KINGDOM OF SPAIN

Rating Analysis - 6/30/16

*EJR Sen Rating(Curr/Prj) BBB+/ BBB+
*EJR CP Rating: A1
EJR's 3 yr. Default Probability: 1.8%

Structural reforms in banking, pensions and labor markets have contributed to a robust recovery of the Spanish economy. GDP growth accelerated from -1.9% in 2012 to 2.1% in 2015, largely on account of a steady growth in private consumption and a revival of investment. However, the government deficits have resulted in rising debt levels. Debt-to-GDP was 99% in 2015 compared to 84% in 2012 - not particularly reassuring, especially as it is projected to expand further in the medium term.

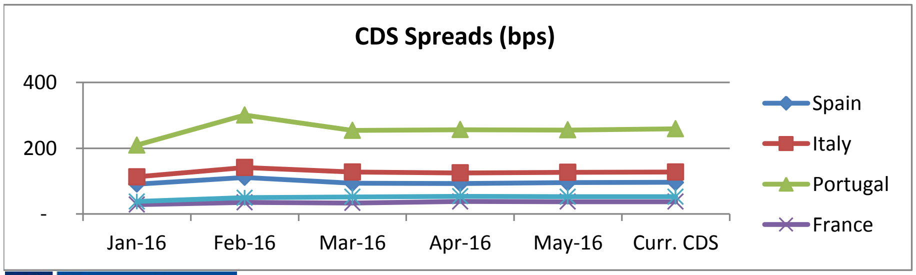
On the political side, the current parliamentary fragmentation is worrisome as it puts at risk the reform agenda that underlies the on-going recovery. On the other hand, the new round of tax cuts that Mr. Mariano Rajoy promised in an effort to court voters might not spur growth. Weakness in the banking sector and high level of unemployment remain sources of downside risk. Upgrading to "BBB+". Note, to reflect the propensity of central banks to support sovereign obligors, we have eased our indicative credit ratios, resulting in some upgrades.

Annual Ratios (source for past results: IMF)

CREDIT POSITION	2013	2014	2015	P2016	P2017	P2018
Debt/ GDP (%)	92.1	97.7	99.2	104.3	108.5	112.1
Govt. Sur/Def to GDP (%)	-7.2	-6.3	-5.3	-4.6	-3.8	-3.0
Adjusted Debt/GDP (%)	92.1	97.7	99.2	104.3	108.5	112.1
Interest Expense/ Taxes (%)	15.4	15.3	13.7	13.6	13.6	13.5
GDP Growth (%)	-0.6	0.9	2.1	2.5	2.5	2.3
Foreign Reserves/Debt (%)	2.4	2.7	3.3	3.1	2.9	2.7
Implied Sen. Rating	A-	A	A	A	A	A-

INDICATIVE CREDIT RATIOS	AA	A	BBB	BB	B	CCC
Debt/ GDP (%)	100.0	115.0	130.0	145.0	170.0	200.0
Govt. Sur/Def to GDP (%)	2.5	0.5	-2.0	-5.0	-8.0	-10.0
Adjusted Debt/GDP (%)	95.0	110.0	125.0	140.0	160.0	190.0
Interest Expense/ Taxes (%)	9.0	12.0	15.0	22.0	26.0	35.0
GDP Growth (%)	3.5	3.0	2.0	1.0	-1.0	-5.0
Foreign Reserves/Debt (%)	3.0	2.5	2.0	1.5	1.0	0.5

PEER RATIOS	Other NRSRO Sen.	Debt as a % GDP	Govt. Surp. Def to GDP (%)	Adjusted Debt/ GDP	Interest Expense/ Taxes %	GDP Growth (%)	Ratio-Implied Rating*
Federal Republic Of Germany	AAA	71.2	0.6	71.2	7.0	4.1	AA+
French Republic	AA	96.0	-3.4	96.0	7.0	2.4	A+
Kingdom Of Belgium	AA	106.0	-2.6	106.0	9.6	1.9	A
Republic Of Italy	BBB-	132.9	-3.0	132.9	13.9	1.1	BBB-
Portugal Republic	BB+	129.0	-5.1	129.0	18.0	3.4	BBB



