

EXECUTIVE SUMMARY

1. Current situation of the City of Madrid

1.1. Economic environment and outlook

Neither the Bank of Spain nor the Federal Reserve consider that the recent signs of economic recovery are sufficiently definitive to justify ending the monetary stimulus policy. The eurozone experienced a strong increase in activity in the second quarter 2013. Growth rates in countries such as France (up 0.3% YoY) and, above all, Germany (0.5% YoY) led to a significant containment of the YoY fall in eurozone GDP (down 0.5%). The improved performance in the peripheral economies, which moderated their contraction, reduced the drag on eurozone GDP growth during the quarter.

With regard to the Spanish economy, there was a notable moderation of the deterioration in domestic spending, while domestic demand constituted a drag on quarterly GDP growth (negative 0.2%). The macroeconomic figures for the Spanish economy remain consistent with the forecast of 0.9% for GDP growth for next year. On the other hand, they lead us to modify the 2013 whole year forecast made in the last quarter, improving the YoY GDP variation by 0.1 percentage points to a fall of 1.2%. The dynamics of the external sector play an important role in these forecasts, having proved key to cushioning the very adverse developments in domestic demand, especially in the case of gross capital formation, with a YoY fall of 6.2%, while the consumption is falling by around 2.5%.

The L. R. Klein-Centro Stone Institute's forecasts for the city of Madrid, prepared in June 2013, point to a 1.2% fall in GDP in 2013. For 2014, however, the forecasts improve, putting GDP growth at 1.3%.

1.2. Economic sectors

INDUSTRY

The summer months seem to represent a turning point in the downward trend seen in the Madrid Region's industrial production since early 2012. The fall in the Industrial Production Index (IPI) is a percentage point less than in the past quarter, when the slowdown in the rate of fall in activity was already noticeable. However, the decline remains notable, at around 10% on a YoY average basis. At the national level, the trend is very similar, even though the fall is considerably smaller, with a decline of 4.4% in July, 0.4 percentage points less than in May.

The YoY fall in the enrolment of workers in the Social Security was 5.1% in June 2013, somewhat lower than in March 2012. In numerical terms, the total declined by 74,267,104 less than in the first quarter 2013 and 3,992 less than a year earlier. With regard to total enrolment in the city of Madrid, the industrial sector continues to show a greater decline, with more than four percentage points of difference in annual average terms.

CONSTRUCTION AND REAL ESTATE MARKET

The number of building licenses issued by Madrid City Council's Town Planning and Housing Department again recorded declines of around 60% in the twelve-month rolling total, similar to the fall in June 2010. In absolute terms, the number of licenses fell by 4,374 in August 2013 compared to the same month in 2012, a figure that eloquently reflects the adjustment still affecting the construction sector in the city of Madrid.

The number of building licenses has been significantly reduced, extending the trend set in the first quarter. In numerical terms, the decrease was around 40.2% for free market housing and 67.1% for subsidized housing. However, the reduction in free market housing licenses granted by the Town Planning and Housing Department was 908, an figure far outweighed by the decline in subsidized housing licenses, which reached 3,466.

SERVICES

Financial System

In the April-June period, the trends manifest in the first quarter of 2013 were maintained. There was a significant increase in deposits with banks, accompanied by a continuing squeeze on credit channelled to the private sector. This trend, while improving the liquidity position of the financial institutions, only aggravates the difficulties faced by households and firms in access to credit, and is one of the fundamental determinants - perhaps the main one - of the slackness in the real economy and, in particular, of the sickly trend in domestic demand.

The trend in credit reflects the problems that the banking sector continues to face in restoring funding. The enormous indebtedness that weighs it down, combined with increased loan delinquency, the uncertainty caused by economic stagnation and the difficulties inherent in the recapitalization of financial institutions, are the obstacles that continue to hold back the flow of credit and, with it, the recovery of economic activity. In the city of Madrid, the total volume of credit amounted to €367.1 billion in June, 14.7% less than the same month last year.

Tourism

The figures for tourism reflect the strong downturn that the sector suffered during the summer of 2013. The number of passengers arriving in the capital has fallen drastically - the annual cumulative total is down 7.8% - as has the number of overnight stays, due in large part to the fall in air traffic suffered by Barajas airport in recent months, but also to the collapse of traditional source markets such as Italy and Portugal. On the other hand, the city of Madrid has not benefited from tourists switching from countries with political instability - as is the case of Egypt - which has served to increase tourism in other Spanish destinations. Thus, room occupation has suffered as a result, with a decline of 7.5%.

The fall in the tourist demand in the city together with the increase in the supply of hotel rooms has resulted in a decline in the average income per available room. In August, the fall was 9.4% in YoY terms, implying an average reduction of €3.10 per room. Meanwhile, this same indicator grew by 4.1% for the country as a whole. In this respect, though the differential in income always favors the nationwide figure in the months of July and August, the summer of 2013 has seen it register a maximum of €32.50 in August in favor of the nation as a whole.

