

EXECUTIVE SUMMARY

1. Current situation of the City of Madrid

1.1. Economic environment and outlook

The recent episode of instability in some emerging markets threatens to jeopardize the recovery of the major developed economies, and those of the euro area in particular, at a time when the dynamism of external demand remains key to consolidating economic growth. However, the latest data on economic activity in 2013 are surprising on the upside and GDP growth in the fourth quarter in regions such as the eurozone may have been the highest of recent years. In this period, growth was supported not only by the strength of demand in countries such as Germany, but also by the growth of spending in peripheral countries such as Spain.

In Spain, the restructuring of the financial system is being successfully completed, while domestic demand is recovering though the external sector's contribution to growth is weakening. The growth in Spanish GDP in the third quarter (0.1% QoQ) was confirmed and moreover it was accompanied by the first quarterly increase in household consumption and domestic demand since the second quarter of 2010. However, the Madrid Region recorded negative YoY GDP growth rates in every quarter of 2013. Despite this, the rate of decline is clearly easing, and positive YoY growth is forecast in mid-2014.

According to the macroeconomic projections for Spain prepared by the Centre for Economic Forecasting, 2014 will see growth in private consumption, and a very marked slowing of the fall in public consumption and gross capital formation, which will record falls of 0.7% and 0.8% respectively. GDP growth in the city of Madrid is forecast at 1.2%.

1.2. Economic sectors

INDUSTRY

The third quarter of 2013 saw a further easing in the rate of decline of the Industrial Production Index (IPI) in the Madrid Region. The largest declines were observed in consumer goods and intermediate goods, with average annual variations of 6.4% and 11.6% respectively. The scale of the fall in the Region is greater than in the country as a whole, although the slowing in the rate of decline has been more marked in the region.

The enrolment of workers in the Social Security in the city of Madrid's companies fell by 2.9% in September 2013, to a total of 74,515, nearly 250 more than in the second quarter of 2013.

CONSTRUCTION AND REAL ESTATE MARKET

The number of building licenses issued by Madrid City Council's Town Planning and Housing department again saw a significant decline, highlighting once more the continuing adjustment that plagues the sector. The average fall in the quarter was around 53%, although the greatest decreases, more than 70%, were recorded in October and November, reaching historical highs in both cases. In numerical terms, the number of licenses declined by 5,907 in the period between January and November of 2013, compared to the same period of 2012.

With regard to the distribution of licenses by type and by zone, the bulk of licenses for subsidized housing (close to 90%) were concentrated in the district of Vicalvaro, while developments of new free-market urban housing were shared between Moncloa-Aravaca, Chamberi, Villa de Vallecas and, to a lesser extent, Barajas.

SERVICES

Financial System

The number of bank branches in the city of Madrid declined by 9% YoY in the third quarter of 2013, representing an acceleration of the reduction in previous quarters.

On the other hand, the growth in deposits in financial institutions has not yet been reflected in the availability of credit. The high level of indebtedness, loan delinquency and the ongoing recapitalization of financial institutions continue to impede the flow of financing to the real economy. In September 2013, the total volume of credit in the city of Madrid stood at €360.7 billion, 13.5% less than in the same month of the previous year.

Tourism

In the last quarter of the year, the performance of tourism improved, thanks to domestic tourists, who represent more than 60% of the total number of visitors to the city of Madrid. This improvement occurred despite the persistence of the difficulties in recovering the foreign market, which was reflected in the fall in air traffic at Barajas airport, in the absence of tourists switching from destinations affected by political instability and in the effect of the economic crisis on certain traditional markets.

The latest data available on the supply of hotel rooms in the city of Madrid showed a 2.7% YoY increase in the number of beds in the fourth quarter of 2013, higher than that observed during the previous quarter. Thus, the last few months of the year saw highs in this series, with a quarterly average of 82,313 beds. However, growth rates are similar to those seen in early 2012, which implies a slowdown in the pace of growth experienced in 2011 and 2012.

Transport

The trend in air traffic over the first eleven months of 2013 continued to fall in year-on-year terms, with an annual decline of 12.9% up to November. This drop was due both to a decline in both domestic and international passengers, although it was domestic traffic which registered the largest fall in numbers.

Journeys on urban transport in the city of Madrid fell by 4% YoY up to November. The Metro was the mode of transport most affected, with a decline of 7.9%, while transportation by bus and the local train network suffered significantly smaller declines, in both cases below 1%.

1.3. Business trends

In the third quarter of 2013, the city's business trends, measured in terms of net creation of companies, experienced a deterioration compared to previous periods. Thus, in the third quarter of 2013, net company creation fell by 35.6% from the previous quarter and by 10.8% on a YoY basis, to 524.

Business confidence recorded a significant improvement in the fourth quarter of 2013 with respect to the trend in recent years. Even though the business confidence indicator remains in negative territory, still affected by the stagnation of the Spanish economy, the figures were far better than those for previous quarters. Thus, the index recovered the level of early 2011, with a fifteen point improvement over the previous quarter.