Country	CDS
Spain	96
Italy	128
Portugal	259
France	37
Belgium	53

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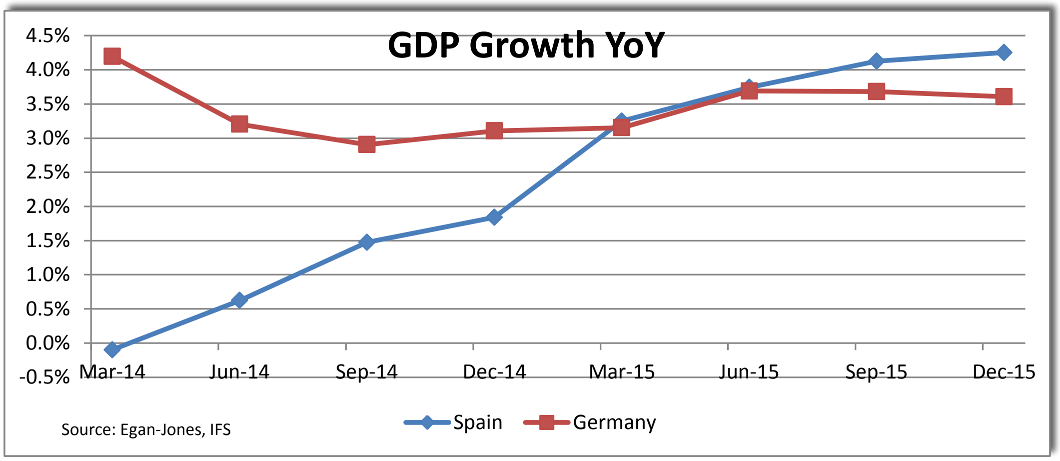
Economic Growth

Spain has been leading other EU countries in growth since 2015, with nominal GDP expanding at 4.25% for the fourth quarter of 2015, surpassing that of Germany. A key driver was the robust recovery of private consumption, followed by growth in investment. On the other hand, government spending has reported a minimal increase, suggesting that public debt is contained.

Another factor to consider is the implementation of structural reforms, which has been favorably contributing to growth, but is likely to be undermined if the current political deadlock persists after the June election, or if the emerging administration overturns the reforms of the previous government.



Fiscal Policy

Spain's deficit-to-GDP of 5.32% is not particularly comforting. As can be seen from the chart to the right, Spain has the worst deficit compared to its peers. However, improvements have been shown as the budget deficit narrowed from 10.4% of GDP in 2012 to 5.3% in 2015. Government revenue is growing at an annualized rate of 1.9% from 2012 to 2015, whereas expenditure is decreasing at 2.1% for the same period, owing to the recovery of the private sector that necessitates minimal fiscal stimulus and lowers unemployment.

	Surplus-to-GDP (%)	Debt-to-GDP (%)	5 Yr. CDS Spreads
Spain	-5.32	99.17	96.06
Germany	0.59	71.22	19.80
France	-3.40	95.96	37.34
Belgium	-2.62	105.96	52.60
Italy	-2.96	132.89	127.50
Portugal	-5.10	128.97	259.08

Sources: Thomson Reuters and IFS

Unemployment

Unemployment has been a scourge on the country. The 2015 statistics came in at 22.1%, which, despite signs of improvement as compared to 24.5% in 2014, is still the second highest in the Eurozone. We expect several factors to continue to alleviate the unemployment condition, including the growth of the services sectors and the potential tax cuts promised by Marioano Rajoy, assuming his re-election.

Unemployment (%)	2014	2015
Spain	24.50	22.10
Germany	6.70	6.01
France	10.30	10.40
Belgium	8.50	8.50
Italy	12.65	11.89
Portugal	14.10	12.60

