at 15.1%.

By sex, the trend seen in recent months continued with a 1.1% year-on-year drop in the number of males registered and a rise of 3.4% in the case of females. As a result, females continue to increase their proportion of the total putting it at a high of 42.7%.

In addition, job creation was concentrated in large companies and very small enterprises, according to the Labour Force Survey for the first quarter of 2008. In fact, workers in companies with more than 250 employees rose by 4.3% in the past 12 months and 1.8% in the case of companies with 1-10 employees. On the other hand, in the case where there were 11-50 employees, the numbers were down by 1.9% while in those with 51-250 employees the drop was 0.8%.

Number of registered unemployed also up in May

The modest job creation in March was not sufficient to absorb those joining the labour force, which meant an increase in unemployment. This continues to be reflected in the figures for registered unemployed at public employment offices. In fact, the number of unemployed registered at those offices in May rose by 15,058 whereas normally this month records a decrease. The number of registered unemployed rose to 2,353,575, an increase of 19.3% compared with the same month last year. As a result, the number of unemployed continued to rise.

REGISTERED UNEMPLOYMENT BY SECTOR, SEX AND AGE

May 2008

	No. of unemployed	Change over December 2007		Change over same period year before		% share
		Absolute	%	Absolute	%	
By sector						
Agriculture	77,327	8,515	12.4	14,673	23.4	3.3
Industry	299,496	19,515	7.0	29,340	10.9	12.7
Construction	349,128	65,261	23.0	134,885	63.0	14.8
Services	1,397,851	113,601	8.8	196,227	16.3	59.4
First job	229,773	17,136	8.1	5,219	2.3	9.8
By sex						
Males	1,019,759	134,620	15.2	275,922	37.1	43.3
Females	1,333,816	89,408	7.2	104,422	8.5	56.7
By age						
Under 25 years	277,748	37,365	15.5	49,525	21.7	11.8
All other ages	2,075,827	186,663	9.9	330,819	19.0	88.2
TOTAL	**2,353,575**	**224,028**	**10.5**	**380,344**	**19.3**	**100.0**

SOURCE: INEM and own calculations.

Logically enough, the sector to suffer the worst effects of unemployment was construction. In this sector, the number of unemployed was up 63.0% in the past 12 months. In fact, no large economic sector was able to avoid an increase in unemployment. During the same period, unemployment went up to 16.3% in services and 10.9% in industry.

The increase in unemployment was also spread generally over the various national groups. The number of Spanish nationals registered as unemployed was up 15.4% while for foreign workers the rise was 67.2%.

In view of this situation, the government introduced an extraordinary plan covering aspects such as personal orientation, job training and entry into the labour force in order to increase hiring. This plan includes allowances for job search and increasing geographical mobility.

Sharp rise in labour costs

The increase in inflation in recent months is being passed through to labour costs. This is happening not only because of wage revision clauses, well established in Spain's labour market, given that the increases established in collective bargaining agreements before applying those clauses was 3.4% in the first quarter, above the 2.9% recorded in the first quarter of 2007.

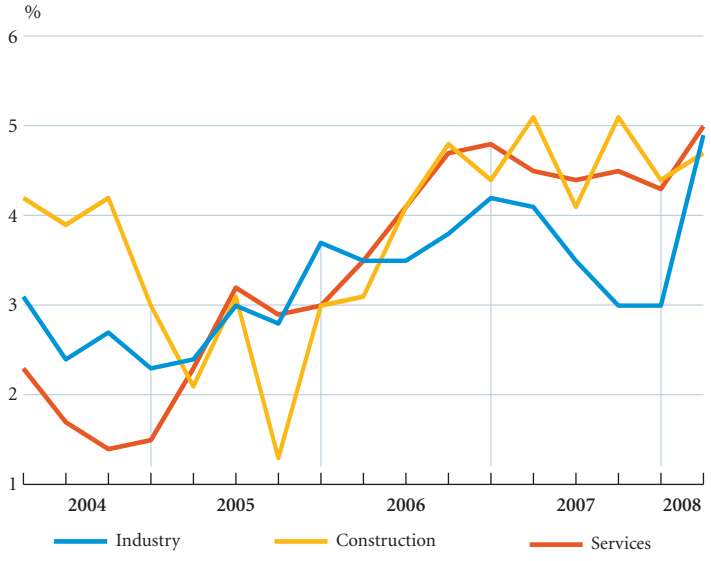
Labour costs of companies rose by 5.1% in the first quarter compared with the same period last year, according to the Quarterly Survey of Labour Costs carried out by the National Institute of Statistics. This was the biggest rise since the first quarter of 2003. Wage costs proper rose by 5.3% to 1,689.1 euros per worker per month on average. Non-wage costs, made up mainly of Social Security contributions, rose by 4.5%.

Unemployment among foreign workers in construction up more than 60% in past 12 months.

Increased inflation being passed through to labour costs.

WAGE PRESSURES IN INDUSTRY AND SERVICES

Year-on-year change in ordinary wage costs per worker



SOURCE: Quarterly Survey of Labour Costs and own calculations.

WAGE INDICATORS

Percentage change over same period year before

	2006	2007	2007			2008
			2Q	3Q	4Q	1Q
Increase under general wage agreements (*)	**3.3**	**3.1**	**2.9**	**2.9**	**3.1**	**3.4**
Wage per job equivalent to full-time work (**)	**3.0**	**3.6**	**3.4**	**3.5**	**3.8**	**3.9**
Quarterly labour cost survey						
Wage costs						
Total	3.4	3.9	3.8	3.8	3.7	5.3
Industry	*3.6*	*3.0*	*3.1*	*2.3*	*2.8*	*5.8*
Construction	*3.7*	*4.8*	*3.9*	*4.8*	*5.1*	*4.8*
Services	*3.7*	*4.2*	*4.3*	*4.2*	*3.8*	*5.1*
Average wages per hour worked	4.2	4.4	4.2	4.6	4.1	9.0
Other labour costs	3.6	4.4	4.0	5.2	5.3	4.5
Work day (***)	–0.6	–0.4	–0.3	–0.9	–0.3	–3.5
Farm wages	**2.8**	**3.1**	**2.5**	**3.3**	**3.5**	**4.6**
Labour cost in construction	**4.4**	**2.4**	**2.4**	**2.3**	**2.3**	**0.8**

NOTES: (*) Does not include wage revision clauses. Cumulative figures.
(**) Quarterly National Accounts: figures adjusted for seasonal and calendar differences.
(***) Effective hours worked per worker per month.
SOURCE: National Institute of Statistics, Ministry of Labour and Social Affairs, Ministry of Agriculture, Fishing and Food, Ministry of Public Works and own calculations.

By sector, ordinary wage costs, excluding overtime and back-pay, rose most in services which recorded a year-on-year change of 5.0%. In construction, where the increase was lower at 4.7%, it was still relatively high in view of the state of lower employment in the sector.

