

**EXECUTIVE  
SUMMARY**



# **1. Current situation of the City of Madrid**

## **1.1. Economic environment and outlook**

The Cyprus rescue has plunged the eurozone into instability once again and sets a precedent for the future. At the macroeconomic level, the fourth quarter of 2012 has been the worst in terms of growth in the G-4 economies (US, eurozone, Japan and United Kingdom) since the outbreak of the crisis. However, the first indicators for 2013 point to a recovery of activity at the global level, again led by the emerging economies but also, to a lesser extent, by the US. In the eurozone, the improvement of the January and February business and consumer confidence surveys has been cut short in March.

The Madrid Region's main macroeconomic variables deteriorated in the fourth quarter of 2012. With two quarters of negative GDP growth, the region found itself in recession at the end of 2012. The year ended with a 1.1% decline in GDP, 0.6 percentage points (pp) worse than the third quarter, and the trend points to a worsening of the economic recession in 2013. By sector, the GVA of industry and construction fell in 2012 (by 5.5% and 4.3% respectively), while the services sector grew by only 0.8pp, shrinking by 0.2pp in the fourth quarter. With regard to the labour market, the most significant change in the EPA labour market survey was due to the 13.9% increase in unemployment, with the unemployment rate reaching almost 20% in the fourth quarter, a level not seen since 1996.

CEPREDE forecasts that the crisis will continue in 2013, although 2014 is expected to mark a reversal of the trend in the Spanish economy, with GDP growth of 0.9%. Exports, the only economic variable to show a positive trend, are key to offsetting the fall in consumption and fixed capital. The economic forecast for the city of Madrid indicates a mild recovery in 2014, with growth of 0.5%, based on the possible growth of GVA in market services.

## 1.2. Production activities

### INDUSTRY

The crisis in industrial activity in the Madrid Region is deepening. The Industrial Production Index fell at an average annual rate of 12.8% at the beginning of 2013, 6.8pp worse than the Spanish average. The decline of industrial activity in the Madrid Region is also reflected in GVA: 2012 ended with a YoY fall of 6.4%. However, in January 2013 the Industrial Production Index fell 3.5 points with regard to the January 2012 figure, to 72.1, a slight improvement (0.4 points) on the average annual rate.

The industrial sector's lack of dynamism has a negative impact on employment, whose decline accelerated in the last quarter of the year (down 7.9%), 5pp worse than the average for the city. The greatest job losses occurred in the 'waste collection and treatment' sub-sector. With regard to the number of businesses, the decline in social security contribution accounts was similar, 7.1%, 1.8pp up on the third quarter.

### CONSTRUCTION AND REAL ESTATE MARKET

The trend in employment in the construction sector offers few novelties (a fall of 13% in the fourth quarter 2012) and, like the rest of the country, it remains mired in a deep depression.

Judging by the number of new build licences, construction activity has entered a recessive phase, with an annual average fall of 23.3% in January 2013. This decline was due largely to the sharp fall in social housing in the past few months. Unlike the decline in housing licences, the trend in new build completion certificates registered in the Madrid Surveyors and Architects Association is favourable, with an annual average rise of 89.5% in February of 2013. Non-residential demand has also experienced an improvement in recent months. The surface area authorized in non-residential construction licences increased by an annual average of 10.8% in January 2013. However, not all use types saw such an improvement. Licences for industrial land were down 91.9% and those for civic facilities fell 68.3%, reflecting the lack of dynamism of these activities in the city of Madrid.

### SERVICES

#### Financial System

The poor 2012 data, together with the absence of signs of improvement, suggest an unpromising financial outlook for 2013. At the end of the year, the reduced savings capacity was reflected in the level of deposits, which saw an annual average fall of 2.6%. The decline in lending was even more pronounced, down 3.2%, an obstacle to economic recovery. The YoY fall of 27.8% in mortgage lending at end year symbolizes the situation of economic distress of

families and the restrictions of a financial sector still excessively exposed to the property sector. After the last stock market tempest, caused by the terms of the Cyprus rescue, the rise seen at the beginning of 2013 has given way to another recessionary phase. The impact on the Madrid Stock Exchange is more acute than in other European markets (a fall of 8.7% in the second half of March), because of its greater exposure to the debt market of peripheral countries, as well as the bank restructuring process in progress.