Source: Intl. Finance Statistics

Banking Sector

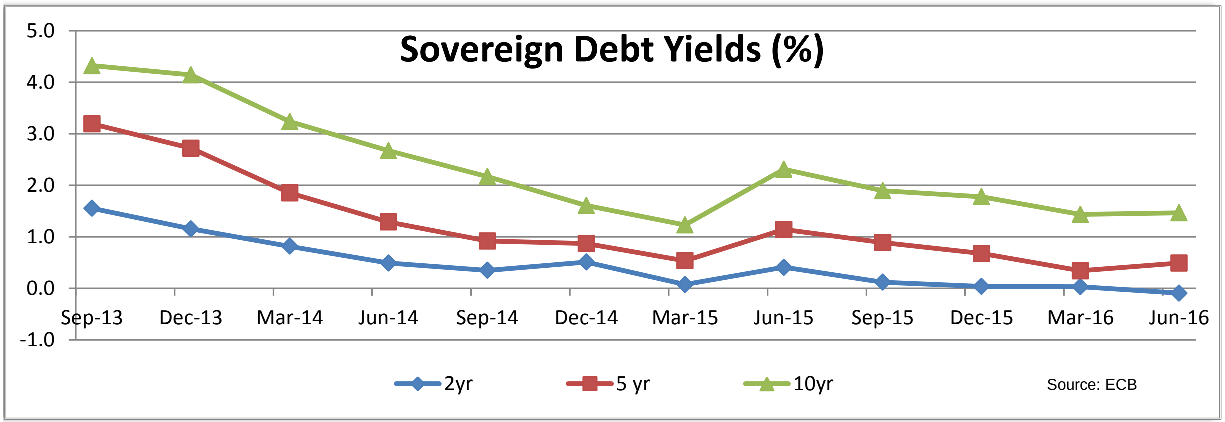
The banking sector required a bailout of $100 billion in 2012, but has coped well since. According to an ECB review in 2014, capital and earnings are improving along with the asset quality. However, given the significant size of the banks' balance sheet (top five account for 264% of GDP), substantial risks remain in the sector concerning profitability pressures and high (albeit declining) level of non-performing loans.

Bank Assets (billions of local currency)

	Assets	Cap/ Assets %
BANCO SANTANDER	1340.26	4.35
BBVA	750.08	4.91
CaixaBank	344.26	4.11
Bankia	206.97	4.23
Banko de Sabadell	208.63	4.00
Total	2,850.2	
EJR's est. of cap shortfall at 10% of assets less market cap		158.6
Spain's GDP		1,081.2

Funding Costs

As can been seen in the graph below, the bond yields have seen a steady decline since 2013, except for a hiccup in June 2015 when the Greek crisis stirred European markets. 10-year sovereign debt yield dropped from 4.3% in September 2013 to 1.5% in June 2016, and is likely to drop further as the negative yields in one-third of the existing Eurozone sovereign bond market drive investors elsewhere.



Ease of Doing Business

Major factors for growing the economy are the ease of doing business and the economic freedom; although not the sole factor for determining economic growth, a country which makes it easy for businesses to operate and provides a reasonably free environment to conduct business has a good chance for growth. The chart on the right indicates that with an overall rank of 33 (1 is best, 189 worst) is above average.

The World Bank's Doing Business Survey*

	2015 Rank	2014 Rank	Change in Rank
Overall Country Rank:	**33**	**34**	**1**
Scores:			
Starting a Business	82	78	-4
Construction Permits	101	97	-4
Getting Electricity	74	78	4
Registering Property	49	48	-1
Getting Credit	59	52	-7
Protecting Investors	29	44	15
Paying Taxes	60	79	19
Trading Across Borders	1	1	0
Enforcing Contracts	39	39	0
Resolving Insolvency	25	23	-2

* Based on a scale of 1 to 189 with 1 being the highest ranking.

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Economic Freedom

As can be seen below, Spain is above average in its overall rank of 67.6 for Economic Freedom with 100 being best.

Heritage Foundation 2015 Index of Economic Freedom
World Rank 67.6*

	2015 Rank**	2014 Rank	Change in Rank	World Avg.
Property Rights	70	70	0	42.2
Freedom from Corruption	59	62.6	-3.6	41.9
Fiscal Freedom	53.1	54	-0.9	77.4
Government Spending	39.8	38.7	1.1	61.7
Business Freedom	77.5	77.3	0.2	64.1
Labor Freedom	52.6	52.2	0.4	61.3
Monetary Freedom	81.3	79.9	1.4	75.0
Trade Freedom	88	87.8	0.2	75.4
Investment Freedom	85	80	5	54.8
Financial Freedom	70	70	0	48.6

*Based on a scale of 1-100 with 100 being the highest ranking.
**The ten economic freedoms are based on a scale of 0 (least free) to 100 (most free).
Source: The Heritage Foundation

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EJR's 3 yr. Default Probability: 1.8%

Valuation Driver: Taxes Growth:
KINGDOM OF SPAIN has grown its taxes of 5.2% per annum in the last fiscal year which is more than the average for its peers. We expect tax revenues will grow approximately 3.0% per annum over the next couple of years and 3.5% per annum for the next couple of years thereafter.

Valuation Driver: Total Revenue Growth:
KINGDOM OF SPAIN's total revenue growth has been more than its peers and we assumed no growth in total revenue growth over the next two years.