Biggest increase in company labour costs in past five years.

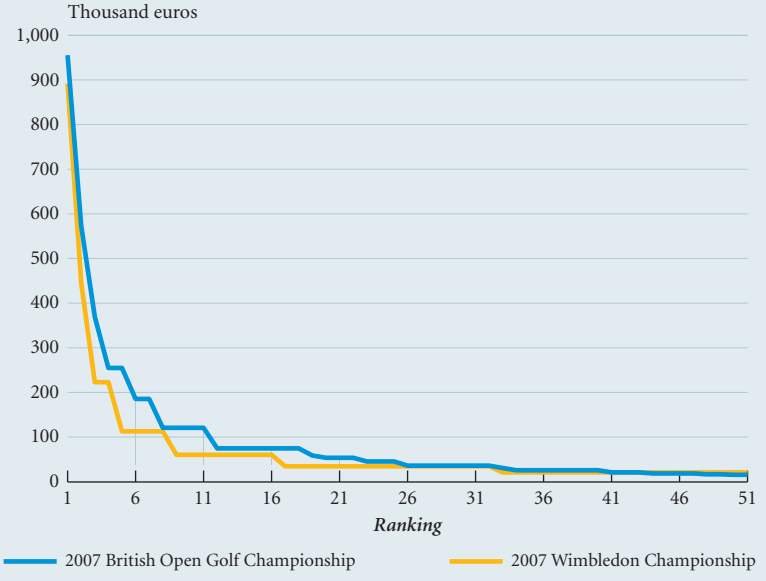
Winner take all

In 1980, the famous Swedish ABBA group gained much success with a song entitled «The Winner takes it All». While the song had a completely different context, the title sums up the method of payment in many sports events where the winner takes most of the prize money and the losers carry away little more than the crumbs. A large part of the interest generated by a sports match arises precisely due to this system of rewarding the participants based on the final classification of a competition. This system is also used in the world of business where, analogous to the sporting world, remuneration is decided by competition.

The reward formulas most widely used for employees are those where the worker is paid a fixed wage according to his/her individual output and where what the others produce does not affect his/her wage. In a competition, on the other hand, participants are classified according to results and this ranking determines final earnings. In this case, the comparison of rivals, and their production, decides what payment is made. Another distinguishing factor of the competition is that the champion receives a very substantial prize in relation to that going to the other participants. To sum up, the winner takes practically all. For example, in 2007, the winners of both the Wimbledon Tennis Championship and the British Open Golf Championship

FORTUNE IS SPLIT BETWEEN THE CHAMPIONS

Split in prizes between those participating in British Open Golf Championship and Wimbledon Championship



SOURCE: *The Open Championship Annual*, Carnoustie (2007) y www.wimbledon.org.

received close to a million euros, approximately double that of those who came second (see graph). Very likely, the differences in the quality of play and effort between the first and second runner did not justify the difference between the respective prizes. Similarly, in both competitions the prize for the best player was 70 times higher than that received by those who came at the tail-end. It is hard to see that the champion's play was worth all that.

The use of the match as a means of deciding on remuneration is not exclusive to the world of sport. For example, promotion to chief executive officer (CEO) of a company follows a similar pattern. All the vice presidents compete for the top post and it is customary to receive a major rise in salary when one reaches the lead spot in executive ranking. In the United States, a survey carried out among 200 large companies showed that such promotion meant a salary increase of 142%.

In general, a competition may be proper in those situations where it is simpler to establish the position of a player within a ranking than to measure his/her specific contribution to the spectacle. For example, a soccer match may show more or less clearly which team is playing best but it is difficult to quantify how much better that team has been. Something similar takes place in the business sphere where classifying all the possible candidates for CEO is easier than knowing what is his/her specific contribution to corporate profits.

On the other hand, if it were not for the champion's prize, competitors might not push themselves to the hilt. For example, while the likelihood of winning is increased by the effort made, players know that the more they push themselves the greater risk they run of being injured or of weakening. This situation, which in economic jargon is called increasing marginal costs to the allocation of effort, creates some predisposition to not push to the limit, a tendency that increases with the degree of difficulty of the «elimination trials». In addition, in the sporting events market, «demand» or the spectators at a match are looking for some special attraction, particularly the closer things are to the elimination that comes at the end. If the two opponents do not play at top level, the spectators may decide to leave the stadium or turn off their television sets before the game is over.

The risk of being injured and a demanding public make it essential that there be monetary incentives to stimulate a high level of effort right to the end and, in this way, obtain a stimulating level of play. When both adversaries do their utmost, the game is more even and perhaps it is decided only in the last few minutes who will carry off the victory. This is what sells. Only a very big difference in the pay going to the champion and the rival, the formula of «winner take all», can achieve the desired effect.

We have seen how in theory the use of the match attempts to stimulate the maximum effort by the players. Nevertheless, does this formula for payment mean that the players really go all out? In general, empirical studies would so indicate. A pioneer study was carried out on 45 golf tournaments held in the United States in 1984 in which, in spite of the fact that the total prize money was different in each tournament, the distribution of remuneration to participants in each competition was the same – 18% of the total went to the winner, 11% went to the second in line and 7% to the third runner. The other golfers received a relatively small prize, a lot less related to their position in the ranking. In keeping with the theory, the study showed the following: golf professionals made a greater effort (that is, they needed fewer drives to put the ball in the hole) in the biggest paying tournaments where the difference in winnings between first and second was more significant. Furthermore, the effort was especially greater in the final stages of the tournament. Other studies on tennis matches and car races have found the same kind of result. In one study, it was shown that drivers took more risk in those races where the differences in rewards between the best and worst classified were greater.

While, as we have seen, the match formula may be the most suitable for sporting events, this method of compensation is not without its disadvantages. In general, there are two problems – the risk of collusion or agreement between the participants and the temptation to sabotage the work of others.

How is it possible to resort to collusion between the finalists of a match? By way of illustration, let us imagine the end of a tennis match in which the recompense is set up as *winner take all.* The opponents know each other from earlier encounters and know that they have the same abilities. At the same time, they are aware that in spite of pushing themselves to the limit it could be the wind direction that determines the champion. In view of this situation, why not agree beforehand who is to be the winner, split the prize in half and save the expenditure of energy? While this is not usual, among other things because of the high risk of a breakdown in the agreement between the players, some examples have been known, especially in soccer games. In a recent case, known as the Calciopoli, a number of teams in the Italian league, such as Juventus, A.C. Milan, Florentina, Lazio and Regina, were sanctioned for having come to an agreement on the outcome. France went through a similar scandal in 1993 when an arrangement was discovered between the Olympique de Marseille and the Valenciennes.