### **Tourism**

The main tourist variables experienced a setback in 2012. Visitors to the city were down by nearly a million and overnight stays by two million. With regard to the last three months, up to February 2013, tourism continues to decline, with steep falls of both visitors and overnight stays (10.9% and 11.1%, respectively). The fall in overnight stays of foreign tourism is due, in large measure, to the intense contraction of the Italian market, which was not offset by the growth in non-EU European markets. Moreover, domestic tourism has ceased to offer an alternative to foreign tourism, and has entered a recessionary phase in recent months. In comparative terms, the annual average fall in overnight stays marks a low in the data series, down 6.9%, and 4.3pp worse than in the country as a whole.

Hotel capacity remains stable and for now it does not reflect the fall in tourist demand. On the other hand, employment in Madrid's hotels is suffering. The average YoY variation in the past three months is a fall of 3.4%, 2.1pp worse than the previous three months, and contrasts with the growth of 0.7% seen in the same period last year. The sector's profitability is also declining: revenue per available room in February 2013 was 7.9% down on a year before.

### **Transport**

The country's economic crisis caused domestic passenger traffic to collapse in 2012 (down 15.3%). Moreover, Barajas airport has to cope with the growing fall in international demand (down 5.7%), the reduction of frequencies on many commercial routes and the suppression of others, and the uncertainty generated by the restructuring of Iberia. On the other hand, the decline in international trade, due to the sharp fall in imports for the domestic market and lower expectations of external demand, is reducing freight traffic.

In regard to the city's urban transport, the total volume of travellers on public services fell by 4% in 2012. The most pronounced decreases were in Metro and EMT (bus) passengers, both with falls at around 5%, while local train services were down only 0.2%.

## 1.3. Business dynamic

Company formation in the city of Madrid slowed in the fourth quarter 2012; the increase of 1.4% was lower than the rise in closures (13.1%) and hence the net balance of creation has fallen (down 2.9%). Also, the capitalization of the companies slowed at the end of the year, the impact of the bank recapitalization having fallen out of the figures. In December, the annual average fell by 30.2% compared with November. In contrast, the number of Social Security contribution accounts increased, reaching its highest level in 2012 (almost 200,000, a YoY increase of 31.8%), driven by the new regulation of domestic work and self-employment in the services sector.

The business confidence indicator for the first quarter of 2013 remains mired in deeply negative values (the fifth consecutive quarter with values close to the threshold of 30 points negative). By sector, construction continues to show the least confidence, with -47.1, although the trend has been particularly adverse in industry, where the indicator fell 9.4 points over the previous quarter. Business perceptions of economic conditions, except for selling prices, were worse than initially expected, and in the forecasts for the second quarter, despite relative improvements, all the variables are still well into negative values.

## 1.4. Demand

The deterioration of consumption in Madrid is reflected in the fall in retail sales, with an annual average fall of 6% in 2012. The situation was even worse at the beginning of 2013, with a YoY fall of 6.5% in February, 1.5pp worse than the Spanish average. The city of Madrid's Consumer Confidence Index stood at 24.5 in the first quarter of 2013, four points above the previous reading and 3.3 less than a year before. The fall in sales has impacted employment in the retail trade, which ended the year with a fall of 3%, although it picked by 1.5pp in February 2013. The sharp fall in registrations in the fourth quarter (24.9%) reflects the collapse of vehicle sales in 2012, but in 2013 it is expected that the Plan PIVE subsidies should at least contain this fall.

In terms of the change in productive investment, in 2012 all the growth experienced a year earlier was reversed. However, the slight improvement seen in January 2013, with a YoY increase of 2.2% in capital goods investment, although an isolated occurrence, put an end to sixteen consecutive months of negative numbers, softening by 0.8pp the fall in the average annual rate (11.8%).