1.4. Demand

In the third quarter of 2013, the general retail trade index for the city of Madrid fell by around 8%, in line with the previous quarters. However, the trend shows a moderation in the decline, similar to those reflected in parallel in other economic indicators.

The city of Madrid's Consumer Confidence Index again increased, rising 8.3 points above the levels of the same quarter of last year. This increase takes the indicator to 28.8 points, a level last recorded in 2011, though it still reflects a degree of uncertainty about the short term.

Productive investment shows a similar behaviour to that reflected in the industrial production indices, while maintaining the trend of previous periods, with a slowing average annual rate of decline. Thus, in the Madrid Region, capital investment experienced positive average annual rates of variation in August and September (2.4% and 4.2% respectively), interrupting the process of deceleration. However, in October it again declined, with an annual average fall of 1.8%, six points below the figure for the previous month. Comparison with the nationwide data shows that there has been a similar process of slowing falls since the beginning of the year, though less marked than in the Madrid Region. In October, the rate of the Madrid Region converged with that recorded by the country as a whole, with a fall of 1.7% in the annual average.

Madrid's economy is turning to foreign markets to compensate the weakness of domestic demand. The Madrid Region's opening up to the global market for goods and services coincides with the increase in its competitiveness, due to the decline in unit labour costs, which gives an extraordinary boost to exports. On the other hand, the stagnation of domestic demand contributes to the decline in imports, which also contributes positively to the trade balance. In the twelve months to October 2013 (the latest data available) exports totalled €30.7 billion, €3.5 billion more than the same period of the previous year; in YoY terms that represents remarkable growth of 13.0%, two percentage points more than in September.

1.5. Prices and wages

The fourth quarter confirmed the easing trend in the rise in prices. The YoY change in the CPI in October was a decline of 0.2%, a negative trend not seen since the summer of 2009.

Underlying inflation - the rise in prices excluding certain foods and raw materials from the index - has followed the same trend as overall inflation, without significant differences in the YoY rates. Prices are expected to rise steadily in 2014, as demand recovers, although it will not exceed the 1.5% mark, as long as demand and costs behave as expected and there are no substantial modifications in indirect taxation.

By economic sector, goods in the category of 'Alcoholic beverages and tobacco' show the highest growth, 5.5% YoY, followed by 'Schooling', which has nevertheless seen a reduction in inflation to 4.1%, after eleven consecutive months of rises in excess of 11%. The biggest fall occurred in the category of 'Communications', which decreased by 6.6%, half a percentage point more than the figure for the third quarter.

Among the goods categorized as 'special', processed foods, beverages and tobacco experienced the greatest increases in the quarter, at around 2.7%, while industrial goods, excluding energy products, were down by 1.2%.

The trend in the Industrial Price Index (IPRI) tends toward stagnation, in line with the general index. After the rebound seen in the third quarter, price rises eased again in the last months of the year. In YoY terms, December ended with a rise of 1.1%, half a percentage point below the average for the year.

In 2013, the moderation of labour costs has been felt more strongly in Spain as a whole than in the Madrid Region. In any case, both indicators appear to be converging towards the stagnation of costs, in line with the trend in prices. In the third quarter, the region's average labour cost amounted to €2,842.80 per worker, €177 less than the previous quarter.

1.6. Labour market

According to the EPA labour force survey for the fourth quarter of 2013, the city of Madrid's labour force declined by 4.8% in YoY terms, a fall of 77,300. This is a smaller decline than the previous quarter, when the labour force fell by 6.9% YoY (down 114,500), the largest quarterly decline of the year. The activity rate stood at 59.5% in the fourth quarter, the lowest level recorded during the year.

Meanwhile, employment in the city of Madrid showed a decrease of 4.1% (53,400), the smallest decline of the year. This took employment to 1.25 million.

Social Security enrolment in the city rose to 1,671,105 in December 2013, a level that, though less than the same month of the previous year (down 0.8%), is nevertheless above the average for 2013. The pace of job losses, measured as the average of the YoY rate of the last twelve months, stands at 2.3%, signifying a certain acceleration of this negative trend in the last year.

According to the EPA, the number of unemployed decreased significantly, with a YoY decline of 8.0%. The unemployment rate stands at 17.6%, similar to the level recorded in the third quarter of 2012 and slightly lower than in the first half of 2013.

With regard to the statistics of registered unemployment in the city of Madrid published by the State Employment Service (SEPE), the number of unemployed amounted to 247,000 in December 2013. This represents an annual increase of 4.2%. Thus, the slowdown in the growth rate of registered unemployment, which has been observed since the end of the year 2012, led to a fall of 1% in the number of unemployed in December 2013, the first decline since June 2011.

2. Monographic report

Ranking of European Cities 2013

For the seventh consecutive year, we present the ranking of the 25 European cities considered large metropolises, based on an analysis using 25 indicators divided into four dimensions: Economy, Transportation and communications, Knowledge society and Quality of life.

In the 2013 ranking, Madrid takes the fourth place among the large European metropolises, behind only London, Paris and Berlin. Thus, Madrid moves up one place with respect to 2012, with Frankfurt, previously fourth, falling to seventh. Meanwhile, Munich and Amsterdam rise two places, to fifth and sixth respectively, while Stockholm slips from seventh to eighth. Barcelona keeps the ninth slot, while Brussels rises to tenth, completing the top ten.