As well as collusion, the match presents another risk, namely sabotage. The players are fully aware that what is important in terms of money is to win and this generates the incentive to prejudice the opponent and thus increase the likelihood of winning. Various cases have been known or suspected involving spying or tinkering with a rival's car in the world Formula One championships. An example of the former took place in the 2007 championships when McLaren was accused of spying on Ferrari and there were rumours of things done to prejudice the car of Fernando Alonso, one of the pilots. It is also suspected there were a number of times when a runner has caused an accident in order to disqualify an opponent from a race as when Michael Schumacher bumped into Damon Hill in 1994, which served to have him declared the champion. Three years later, Schumacher was disqualified for purposely bumping into Jacques Villeneuve in the last race of the championships held in Jerez. In that case, Villeneuve ended up winning the championship.

To sum up, in the world of sport, the dictum *winner take all* has its logic. This mechanism helps the players to push themselves to the limit right to the end of the championship. Only in that way can the spectator be kept fired up all through the event.

Prices

Oil again pushes up CPI

CPI stands at 4.6%, highest year-on-year rate since 1995.

The spell in inflation in April was short-lived. As expected, inflation of consumer prices rose in May but the sharpness of the increase was surprising. In fact, the year-on-year inflation rate for the general consumer price index (CPI) rose by four decimals to 4.6%, the highest level since 1995. In turn, the more stable core of inflation (known as underlying inflation that excludes fresh foods and energy products) turned around part of the drop in April to stand at 3.3%. As a result, the differential between general and underlying inflation widened to 1.4 points, the highest level since 1984.

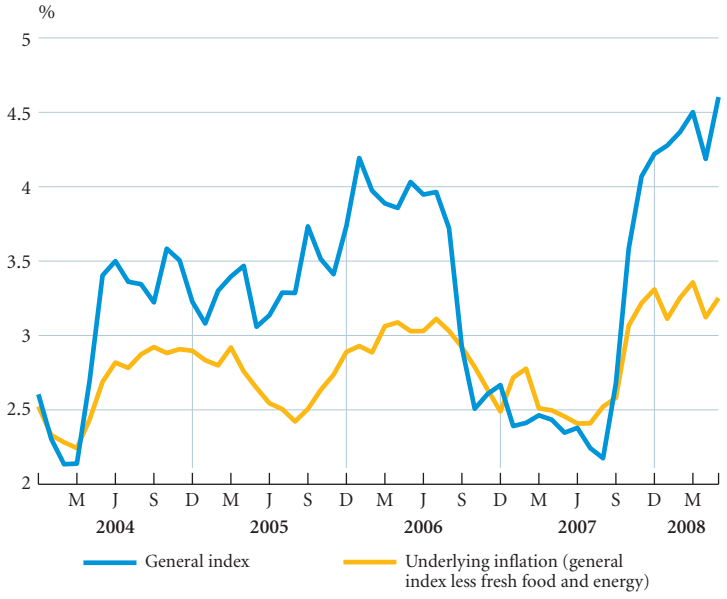
Gap between general inflation index and core inflation records highest level since 1984.

The rise in oil prices, which went to new records during the month, was the main culprit for the rise in consumer prices in May. In fact, fuels and lubricants rose by 6.5% that month, a bigger increase than that recorded in May 2007, so that the year-on-year change rate went up to 20.8%. The monthly rise in heating fuels, such as fuel-oil, was bigger at 9.8%. As a result, fuels and fuel-oils contributed more than three decimals to the increase in annual inflation in May.

On the other hand, upward pressure on food prices was much more moderate so that its contribution to the increase in inflation could practically be ignored. In fact, fresh food prices rose by 4.1% over

WIDENING GAP BETWEEN GENERAL INFLATION INDEX AND CORE INFLATION

Year-on-year change in CPI



SOURCE: National Institute of Statistics.

CONSUMER PRICE INDEX

	2007			2008		
	% monthly change	% change over December 2006	% annual change	% monthly change	% change over December 2007	% annual change
January	–0.7	–0.7	2.4	–0.6	–0.6	4.3
February	0.1	–0.6	2.4	0.2	–0.5	4.4
March	0.8	0.1	2.5	0.9	0.4	4.5
April	1.4	1.5	2.4	1.1	1.5	4.2
May	0.3	1.8	2.3	0.7	2.2	4.6
June	0.2	2.0	2.4			
July	–0.7	1.3	2.2			
August	0.1	1.4	2.2			
September	0.3	1.7	2.7			
October	1.3	3.0	3.6			
November	0.7	3.8	4.1			
December	0.4	4.2	4.2			

SOURCE: National Institute of Statistics.

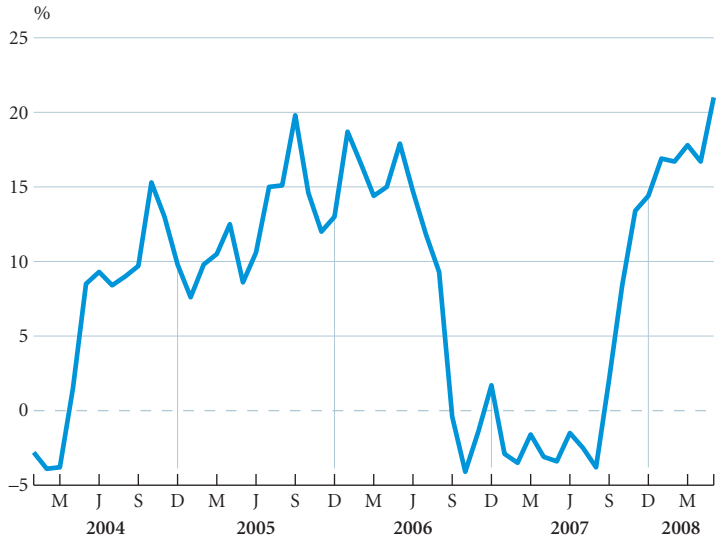
the past 12 months, one decimal more than in April. Inflation on poultry showed a decrease of 1.5 percentage points over the past year putting it at 3.9%. However, this was counteracted by moves in the opposite direction, such as the rise in pork to 2.0% and eggs to 13.0%.

The annual inflation rate for processed foods also rose by one decimal to 7.5%. The price of milk continued to drop

Rises in milk and bread ease but year-on-year rates hold at high levels.

FUELS AND FUEL-OILS MARK UP BIGGEST YEAR-ON-YEAR RISE SINCE 2000

Year-on-year change in prices of fuels and fuel-oils



SOURCE: National Institute of Statistics.