Income Statement	Peer Median	Co. Avg.	Assumptions Yr 1&2	Yr 3,4,5
Taxes Growth%	2.7	5.2	**3.0**	**3.5**
Social Contributions Growth %	1.7	1.7	**1.7**	**1.7**
Grant Revenue Growth %	0.0	NMF		
Other Revenue Growth %	0.0	NMF		
Other Operating Income Growth%	0.0	(5.8)	**(5.8)**	**(5.8)**
Total Revenue Growth%	1.9	2.9	**2.9**	**2.6**
Compensation of Employees Growth%	0.9	3.3	**1.5**	**1.5**
Use of Goods & Services Growth%	1.4	2.6	**1.2**	**1.2**
Social Benefits Growth%	1.8	0.0	**(0.3)**	**(0.3)**
Subsidies Growth%	0.8	10.0		
Other Expenses Growth%	(6.7)	(6.7)		
Interest Expense	0.0	3.1	**2.7**	
Currency and Deposits (asset) Growth%	0.0	0.0		
Securities other than Shares LT (asset) Growth%	0.0	0.0		
Loans (asset) Growth%	(1.5)	(4.2)	**(4.2)**	**(4.2)**
Shares and Other Equity (asset) Growth%	0.9	5.2	**5.2**	**5.2**
Insurance Technical Reserves (asset) Growth%	0.3	0.0		
Financial Derivatives (asset) Growth%	0.0	0.0		
Other Accounts Receivable LT Growth%	(0.2)	(10.6)	**(10.6)**	**(10.6)**
Monetary Gold and SDR's Growth %	0.0	0.0	**5.0**	**5.0**
Other Assets Growth%	0.0	0.0		
Other Accounts Payable Growth%	0.0			
Currency & Deposits (liability) Growth%	2.4	5.4	**5.4**	**5.4**
Securities Other than Shares (liability) Growth%	2.4	4.6	**3.2**	**3.2**
Loans (liability) Growth%	(1.2)	(5.0)	**0.5**	**0.5**
Insurance Technical Reserves (liability) Growth%	0.0	0.0		
Financial Derivatives (liability) Growth%	0.0	0.0		
Additional ST debt (1st year)(millions EUR)	0.0	0.0		

ANNUAL INCOME STATEMENTS

Below are KINGDOM OF SPAIN's annual income statements with the projected years based on the assumptions listed on page 3.

ANNUAL REVENUE AND EXPENSE STATEMENT
(MILLIONS EUR)

	2012	2013	2014	2015	P2016	P2017
Taxes	218,696	225,128	230,398	242,265	249,533	257,019
Social Contributions	131,859	128,217	130,063	132,333	134,643	136,993
Grant Revenue						
Other Revenue						
Other Operating Income	40,613	40,851	41,261	38,858	38,858	38,858
Total Revenue	391,168	394,196	401,722	413,456	423,034	432,869
Compensation of Employees	113,925	114,711	114,938	118,699	120,479	122,287
Use of Goods & Services	58,599	54,974	54,957	56,389	57,066	57,750
Social Benefits	197,042	198,812	198,747	198,800	198,204	197,609
Subsidies	10,004	10,853	11,400	12,536	12,537	12,539
Other Expenses	63,019	28,072	25,200	23,516	23,516	23,516
Grant Expense						
Depreciation	27,898	27,832	27,775	27,952	27,952	27,952
Total Expenses excluding interest	470,487	435,254	433,017	437,892	439,754	441,653
Operating Surplus/Shortfall	-79,319	-41,058	-31,295	-24,436	-16,720	-8,783
Interest Expense	30,922	34,669	35,291	33,122	34,016	34,935
Net Operating Balance	-110,241	-75,727	-66,586	-57,558	-50,737	-43,718

ANNUAL BALANCE SHEETS

Below are KINGDOM OF SPAIN's balance sheets with the projected years based on the assumptions listed on page 3.