The pace of growth of Madrid's exports slowed strongly in the course of 2012, to the point of falling almost to 0% at the end of the year. Despite the stagnation of exports, the fall in imports has helped to reduce significantly the trade deficit, whose cumulative fall reached 17.5% in January. The sectors with the largest increases in exports have been 'capital goods', 'other merchandise' and 'vehicles'.

## 1.5. Prices and salaries

The inflation rate in the Madrid Region in the past few months has been restrained at around 2.5%. Looking at developments in the twelve months to February 2013, headline inflation has risen by 0.5pp, due largely to the pressure of core inflation, which increased by 0.9pp, as a result of the increase in VAT rates in September last year. However, given the moderating inflation of energy products and assuming there are no new administrative decisions causing a rise in prices, average inflation for 2013 as a whole could reach 1.9%, 0.5pp lower than in 2012.

By sector, the groups that are contributing most to the rise in inflation at the start of 2013 are 'alcoholic beverages and tobacco', 'communications' and 'transport', while prices fell for all 'special groups' with the exception of the 'processed foods, beverages and tobacco'. Industrial prices are tending to decline. The Industrial Price Index saw a 1.4% rise in February 2013, 7.3pp less than a year earlier. The fall in housing prices accelerated in the fourth quarter of 2012, particularly in the case of new housing (down 25.8%). The decline in used housing prices was somewhat less severe, at 17%. This fall in housing prices was more pronounced than the Spanish average. Lastly, the correction in labour costs in the Madrid Region is accelerating, with a YoY fall of 3.2% in the last quarter of 2012, which contrasts with the increase of 1.6% a year earlier.

## 1.6. Labour market

In a context of generalized economic recession in Spain and the eurozone, all the variables of Madrid's labour market were deteriorating as 2012 ended. The labour force has fallen back to the 2006 level, while employment is decreasing and unemployment increasing. As a result, the activity rate has declined to 60.8%, 0.8pp less than a year before. The decline in employment (4.1% in the fourth quarter 2012) affects salaried workers, particularly those with temporary contracts (down 15.4%), while the number of non-salaried workers has increased (11.9%), due largely to workers adopting a strategy of self-employment. Young people and women, the most vulnerable groups, are especially affected by the deterioration in employment and unemployment. By sectors, industry is the worst affected, both by the decline in the number of employed and Social Security enrolments, and by the rise in unemployment. On the other hand, the decline of the services sector would have been more intense were it not for the mass regularisation of domestic workers, while in the rest of the sector employment is falling and unemployment growing.

At the start of 2013, the data on Social Security enrolment and unemployment are also unpromising. In February there were 46,709 fewer enrolments and in March there were 17,309 more registered unemployed than a year ago.

Forecasts for enrolment in the city of Madrid point to a YoY contraction of 2.7% in enrolment in the first quarter 2013 and 2.5% in the second quarter 2013. The only positive aspect of the forecasts is that the rate of decline is moderating, 0.5pp less unfavourable in the second quarter 2013 than fourth quarter 2012. The number of registered unemployed in the city of Madrid is projected to be about 254,000 in the second quarter of 2013. In line with this, the YoY rise in June would slow to 5.4%, 1.7pp less than in March.



## 2. Monografic report

### BARAJAS IN THE LOCAL ECONOMY: IMPACT AND MANAGEMENT MODEL<sup>1</sup>

Annual traffic through Madrid-Barajas Airport in 2012 was **45 million passengers** and **370,000 tons of cargo**. This made it the leading Spanish airport with a market share of **23%** in passengers, **55%** in cargo and **19%** in operations, i.e. Madrid-Barajas has almost a quarter of the Spanish air passenger market and more than half the market for air freight. At international level, Barajas is the **fifth** (5th) European airport passengers after Heathrow, Charles de Gaulle, Schiphol and Frankfurt; and **sixteenth** (16th) in the world.