CONSUMER PRICE INDEX BY COMPONENT GROUP

May

	Indices (*)	% monthly change		% change over previous December		% annual change	
		2007	2008	2007	2008	2007	2008
By type of spending							
Food and non-alcoholic beverages	109.4	0.1	0.2	1.1	1.2	3.1	6.7
Alcoholic beverages and tobacco	111.3	0.1	0.1	5.5	3.5	6.2	4.1
Clothing and footwear	107.9	1.3	1.3	0.0	–0.4	1.1	0.8
Housing	110.1	0.2	0.7	2.7	4.4	3.0	6.6
Furnishings and household equipment	105.5	0.4	0.5	1.6	1.6	2.6	2.5
Health	98.1	0.2	–0.6	–2.8	–0.4	–2.1	0.4
Transport	111.0	1.0	2.5	4.1	5.3	0.5	8.4
Communications	100.3	–0.3	0.0	1.0	0.3	0.1	0.1
Recreation and culture	98.5	–0.8	0.1	–1.1	–0.9	–0.2	–0.6
Education	107.5	0.0	0.0	0.5	0.3	4.5	3.9
Restaurants and hotels	109.4	0.0	0.2	3.2	3.1	4.9	4.8
Other goods and services	106.6	0.1	0.1	2.4	2.6	3.4	3.2
By group							
Processed food, beverages and tobacco	110.3	0.2	0.2	2.1	2.3	2.3	7.5
Unprocessed food	108.0	0.0	0.1	0.5	–0.4	6.0	4.1
Non-food products	107.0	0.3	0.8	1.9	2.4	2.0	4.0
Industrial goods	106.7	0.7	1.4	1.5	2.5	0.1	4.2
Energy products	*118.4*	*1.5*	*4.3*	*5.3*	*10.1*	*–1.6*	*16.5*
Fuels and oils	*122.3*	*2.0*	*5.7*	*6.2*	*12.4*	*–3.4*	*21.0*
Industrial goods excluding energy products	*102.8*	*0.4*	*0.3*	*0.2*	*0.0*	*0.7*	*0.2*
Services	107.4	–0.1	0.2	2.3	2.3	4.0	3.8
Underlying inflation (**)	106.4	0.2	0.3	1.5	1.5	2.5	3.3
GENERAL INDEX	**107.7**	**0.3**	**0.7**	**1.8**	**2.2**	**2.3**	**4.6**

NOTES: (*) Base 2006 = 100.
(**) General index excluding energy products and unprocessed food.
SOURCE: National Institute of Statistics.

Inflation differential with Euro Area holds at one percentage point.

gradually thanks to imports although the year-on-year increase held at the high level of 24.8%. At the same time, the annual inflation rate dropped slightly to 10.9%. The price of sugar also showed a decrease to below the level 12 months earlier. Nevertheless, the year-on-year drop in potatoes was reduced to 8.0% and inflation on cooking oils and fats went up to 3.6%.

The upward contribution of services to inflation was of greater importance at one decimal. Nevertheless, this was mainly due to organized travel seeing that last year prices dropped in May because of the end of Easter Week whereas this year those holidays came earlier. At the same time, prices at hotels, cafés and restaurants rose by 4.8% in the past 12 months, three decimals more than in the month before.

In turn, annual inflation on industrial goods excluding energy products continued to be very moderate (0.2%), thanks to the strength of the euro and sharp competition in international markets. Also contributing was a monthly reduction of 2.2% in prices of medicines and other pharmaceutical products which increased their year-on-year drop to 6.0%.

The year-on-year change in the consumer price index harmonized with the European Union was 4.7%. Nevertheless, the inflation differential with the Euro Area held at one percentage point due to a similar rise in the Euro Area.

Because of more costly oil and other commodities inflation prospects for coming months have worsened. It is likely that the year-on-year change rate of the CPI will continue to rise in the summer going to around 5%, only to later ease so long as this is not stopped by oil prices.

Sharp increases in wholesale prices

The rise in prices of oil and other commodities in recent months has brought about inflationary pressures on wholesale prices. These increases have been passed through to consumer goods prices which have also reached the highest levels in recent years.

The year-on-year change rate for industrial prices rose to 7.9% in May. It thus marked up the highest level in the past 23 years. The increase in May was entirely due to energy products for which the year-on-year change rate rose to 21.2%.

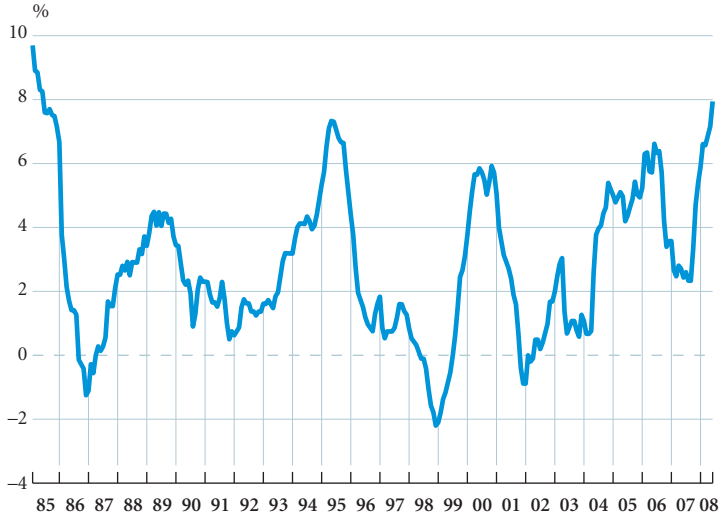
Thanks to the appreciation of the euro, the rise in prices of energy and imports had limited repercussions. In April, the year-on-year rate for the general price index for imports moved up two decimals to 6.6% although this put it two decimals below the January figure. Also due to pressure from sharp competition

Inflation prospects worsen for coming months.

Price increases in oil and other commodities push up wholesale prices.

INFLATION IN INDUSTRIAL PRICES MARKS UP HIGHEST LEVEL SINCE 1985

Year-on-year change rate in general industrial prices index



SOURCE: National Institute of Statistics.

INFLATION INDICATORS

Percentage change over same period year before

	Farm prices	Producer price index					Import prices				GDP deflactor (*)
		General index	Consumer goods	Capital goods	Intermediate goods	Energy goods	Total	Consumer goods	Capital goods	Intermediate goods	
2007											
March	1.5	2.8	1.7	3.3	6.3	–1.6	0.4	0.4	–0.3	7.2	–
April	6.7	2.7	2.2	3.1	6.5	–2.6	0.2	0.7	–0.1	6.3	–
May	0.4	2.4	2.0	3.3	6.0	–2.8	0.9	1.5	0.1	5.9	3.2
June	2.6	2.6	1.8	3.1	5.8	–1.4	1.3	0.9	–0.1	6.1	–
July	2.5	2.3	1.9	3.1	5.6	–2.6	0.7	0.9	–0.2	4.3	–
August	5.1	2.3	2.4	3.1	5.4	–2.9	0.7	1.4	0.3	3.8	2.9
September	12.1	3.4	3.2	3.2	5.4	0.8	2.0	1.0	0.2	3.0	–
October	13.8	4.7	4.2	3.2	5.3	6.1	3.0	0.6	0.0	2.0	–
November	15.7	5.4	4.5	3.1	5.1	9.8	4.0	0.7	–0.1	0.7	2.9
December	17.6	5.9	4.8	2.9	5.0	11.6	5.0	1.1	–0.2	0.7	–
2008											
January	11.1	6.6	5.4	2.7	5.9	13.3	6.8	1.1	0.5	1.8	–
February	7.3	6.6	5.4	2.5	6.0	13.3	6.7	1.4	0.3	1.9	3.1
March	10.5	6.9	5.5	2.3	6.3	14.6	6.4	0.8	–0.1	2.1	–
April	...	7.2	5.3	2.2	6.0	16.5	6.6	0.5	–0.1	2.5	–
May	...	7.9	5.3	2.0	5.9	21.2	...	...	...	...	...