In the dimension of Economy and labour market, Madrid takes the second spot of the ranking, moving up one position with respect to 2012, despite the current economic situation. This puts it behind London, and ahead of other notable economic centres such as Berlin, Paris, Frankfurt and Barcelona. The city's good performance in this dimension was notably good, achieving a top ten slot in eleven of the dimension's fifteen indicators. The best results were obtained in "Availability of office space", "Worker qualifications" and "Population in 2020", in which Madrid is placed among the top three European cities. These improvements may be indicative of the economic progress reflected in the latest forecasts for Madrid's GDP. Nevertheless, the indicators of "Unemployment rate" and "Salary level" show a deterioration.

Madrid is ranked seventh in the dimension of Transportation and communications, rising one place with respect to the previous year. This advance was achieved despite the weaker trend in arrivals at Madrid Barajas airport, with negative growth, though lower than the previous year. This puts Madrid in 23rd position for this indicator, one notch above that reached in 2012. It maintained its slots for "Total passenger traffic" and communications, reflected in the "Accessibility" indicator, with positions 5 and 6 respectively.

Madrid's performance in the Knowledge Society ranking held steady with regard to the previous years, occupying an intermediate level in the classification. Thus, it stood in 11th position, immediately behind Amsterdam and in front of Prague. With regard to investment in R&D, the city registers a fall of 3% with regard to the previous ranking. Nevertheless, it maintains the position of the previous year in terms of R&D spending, occupying position 16, ahead of Rome and Lisbon. On the other hand, with regard to the relative weight of research staff in total employment, the city rises two places with regard to the previous year, to 8th.

In the quality of life dimension, the city of Madrid rises to 11th position, one better than the previous year. This improvement is due to better figures for the indicators of "Air quality", where it rises seven places to number 14, and "Quality of life", prepared by Mercer, which saw the most notable improvement, rising to 11th. Meanwhile, Madrid maintained its ranking in the indicator of "Most liveable cities", in eighth position.

Metropolitan region

Madrid's metropolitan dimension was analysed under the concept of "metropolitan region" which, besides the more consolidated central metropolitan areas, includes the zones of influence beyond the region's administrative limits.

In terms of concentric rings, five areas can be distinguished. The central area contains the bulk of the population and economic activities, together with centralizing key functions and the communications network. The second and third intermediate areas have featured the highest population and urban growth over the past decade. The process of metropolisation is more diffuse in the peripheral areas, into which the metropolitan corridors extend or which include other urban conglomerations which have grown up around the provincial capitals.

The metropolitan region constitutes a diverse, complex socio-economic space, undergoing constant transformation. The distribution of the population is polarized: the Consolidated Urban Area accounts for 68.5% of the population, in an area that represents only 7.9% of the metropolitan region, which represents a density of more than 4,000 inhabitants per square kilometre (compared with 46 in the most peripheral zone). Nevertheless, the greatest demographic dynamism is found in the intermediate and peripheral metropolitan zones, which translates into a younger age structure. Thus, in the 2001-2012 period, the third zone increased its population by 85.4%, far above the average growth of the metropolitan Region, of 23.6%, or the growth of the central area, 12.7%.

The distribution of economic activity is even more polarized. 60% of the metropolitan region's GDP is concentrated in the city of Madrid and, if all the central municipalities of zones I and II are considered, this proportion rises to 86,7%. The small share of the remaining areas is accounted for by the more diffuse distribution of economic activities, together with the greater residential specialization. Employment follows a similar pattern. The city itself is the main centre of employment, with 680 Social Security enrolments per 1,000 residents. This proportion declines considerably as we move away from the capital, to 207 per 1,000 in the most peripheral zone. With regard to sectoral distribution, the economy of the metropolitan region is highly specialized in the services sector, which represented 85.3% of Social Security enrolments in 2012. Industry and construction follow far behind (8.3% and 5.9% respectively), while agriculture is a residual activity (0.5%). This distribution is uneven, however: the predominance of services decreases noticeably from the centre (88.3% in Zone I) to the periphery (57.6% in Zone V). The relative weight of industry is significantly higher in the third and fifth areas (18.8% and 22.9% respectively) and it has a smaller presence in the central area (6.4%).

The high mobility of the population is one of the metropolitan region's main characteristics. The large numbers of workers and students arriving in the city of Madrid testify to its power of attraction as a great metropolitan centre. The central areas account for no less than

80% of the daily journeys by workers and students in the Metropolitan Region (more than two million people). The majority of Europe's inhabitants live and work in metropolitan regions. With more than seven million inhabitants, the Metropolitan Region of Madrid leads the Spanish ranking, followed by Barcelona and Valencia (with 5.5 and 2.6 million respectively). In the EU, the metropolis of Madrid is notable for its spectacular population growth (together with London, the two only examples of cities that saw population increases of more than a million in the 2003-2012 period) and for its leading international functions such as air transportation.