In cargo traffic, however, Madrid-Barajas lags far behind Frankfurt which, with 2.1 million tonnes, is the leading European airport for freight and, of course, behind Hong Kong and Memphis which, with almost 4 million tonnes, are the world's busiest airports with regard to cargo.

Airports are much more than a transportation terminal, because they generate a great deal of economic activity to service the air transport itself and due to the other service activities, both commercial and industrial, located in the airport itself.

These activities draw their business from the passengers and shippers who use the airport's air transport services, from passengers who buy products and services at the airport, from the airline companies that have their aircraft repaired in the maintenance centre and from the public administration providing certain public services at the airport.

These businesses also have an effect on the rest of the regional and national economy, generating an economic impact in terms of the generation of wealth and employment. These impacts are derived directly or indirectly from, or are induced by, the activities carried out at the airport.

However, there are other economic effects that could be attributed to the presence of the airport in the area, such as those arising from the economic activity generated by visitors to the area who arrive and leave via the airport.

This economic activity might not exist or be much smaller if there were no airport, since the existence of air travel connections is an important factor in the choice of journey destinations. This economic impact is known in the literature as catalytic.

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The study evaluates these four impacts generated by the airport with the following considerations:

**Direct impact** composed of the jobs created in the airport and the value added generated by its activity.

**Indirect impact** composed of the jobs and value added generated in the rest of the economy by the intermediate consumption of the airport.

**Induced impact** composed of the jobs and value added generated by the private consumption arising from the income earned by the jobs created.

**Catalytic impact** composed of the jobs and value added generated by the spending of tourists entering the territory through the airport.

The values obtained for these impacts are as follows:

- Total production (direct, indirect, induced and catalytic) of almost **€40 billion**, of which more than a quarter is carried out in Madrid.
- **€15 billion of GVA**, 20% of which is generated in Madrid.
- **305,000** full-time equivalent jobs throughout Spain, nearly one third of which correspond to the direct, indirect and induced effects. 18% of these jobs, about 55,300 are created in Madrid.

With regard to management models, airports in Europe have traditionally been seen as providers of a public service. Hence, public ownership, with different degrees of involvement of the respective regional governments, has been predominant until very recently.

Nevertheless, the privatization processes implemented in recent decades have also affected airport policies in many countries. Thus, different ownership structures can now be found in airports across Europe.

In the case of the US, various formulas are in use, but in general they are under the control of Federal or local authorities, as is the case of Atlanta, the world's leading airport in passenger traffic, which is owned by the local administration, and Memphis, the world leader in freight traffic, which is owned by the counties of Memphis and Shelby.

In the case of Spain, the airport management model is in the process of change. As part of this process, AENA Aeropuertos S.A. is being prepared for the entry of private capital, with a cap of 49% on this private capital, so that the state retains a majority holding.

We are, therefore, at a momentous time for airport management in Spain and for an infrastructure facility as is Barajas airport, crucial to the future of the city and of Spain as a whole, with direct effects on the well-being of the population and on the territory in it is situated. A management model in which the city will need to participate, as required by the legislation, in pursuit of the efficient coordination of a multitude of aspects in which the City Council will contribute to excellence.

## EFFECTS OF THE OLYMPIC CYCLE ON THE CITY OF MADRID

The Olympic bid process, initiated by the city of Madrid with its candidacy for the 2012 Games, is one of the city's aspirations and has been integrated into its medium and long term strategic planning processes, from the 1997 Urban Development Plan to the Madrid 2020 City Future Strategic Plan. In this respect, the investments made in the city during these years have supported the various Olympic candidacies but at the same time form part of a long-term strategic vision of the city, structured around: (1) restoration of green spaces; (2) improvement of transport; (3) development of renewable energy; (4) construction of new sports facilities; and (5) enhancement of the city's image at the international level.

The investments already made, together with the growth of tourist flows arising from the greater international visibility of Madrid, has resulted in the generation of economic activity and employment for the city.