NOTES: (*) Figures adjusted for seasonal and working days effects.
SOURCE: National Institute of Statistics, Ministry of Economy and own calculations.

Rise in farm prices at origin.

in world markets prices of imported consumer goods rose by only 0.5% in the past 12 months, three decimals less than in the month before, whereas capital goods prices held below the level of one year earlier.

Prices obtained by crop farmers bounced back in March to show a year-on-year change rate of 10.5%. On this occasion, the drive came largely from farm products with the increase in world prices as background.

Foreign sector

Oil adds to trade deficit

For the period between January and April 2008 the trade deficit amounted to 34.88 billion euros, which implies sharper increases in recent months. With regard to the export/import ratio, this stood at 65.2% in the first four months of the year, slightly below the 66.4% for the same period in 2007.

From the beginning of the second half of 2007 the sharp increase in the deficit in the energy trade balance has brought about a worsening of the overall trade deficit. For the last 12 months ending in April, the trade deficit was 103.85 billion euros, some 12.19 billion euros more than one year earlier. Of this increase, 7.76 billion euros (nearly two-thirds) was due to the energy sector. We should add that, while the energy balance keeps getting worse, the growth of the non-energy deficit is rapidly weakening. In this respect, in the first four months of 2008 the non-energy deficit was 18.18

Trade deficit up 16% because of worse energy balance.

FOREIGN TRADE

January-April 2008

	Imports			Exports			Balance	Export/ Import rate (%)
	Million euros	% annual change by value	% share	Million euros	% annual change by value	% share	Million euros	
By product group								
Energy products	20,159	62.8	20.1	3,461	64.0	5.3	–16,698	17.2
Consumer goods	23,936	–2.6	23.9	24,067	8.9	36.8	131	100.5
Food	*5,048*	*6.8*	*5.0*	*7,894*	*6.9*	*12.1*	*2,845*	*156.4*
Non-foods	*18,888*	*–5.3*	*18.8*	*16,174*	*5.9*	*24.7*	*–2,714*	*85.6*
Capital goods	8,821	–9.4	8.8	5,329	–1.4	8.1	–3,492	60.4
Non-energy intermediate goods	47,356	10.6	47.2	32,538	8.8	49.8	–14,818	68.7
By geographical area								
European Union	56,100	4.9	55.9	46,726	9.2	71.5	–9,374	83.3
Euro area	*46,823*	*4.3*	*46.7*	*37,196*	*7.6*	*56.9*	*–9,627*	*79.4*
Other countries	44,171	22.6	44.1	18,669	11.5	28.5	–25,502	42.3
Russia	*3,262*	*22.2*	*3.3*	*883*	*49.8*	*1.4*	*–2,379*	*27.1*
United States	*3,981*	*27.5*	*4.0*	*2,420*	*–0.5*	*3.7*	*–1,561*	*60.8*
Japan	*2,047*	*–1.7*	*2.0*	*466*	*5.8*	*0.7*	*–1,581*	*22.8*
Latin America	*4,828*	*5.9*	*4.8*	*2,902*	*–14.7*	*4.4*	*–1,926*	*60.1*
OPEC	*9,126*	*37.4*	*9.1*	*1,957*	*18.5*	*3.0*	*–7,170*	*21.4*
Rest	*20,928*	*22.3*	*20.9*	*10,042*	*22.1*	*15.4*	*–10,886*	*48.0*
TOTAL	**100,272**	**12.0**	**100.0**	**65,395**	**9.9**	**100.0**	**–34,877**	**65.2**

SOURCE: Department of Customs and Special Taxes and own calculations.

Non-energy deficit down but fails to compensate increased cost of oil.

billion dollars, down by 1.52 billion dollars from the same period in 2007.

In April, exports of goods grew by 22.7% compared with the same month in 2007 while imports were up 13.0%. By sector, the strongest product groups among exports was energy goods which, in spite of representing 5.9% of exports, showed an increase of 82.7% compared with the same period last year. Sectors with greater weight, such as cars and capital goods, also showed increases of 24.9% and 16.7% respectively, while the chemical sector was up 32.3%. With regard to imports, energy products (19.3% of the total) grew by 59.5%. Chemical products and foods also recorded major increases.

Trade deficit increases and current account balance worsens sharply.

Finally, the recent trend in foreign markets remains on a similar track. In April, the European Union (EU) continued to be the Spanish economy's trade partner of reference as the destination of 68.5% of Spain's exports and the origin of 57.6% of its purchases abroad. Nevertheless, exports to Asia showed up very strong with growth of 35.9% while those to Africa grew by 37.4%. Imports from Asia (16.2% of the total) were up by 19.1% while that from Africa (at 9.6% of the total) rose by 85.2%.

Incomes balance and transfers balance growing less.

Balance of payments: current account deficit grows sharply

The current account balance recorded a deficit of 12.05 billion euros in March, a level 64.8% higher than in the same period last year. The increase in the current account imbalance was four-fifths due to the bigger deficit in the incomes balance and the trade balance (each with a similar contribution). The rest was due to the increased deficit in the current transfers balance.

In order to evaluate the above results over a longer time span, it is necessary to show the trend in cumulative figures for 12 months which makes it possible to make a better appreciation of the various trends. At first sight, we note that, since the second half of 2007, the current account imbalance again increased growth thus breaking with the tendency to more moderate increases over the past two years. In the 12 months ending in March, the current account deficit grew by 21.9% year-on-year, a rate higher than that over the past five months due to the sharper worsening of the trade balance, which is not unconnected to oil prices.

Showing a different profile, the deficits in the incomes balance and the transfers balance, while still growing, reported less of a worsening. In the 12 months ending in March, the combined deficit of these two headings went from 30.20 million euros to 40.05 million euros, an increase of 9.85 million euros, which is 25% lower than the increases in the second half of 2007.

Net portfolio investment inflows down to a fifth of highs seen at end of 2006.