ANNUAL BALANCE SHEETS
(MILLIONS EUR)

Base Case						
ASSETS	2012	2013	2014	2015	P2016	P2017
Currency and Deposits (asset)						
Securities other than Shares LT (asset)						
Loans (asset)	55,637	60,179	61,210	58,634	56,166	53,803
Shares and Other Equity (asset)	139,916	141,054	148,663	156,333	164,399	172,881
Insurance Technical Reserves (asset)	4,895	4,907	2,717		0	0
Financial Derivatives (asset)	84,693	71,418		85,455	85,455	85,455
Other Accounts Receivable LT	59,498	68,315	69,414	62,055	55,476	49,595
Monetary Gold and SDR's						
Other Assets					3,833	3,833
Additional Assets	1	-1	82,401	3,833		
Total Financial Assets	344,640	345,872	364,405	366,310	365,329	365,566
LIABILITIES						
Other Accounts Payable						
Currency & Deposits (liability)	3,681	3,696	3,847	4,056	4,056	4,056
Securities Other than Shares (liability)	674,834	812,063	960,528	1,005,058	1,037,674	1,071,349
Loans (liability)	217,157	196,598	204,739	194,557	245,294	289,012
Insurance Technical Reserves (liability)						
Financial Derivatives (liability)						
Other Liabilities	65,464	59,214	58,187	58,270	58,270	58,270
Liabilities	961,136	1,071,571	1,227,301	1,261,941	1,311,697	1,355,652
Net Financial Worth	-616,496	-725,699	-862,896	-895,631	-946,368	-990,086
Total Liabilities & Equity	344,640	345,872	364,405	366,310	365,329	365,566

*EJR Sen Rating(Curr/Prj) BBB+/ BBB+
*EJR CP Rating: A1
EJR's 3 yr. Default Probability: 1.8%

Comments on the Difference between the Model and Assigned Rating

SEC Rule 17g-7(a) Disclosure

Below are the disclosures as required by Paragraph (a) of Rule 17g-7.

1. The symbol in the rating scale used to denote the credit rating categories and notches within categories and the identity of the obligor, security, or money market instrument as required by Paragraph (a)(1)(ii)(A) of Rule 17g-7:
For the issuer KINGDOM OF SPAIN with the ticker of 1841Z SM we have assigned the senior unsecured rating of BBB+. There are three notches in our rating categories (e.g., A-, A, and A+) other than those deep into speculative grade; for CC, C, and D there are no notches.

2. The version of the procedure or methodology used to determine the credit rating as required by Paragraph (a)(1)(ii)(B) of Rule 17g-7:
We are using the methodology available in our Form NRSRO Exhibit #2 dated May 10, 2015 available via egan-jones.com under the tab at the bottom of the page "Methodologies".

3. The main assumptions and principles used in constructing the procedures and methodologies used to determine the credit rating as required by Paragraph (a)(1)(ii)(C) of Rule 17g-7:
The credit rating assigned reflects our judgement regarding the future credit quality of the issuer. Regarding the specific assumptions used, please refer to page 3 of this Rating Analysis Report.

4. The potential limitations of the credit rating as required by Paragraph (a)(1)(ii)(D) of Rule 17g-7:
Our rating pertains solely to our view of current and prospective credit quality. Our rating does not address pricing, liquidity, or other risks associated with holding investments in the issuer.

5. Information on the uncertainty of the credit rating as required by Paragraph (a)(1)(ii)(E) of Rule 17g-7:
Our rating is dependant on numerous factors including the reliability, accuracy, and quality of the data relied used in determining the credit rating. The data is sourced from publicly-available 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources. In some cases, the information is limited because of issues such as short operating histories, the lack of reported data, a delay in reporting data, restatements, inaccurate accounting, and other issues. Such shortcomings are not always readily apparent. EJR aims to identify such shortcomings and make adjustments using its best judgement.

6. Whether and to what extent third-party due diligence services have been used in taking the rating action as required by Paragraph (a)(1)(ii)(F) of Rule 17g-7:
EJR does not utilize third-party due diligence services.

7. How servicer or remittance reports were used, and with what frequency, to conduct surveillance of the credit rating as required by Paragraph (a)(1)(ii)(G) of Rule 17g-7:
Servicer or remittance reports normally pertain to structured finance issuers; this report does not pertain to a structured finance issuer (EJR is not an NRSRO for structured finance or sovereigns/ municipal issuers). Regarding surveillance, the minimum time period for corporation issuers is normally one year.

8. A description of the data that were relied upon for the purpose of determining the credit rating as required by Paragraph (a)(1)(ii)(H) of Rule 17g-7:
EJR uses 10Q and 10K statements, quarterly reports, 8K filings, earnings reports, and other similar sources for ratings on publicly-traded issuers. In the case of private issuers, EJR relies on information provided mainly by issuers.

9. A statement containing an overall assessment of the quality of information available and considered in the credit rating as required by Paragraph (a)(1)(ii)(I) of Rule 17g-7: The information is generally high quality and readily avail.