In this respect, our estimates indicate that the approximately €6.49 billion euros already invested in transport infrastructure and sports facilities, both in Madrid and in the surrounding metropolitan area, over the 2004-2012 period, has contributed to an increase of €9.15 billion in the city's production (equivalent to 4.1% of the city's figure for 2011) or €1.02 billion each year (0.5% of the city's 2011 production). In terms of GVA, the increase is €3.8 billion for the whole of the 2004-2012 period (3.2% and 0.4% respectively of the city's GVA). This activity has led to the creation/conservation of 75,536 full-time equivalent jobs, equivalent to 8,393 jobs each year (4% and 0.4% respectively of employment in 2011).

Likewise, Madrid's successive Olympic candidacies have constituted an excellent marketing campaign for the city, keeping the YoY growth rate in the number of tourists an average 3.8 percentage points higher than for Spain as a whole in the 2004-2012 period.

This positive growth differential, which has been accompanied by an expansion and upgrading of the city's hotel capacity, allows us to estimate the additional tourism revenue derived from the successive Olympic candidacies at €504.1 million at 2012 prices for the 2004-2012 period. This additional revenue from tourism has had the effect of increasing production by €743 million (€353 million in terms of value added) and has allowed the creation of 7,545 full-time equivalent jobs.

The bulk of the investment needed to host the 2020 Olympic Games has already been made, apart from €2.30 billion for permanent facilities and refurbishment of existing installations.

These investments, which will be carried out only if Madrid is finally selected to host the Games, would be a stimulus for the city's economy, estimated to generate increases in GDP of €3.24 billion and

€1.33 billion in GVA, with the creation of 26,717 full-time equivalent jobs, over the 2013-2020 period.

In terms of tourism, the prospect for Madrid, somewhat more moderate than that experienced by Barcelona, is for a total of 1.5 million visitors in the year of the games themselves (equivalent to 19% of the number the city received in 2012) and an additional 1 million in the subsequent five years (up 12.6% on the pre-Olympics figures). This would mean an additional €3.95 billion in tourism revenue for the city in the 2020-2025 period at 2012 prices, which would translate into an increase in GDP of €5.82 billion euros, €2.76 billion in GVA and the creation of 59,095 full-time jobs equivalent, 9,849 jobs per year, 0.5% of the city's total employment.

The overall economic impact of the Olympic cycle if Madrid is successful in its quest for the 2020 Games can be estimated by adding the positive impacts before and after the celebration of the Games, derived from both the investments and the increased tourist revenues. It would lead to an increase in the actual production of the city of €19.00 billion, in GVA of €8.22 billion, and the creation of 168,893 full-time equivalent jobs, representing 8.4%, 7.1% and 8.9% respectively of the city's annual figures for GDP, GVA and employment in 2011.

In sectoral terms, construction should benefit most from the Olympic cycle, accounting for 42.5% of the production (€8.05 billion), 37.4% of the GVA (€3.01 billion) and 40.9% of the employment generated, with a total of 69,079 jobs, followed by hotels and catering with 10% of the production (€1.90 billion), 8.8% of the GVA (€723 million) and 17% of the employment (28,710 jobs), and retail trade with €1.29 billion of production (6.8%), €911 million of GVA (11.7% of the total) and 15.9% of employment (25,577).

In geographical terms, all districts of the city benefit from the Olympic cycle, with a very balanced distribution of the impact, particularly in the of Centro, San Blas and Salamanca districts, which would concentrate 13%, 7% and 7%, respectively, of the total economic activity and employment generated by the Olympic process.

Finally, it should be noted that the benefits of the Olympic cycle go beyond the activity generated by the investment and tourism flows. This has contributed to the geographical balance of the city through its legacy in two areas. On the one hand, the major environmental upgrading and improvement of the facilities resulting from the renovation of the banks of the river Manzanares, especially in the districts of Usera, Puente de Vallecas, Villaverde and Villa de Vallecas, and the generation of new town centre facilities in the east of the city, mainly around the San Blas district. On the other hand, the improvement of the transport networks and especially the public transport system.