With regard to financial flows, the most notable factor, in terms of the cumulative figure for 12 months, was the decrease in the balance of portfolio investment which, with net inflows of 38.64 billion euros, was practically half the figure for the month before, thus showing only a fifth of the highs reached at the end of 2006 and the beginning of 2007. In turn, in spite of a rise in March, net direct investment continued to show a trend to gradual decrease, more because of the easing of outflows than for any increase in inflows.

BALANCE OF PAYMENTS

March 2008

	Cumulative for year		Last 12 months		
	Balance in million euros	% annual change	Balance in million euros	Annual change	
				Absolute	%
Current account balance					
Trade balance	–24,450	23.3	–94,434	–10,618	12.7
Services					
Tourism	*4,900*	*5.6*	*28,070*	*526*	*1.9*
Other services	*–1,262*	*–21.5*	*–5,336*	*–137*	*2.6*
Total	3,639	20.0	22,734	389	1.7
Income	–7,676	7.2	–31,953	–7,996	33.4
Transfers	–4,064	51.1	–8,101	–1,854	29.7
Total	**–32,552**	**22.2**	**–111,753**	**–20,079**	**21.9**
Capital account	**2,080**	**88.3**	**5,467**	**–953**	**–14.8**
Financial balance					
Direct investment	–2,658	–68.9	–42,503	–5,885	16.1
Portfolio investment	–13,057	–	38,639	–166,508	–81.2
Other investment	45,374	–	87,833	152,329	–
Total	**29,659**	**0.7**	**83,970**	**–20,064**	**–19.3**
Errors and omissions	1,972	4.8	3,346	999	42.6
Change in assets of Bank of Spain	–1,160	–80.0	18,971	40,098	–

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 own calculations.

Public sector

Central government surplus down 80% as of May

Direct tax collections up less than nominal GDP.

The economic slowdown is having a sharp effect on central government accounts. In the January-May period, the central government's non-financial revenues were down 4.0% before amounts ceded to autonomous governments and local authorities under the present financing system. This is in contrast to the sharp growth recorded in the same period in 2007.

Direct tax collections rose by only 3.3% compared with the same period last year, a rate lower than that of the nominal gross domestic product (GDP) and even lower than inflation. With regard to spending, cumulative current spending was up 6.6% compared with the same period in 2007.

Surplus drops to 0.2% of GDP.

As a result of the outcome of central government revenue and spending, the surplus in terms of National Accounting, that is, taking into account rights and obligations acquired rather than actual cash flows, amounted to 2.72 billion euros. This figure meant a drop of 80.0% compared with that recorded in the same period in 2007. At the same time, in terms of GDP, the central government surplus for the first five months of the year was 0.24%, some 1.05 points less than that recorded in the same period last year.

CENTRAL GOVERNMENT BUDGETARY IMPLEMENTATION

May 2008

	Month		Cumulative for year	
	Million euros	% change over same month year before	Million euros	% change over same month year before
Non-financial revenue	**3,677**	**7.4**	**59,923**	**–8.5**
Non-financial revenue adjusted (*)				
Personal income tax	2,086	19.5	32,442	9.8
Corporate tax	3,539	641.9	6,752	–19.7
VAT	–780	–	26,299	–17.8
Special taxes	1,625	5.8	7,977	2.5
Other	1,713	–9.1	8,975	10.5
Total	**8,183**	**9.3**	**82,445**	**–4.0**
Non-financial spending	**8,867**	**1.8**	**56,737**	**4.5**
Treasury balance	**–5,190**	**–1.8**	**3,186**	**–71.6**
Surplus (+) or deficit (–) (**)	***–6,185***	***–6.0***	***2,722***	***–80.0***

NOTES: (*) Includes tax segments ceded to regional and local governments under current financing system.
(**) In terms of National Accounting.
SOURCE: Ministry of Economy and Finance and own calculations.

The effect of the Olympic flame on the economy

In less than one month, our television sets will bring us the first broadcast images of the opening ceremony of the XXIX Olympic Games in Beijing. Those scenes will remind us of the vast range of emotions we experienced in Barcelona 16 years ago and that we soon hope to relive in Madrid. Sixteen will also be the number of days the Olympic flame will illuminate the fortunate Chinese city and spotlight more than 10,000 athletes meeting there. What is the attraction power of that longed-for Olympic flame so much sought after by so many cities?

Those cities that most seek the Games do not hesitate in declaring their many economic virtues, among which the most outstanding is their potential for boosting the economy of the organizing city and country, partly through public investment. Barcelona'92 is a clear example of the boost effect of the Olympic Games. Between 1986 and 1992 the direct economic impact of the Games was more than 7 billion euros (at current prices for those years), which represented on average approximately 0.3% of Spain's annual GDP at that time (see following Table). If we add to this the multiplier effect of those investments, also known as the induced impact, the total economic impact of Barcelona'92 was 18 billion euros, or 0.75% of annual GDP during a period of seven years. To this we may add the public excitement generated by the organization of an event of this magnitude, undoubtedly an important factor that goes far beyond the economic sphere. Nevertheless, there are those who emphasize the huge deficit the Olympic flame has left behind in some cities, such as Montreal, which had to carry a heavy financial burden following the 1976 Games. While there are major benefits of various kinds, we should not overlook the fact that the Olympic Games also involve costs.

Let us begin with the most obvious. The city hosting the Games must have the necessary facilities needed for the 28 different contests and be able to house the huge number of participants, support personnel, journalists and tourists. Furthermore, it is important to have rapid and efficient movement across the city. All of this demands investment in pavilions, competition areas, housing, improvements in roads and transportation, among many other matters. Many people see these investments as being very positive as they create jobs and thus drive the country's economy, even if this means increasing the public debt. Nevertheless, sooner or later, that increased debt load must be faced and it is therefore essential that those investments not only bring benefits during the Games through ticket sales, television rights and tourism but also spread into the future.

ECONOMIC IMPACT OF BARCELONA '92 OLYMPIC GAMES

	Million current euros	% cumulative GDP 1986-1992
Direct impact	7,005	0.28%
Investment in infrastructures	5,749	
Organization costs	979	
Tourist consumption	277	
Induced impact	11,673	0.47%
Total impact	**18,678**	**0.75%**

NOTES: Effects spread over 1986-1992 period.

SOURCE: Eurostat and Brunet, Ferran (1995), *An economic analysis of the Barcelona'92: resources, financing and impact*, Barcelona: Centre d'Estudis Olímpics UAB.

Athens, for example, built 22 sports pavilions and today, scarcely four years later, 21 of those have been abandoned and are in serious need of repair. London seems to have taken note of the Greek experience and plans to combine the construction of new facilities (some of a permanent nature, others of temporary kind and much more economical) with the use of sports facilities already in existence. This mix of temporary facilities (to be pulled down after the Games) and those of a permanent nature may be ideal if we take into account that sports such as baseball and handball are never going to enjoy the success of soccer or rugby in the United Kingdom so that it would be difficult to make such facilities profitable after the Games. In turn, the permanent infrastructures may be made use of by other international events to be held in the future, as well as be available for local athletes or ordinary citizens, thus encouraging a healthy lifestyle.