10. Information relating to conflicts of interest as required by Paragraph (a)(1)(ii)(J) of Rule 17g-7:
This rating is unsolicited.

*EJR Sen Rating(Curr/Prj) BBB+/ BBB+
*EJR CP Rating: A1
EJR's 3 yr. Default Probability: 1.8%

11. An explanation or measure of the potential volatility of the credit rating as required by Paragraph (a)(1)(ii)(K) of Rule 17g-7:
Our rating aims to assess the probability of the payment of obligations in full and on-time. Factors which affect such probability, and in turn our rating, include changes in the operating performance of the issuer, changes in capital structure, and merger and acquisition events.

12. Information on the content of the credit rating as required by Paragraph (a)(1)(ii)(L) of Rule 17g-7:
Regarding the historical performance of the credit rating, our rating transition matrix is available in our Form NRSRO, exhibit 1. The expected probability of default and the expected loss in the event of default is listed on the first page of this report.

13. Information on the sensitivity of the credit rating to assumptions as required by Paragraph (a)(1)(ii)(M) of Rule 17g-7:
Below is a summary of the impact of the 5 assumptions which independently would have the greatest impact on our "ratio-implied rating":

	Assumptions			**Resulting Ratio-Implied Rating**		
	Base	Optimistic	Pessimistic	Base	Optimistic	Pessimistic
Taxes Growth%	3.0	7.0	(1.0)	A-	A-	A-
Social Contributions Growth %	1.7	(1.3)	4.7	A-	A-	A-
Other Revenue Growth %		(3.0)	3.0	A-	A-	A-
Total Revenue Growth%	2.9	0.9	4.9	A-	A-	A-
Monetary Gold and SDR's Growth %	5.0	3.0	7.0	A-	A-	A-

14. If the credit rating is assigned to an asset-backed security, a description of: (i) the representations, warranties, and enforcement mechanisms available to investors; and (ii) how they differ from the representations, warranties, and enforcement mechanisms in issuances of similar securities, as required by Paragraph (a)(1)(ii)(N) of Rule 17g-7:
This credit rating is not assigned to an asset-backed security.

ATTESTATION FORM

In compliance with the US Securities and Exchange Commission (SEC) Rule 17g-7(a), the Egan-Jones analyst who published the report is responsible for the rating action and to the best knowledge of the person:

1) No part of the credit rating was influenced by any other business activities,
2) The credit rating was based solely upon the merits of the obligor, security, or money market instrument being rated, and
3) The credit rating was an independent evaluation of the credit risk of the obligor, security, or money market instrument.

Analyst Signature: **Today's Date**

Mina Ding

June 30, 2016

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Mina Ding
Rating Analyst

Reviewer Signature: **Today's Date**

Caroline Ding

June 30, 2016

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Caroline Ding
Rating Analyst

Sovereign Rating Methodology (Non-NRSRO)

Scope and Limitations: Sovereign Issuer Credit Quality Ratings (CQR) are a forward- looking assessment of a sovereign's capacity and willingness to honor its existing and future obligations in full and on time. Sovereigns are assigned two CQRs: a Local-Currency CQR, which reflects the likelihood of default on debt issued and payable in the currency of the sovereign, and a Foreign-Currency CQR, which is an assessment of the credit risk associated with debt issued and payable in foreign currencies.

Key Rating Drivers: EJR's approach to sovereign risk analysis is a synthesis of quantitative and qualitative judgments. The quantitative factors EJR uses are:

- Debt in relation to GDP.
- Surplus or deficit in relation to GDP.
- Debt plus potential under-funding of major banks in relation to GDP.
- Interest expense in relation to taxes.
- GDP growth.
- Foreign reserves in relation to debt.

Debt levels for many sovereign issuers have increased at an accelerating rate over the past decade, affecting implied ratings. EJR also considers unemployment levels and funding costs. EJR recognizes that no model can fully capture all the relevant influences on sovereign creditworthiness, meaning that the its sovereign ratings can and do differ from those implied by the rating model. Some of the qualitative factors that impact its ultimate assessment of credit quality include the flexibility, stability and overall strength of the economy, efficiency of tax collection, acceptance of contract law, ease of doing business, trade balances, prospects for future growth and health and monetary policy, and economic freedom. These subjective and dynamic qualitative issues are not captured by the model but affect sovereign ratings

For additional information, please see Exhibit 2: Methodologies in EJR's Form NRSRO.