The benefits the Games may bring to fostering sport as an essential aspect of modern life is not something to be taken lightly. This is especially true in Spain where the rate of child obesity is among the highest in the world. Nearly 14% of young people in Spain suffer from obesity problems, not far behind the United Kingdom with 17% or the United States which heads the list with 22%.[1] Health costs arising from this problem may be considerable in the not too distant future so that a small dose of the Olympic spirit will not go amiss.

A COST-BENEFIT ANALYSIS OF THE OLYMPIC GAMES: NOT AN EASY TASK

Costs	Benefits
• Construction of pavilions	• Ticket sales
• Improvements in transportation and city areas	• Television rights
• Security	• Future use of facilities and improvements
• Administration	• Tourism
• Congestion	• Attraction of foreign investment
• Opening and closing ceremonies	• Reduction of future pollution
	• Healthier life for citizens

SOURCE: Own calculations.

Apart from the construction of stadiums and pavilions, the investment in other infrastructures (public transportation, road communications, renovation of run-down urban areas) no doubt improves the quality of life of the ordinary citizen and makes the city more attractive to tourists. Nevertheless, those opposed to these huge events argue (often correctly) that, if those improvements are so beneficial to the citizenry, why have they not been made already? While it is logical to suppose that the most profitable project is the first to be carried out, it is also true that the funds available to a city are fairly limited as well its ability to go into debt. For this reason, some projects are not carried out for lack of funds or must be put off until the city has saved enough money. The choice of a location for the Olympic Games, however, increases a city's access to funding to carry out many of these projects.

Other benefits of organizing the Olympic Games are gains from tourism. The holding of the Games serves on a silver platter the opportunity of promoting the beauty, cultural heritage and city environment among new tourists. The most immediate objective is the Olympic Games tourist who enjoys sport while taking advantage of the Games to see some of the world. But, the true objective is the tourist who may be induced to visit the

(1) "la Caixa" Foundation (2008), *«Alimentación, consumo y salud»*, Volume 24, Research Department Series.

city in the future after the Games have aroused interest. In the case of Sydney, tourism has grown considerably since 2000, much more rapidly than in the years before the Games. Nevertheless, on speaking of tourism we should not forget that, while there are Olympic Games tourists, there is another type of tourist that would have visited the site or the area and may choose another destination put off by the high prices and crowds typical of an Olympic city, thus creating an effect known as «crowding out». This effect may explain why there was a drop in tourism on the Costa Brava in the summer of 1992.

In the case of Beijing, many people feel that the benefits to be derived from the promotion of the city and the country in general may be considerable although not so much from a tourism point of view as from the business sphere. Countless multinationals from around the world will be there to act as sponsors, thus providing the Asian giant with an unbeatable opportunity to show off its capacity for work and organization. For this reason, hosting the Olympic Games may be a golden opportunity to attract new foreign direct investment, highly beneficial for the host economy.

Another benefit the Olympic Games may bring Beijing, in this case perhaps of a more specific nature, is the promotion of new measures to halt the troubling pollution levels. The Games have fostered the collaboration of the Chinese government and various international agencies in order to find solutions to stop serious deterioration of the environment.

In a nutshell, organizing the Olympic Games is quite a challenge but planning its financing for the day after may be even harder. The organizers of the Games must carefully choose those investments that may turn out most suitable for the city's potential and the needs of its population. This will help to give the Olympic flame a beneficial effect on the economy both over the short and long term.

Savings and financing

Financing granted to private sector on downturn

Hardening of position of European Central Bank and lack of trust in interbank market push 1-year Euribor to record level.

The hardening of the position of the European Central Bank in view of increased inflation in the Euro Area, along with the continuing lack of confidence existing in financial markets, sent the 12-month Euribor (widely used as a reference rate) to all-time highs in June when it went to 5.4%. In May it had reached 5.0% on monthly average, the highest level since 2000.

Differential with Euro Area in growth of credit granted to companies and households down substantially.

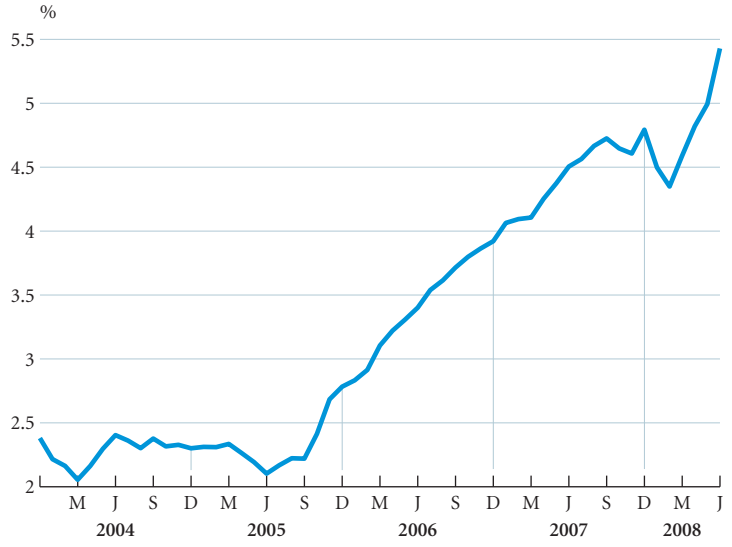
In this context of rising interbank interest rates since March, interest rates on loans and credits to companies moved up somewhat in April. As a result, the monthly average stood at 5.8%, slightly higher than at the end of 2007.

In this situation of increasing interest rates and a slowing down of economic activity, demand from the private sector for financing continued to progressively lose strength. In April, the year-on-year change rate stood at 12.1%, half that at the end of 2006. As a result, the differential with the Euro Area in growth of credit to companies and households was down substantially. The slowdown in financing was more marked in the case of companies than for households in the most recent period although the year-on-year increase continued to be higher in the former case (13.5%) as against 10.3% for the latter.

Under funding for companies, commercial credit for financing working capital continued to show signs of

EURIBOR MARKS UP RECORD HIGH

12-month Euribor



NOTES: On June 25.
SOURCE: Bank of Spain.

CREDIT GRANTED TO COMPANIES AND HOUSEHOLDS

April 2008

	Total	Change this year		Change over 12 months		% share
	Million euros	Million euros	%	Million euros	%	
Commercial credit	84,646	–6,196	–6.8	1,888	2.3	4.7
Secured loans (*)	1,089,526	21,153	2.0	110,584	11.3	60.5
Other term loans	511,974	14,091	2.8	69,011	15.6	28.4
Demand loans	42,461	1,889	4.7	8,281	24.2	2.4
Leasing	46,911	618	1.3	4,617	10.9	2.6
Doubtful loans	24,746	8,496	52.3	12,692	105.3	1.4
TOTAL	**1,800,264**	**40,051**	**2.3**	**207,073**	**13.0**	**100.0**

NOTES : (*) Greater part made up of loans with mortgage security.
SOURCE: Bank of Spain and own calculations.

weakness with growth of only 2.3% in the past 12 months ending in April. Leasing, used for financing investment, showed a better picture with an increase of 10.9% in the past year although this rate was substantially lower than the 17.3% recorded five months earlier.

By sector, based on figures up to the end of the first quarter, we note a widespread drop in credit, except in industry. Credit granted to industrial branches was up 18.7% compared with the first quarter in 2007, slightly above December. The year-on-year growth in credit granted to the

Annual increase in loans for real estate and construction purposes down by half.

CREDIT TO PRIVATE SECTOR BY PURPOSE

First quarter of 2008

	Balance (*)	Change this year		Change over 12 months	
	Million euros	Million euros	%	Million euros	%
Financing of production activities					
Agriculture, livestock raising and fishing	25,003	–242	–1.0	1,567	6.7
Industry	143,816	2,245	1.6	22,668	18.7
Construction	154,237	784	0.5	16,401	11.9
Services	639,277	16,460	2.6	105,599	19.8
Total	**962,333**	**19,247**	**2.0**	**146,235**	**17.9**
Financing to individuals					
Acquisition and renovation of own home	628,482	10,271	1.7	62,142	11.0
Acquisition of consumer durables	57,357	781	1.4	4,644	8.8
Other financing	114,724	262	0.2	7,599	7.1
Total	**800,564**	**11,314**	**1.4**	**74,385**	**10.2**
Financing to private non-profit institutions	**5,804**	**–285**	**–4.7**	**61**	**1.1**
Other unclassified	**22,978**	**1,190**	**5.5**	**1,829**	**8.6**
TOTAL	**1,791,679**	**31,466**	**1.8**	**222,510**	**14.2**

NOTES: (*) By credit institutions as a whole: banking system, loan finance establishments and official credit.
SOURCE: Bank of Spain and own calculations.

Default on increase but still holding at low levels.

services sector was up (19.8%) but showed clear signs of slowing down. This was to be seen in real estate activities for which the annual growth rate was down by half over the last six months, going to 17.6%. In any case, quarterly growth was 2.6%, higher than production activities as a whole. At the same time, credit granted to construction, which was growing at a year-on-year rate of 24.4% in June 2007, went to less than half that figure nine months later.

With regard to funding granted to households, growth of loans for home purchase continued to slacken going to am year-on-year rate of 10.7%, some 2.5 points less than in December 2007. The high prices reached in the market, tougher financing terms and worsening of the labour market were among the main causes of this result.

On the other hand, credit for buying consumer durables slackened off to an annual change rate of 8.8%. This slowdown is in line with the drop in consumer confidence and some hardening of sales conditions.

In turn, the default rate continued to rise going to 1.4% in April for lending institutions as a whole. The default rate for home purchase with mortgage stood at a lower rate, namely 1.0% at the end of March. In spite of the increase in recent months, the default rate at Spanish financial institutions stands at relatively low levels, lower than in the rest of Europe. Furthermore, Spain's financial institutions have a substantial cushion to cover possible failure to pay.

Gap with Euro Area in growth of bank deposits now closed

The slump in economic activity has also affected the situation in bank deposits. These have shown a sharp decline in recent months going from an increase in annual rate of 25.2% in April 2007 to less than half that in April this year, namely 10.1%. As a result, the gap in growth of bank deposits between Spain and the Euro Area has now been closed.

Drop in economic activity affecting trend in bank deposits.

In spite of this slowdown, time deposits, which provide the highest returns, are

DEPOSITS OF COMPANIES AND HOUSEHOLDS AT CREDIT INSTITUTIONS

April 2008

	Total	Change this year		Change over 12 months		% share
	Million euros	Million euros	%	Million euros	%	
On-demand savings (*)	409,053	–29,004	–6.6	–17,501	–4.1	30.7
Up to 2 years	411,211	58,505	16.6	127,861	45.1	30.9
More than 2-year term	398,250	–3,724	–0.9	21,451	5.7	29.9
Repos	74,588	–11,004	–12.9	–8,315	–10.0	5.6
Total	**1,293,102**	**14,773**	**1.2**	**123,496**	**10.6**	**97.0**
Deposits in currencies other than euro	**39,379**	**–4,465**	**–10.2**	**–1,170**	**–2.9**	**3.0**
TOTAL	**1,332,481**	**10,308**	**0.8**	**122,326**	**10.1**	**100.0**

NOTES: (*) Includes deposits redeemable at notice, according to ECB definition.
SOURCE: Bank of Spain and own calculations.

maintaining their attraction for savers with aversion to risk, in view of the situation in other assets such as equity shares or the real estate market. Time deposits for up to two years thus showed a strong boost with an annual increase of 45.1%. On the other hand, total figures for on-demand and savings accounts, providing low returns, showed further decreases. Deposits in foreign currency were also down, given the unfavourable differentials in interest rates in terms of the euro.

Time deposits more attractive given situation in other assets.

Competition for deposits and the instability of financial markets continued to have an unfavourable effect on another financial product, namely mutual funds. Assets of these funds in May dropped by 4.32 billion euros to stand at 210.53 billion euros, some 19.4% lower than one year earlier. This decrease was almost entirely due to net withdrawals by participants totalling 4.21 billion euros that month. As a result, the drain continued with a total of 23.25 billion euros in the first five months of the year. This affected all categories with the exception of guaranteed bond-based funds, which clearly shows the conservative preferences of savers in a volatile environment.

Average yield on funds over the past 12 months ending in May was negative (–1.9%). Nevertheless, the spread in yields was very great, running from 8.2% for emerging country share-based funds to capital losses of 21.2% for Japanese share-based funds. In addition, over the past 17 years average annual return was 4.5%, a figure above inflation in that period.

On the other hand, hedge fund assets continued to rise. At the end of May these amounted to 1.29 billion euros, which means a considerable increase over the figure of 818 million at the close of 2007. Nevertheless, we should keep in mind that the development of this product in the Spanish market is still at an early stage.

Net withdrawals of mutual fund participations continue.

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"la Caixa" GROUP: KEY FIGURES

As of December 31, 2007

FINANCIAL ACTIVITY	Million euros
Total customer funds	223,850
Receivable from customers	161,789
Profit attributable to Group	2,488

STAFF, BRANCHES AND MEANS OF PAYMENT	
Staff	26,342
Branches	5,480
Self-service terminals	8,011
Cards	9,809,909

COMMUNITY PROJECTS: BUDGET FOR ACTIVITIES IN 2008	Million euros
Social	306
Science and environmental	83
Cultural	79
Educational	32
TOTAL BUDGET	**500**

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