Transport

Air traffic continues to show a significant decrease with respect to previous periods. Domestic traffic continues to present the biggest fall, around 20.5% in the period between January and August 2013. The triggers for this decline in domestic air traffic include the persistence of the economic crisis at the national level, switching between different modes of transport due to the reduction in prices for high-speed rail lines and the difficult situation of Madrid-Barajas airport.

The use of urban transportation in the city of Madrid continued to fall between January and August, down by 6.7% compared with last year. The mode of transport most affected by this decline is the metro, down around 9.4%, followed by the EMT bus company with a fall of 2.7%.

1.3. Business trends

The second quarter of 2013 has proved especially positive for the net creation of companies, i.e. the difference between newly formed companies and those which have closed. This indicator reflects the health of the city's business community, which is progressing slowly in a context of persistent stagnation. In the second quarter of 2013, the net value of newly incorporated enterprises rose considerably compared to the first quarter, reaching a quarterly growth rate of 6.1%, or 4.6% when compared to the same quarter of 2012.

Business confidence is still mired at extremely low levels, due to the weakness of domestic demand, the slow pace of the economic recovery and, in short, the stagnation that continues to plague the Spanish economy. The confidence indicator has not recovered from the decline it suffered in the first quarter of 2012, recording a further fall of half a percentage point with regard to the second quarter and nearly two points in relation to the same period in 2012.

1.4. Demand

The retail trade's general index again recorded successive falls during the second quarter, falling below -8%. However, the trend shows some signs of moderation. On the other hand, the city of Madrid's Consumer Confidence Index has rebounded in the third quarter, rising 5.1 points above the level seen in the same quarter of last year. However, the recovery of confidence remains moderate, reflecting the caution of Madrid's consumers given the uncertainty that still reigns in the short term.

The employment index of the Madrid Region's retail trade registered a YoY fall in August of 5.6%, exceeding by more than two percentage points the decline observed in the same month last year.

In line with the trend of the indices of industrial production, productive investment has continued the trend seen in the last quarter, i.e. of significant moderation in the pace of decline in the average annual rate. Investment in capital goods in the Madrid Region fell by 6.6% in August, around seven percentage points above lows recorded in February and March.

1.5. Prices and wages

The growth of prices in the Madrid Region has slackened considerably in the third quarter of 2013, with the YoY rate falling to 0.3% in September. Core inflation, which excludes the most volatile components of the CPI, is tracking headline inflation, with barely appreciable differences between the YoY rates. Inflation is expected to remain at around 1% in the coming months, provided there are no major changes in the fundamentals - increases or declines in demand or supply - or substantial changes in indirect taxes.

With regard to inflation in the different economic sectors, the YoY rise in the CPI reveals quite disparate price increases. The categories with the highest rises are 'schooling', which has already seen eleven consecutive months with increases in excess of 11%, followed by 'Alcoholic beverages and tobacco' and 'Food and non-alcoholic beverages', where prices are rising at a more moderate, though still significant, pace at 5.7% and 2.5%, respectively. Two other categories are rising significantly faster than the general index - which stands at 0.3% - namely 'Other goods and services' and 'Hotels, cafes and restaurants'.

After the rebound observed since the beginning of the year, the rise in the Industrial Price Index stopped dead in the summer, with August recording a fall of 0.1%. Meanwhile, new housing prices again collapsed, registering falls of more than 10% at the municipal, regional and national levels, though it was the national index which saw the heaviest decline, of around 12%.

The internal devaluation through the stagnation or decline of labour costs is making itself felt with greater intensity in Spain as a whole - where unit labour costs have indeed been reduced by 0.3 percentage points and have fallen during four consecutive quarters- than in the Madrid Region, where they rose by 1.1%, despite the fact that the two aggregates show a similar trend.

1.6. Labour market

The city of Madrid's labour force declined by 5% (84,500) YoY during the second quarter of 2013. Moreover, it was down by 1.9% (30,600) compared to the previous quarter. Thus, the total number of active workers has fallen back to the levels of early 2005. The activity rate stands at 60.5%, registering a fall of nearly one percentage point compared to the previous quarter and just below the levels of 2012.

In September 2013, Social Security enrolment in the city of Madrid fell by 3.1% in YoY terms, to 1,640,392. The pace of job destruction, measured as the average of the YoY rate in the last twelve months, stands at 2.8%, meaning that this negative trend is accelerating. A slight improvement is forecast for the fourth quarter, compared with the previous quarter.

With regard to registered unemployment, there has been a clear slowdown of the YoY growth in the last ten months. Forecasts for the fourth quarter of 2013 indicate that this slowdown, which began in December 2012, could moderate in the last month of the year. This would mean growth rates in October, November and December of 1.2%, 0.4% and 0.9%, respectively.

2. Monographic report

INTRA-CITY IMBALANCES AND REBALANCING IN MADRID: 2013 ANALYSIS¹

The dynamics of activities and the population habitually give rise to intra-city imbalances that involve various kinds of problems such as inequality, segregation, dysfunctions, misalignments, etc. This leads to the urban structure and form diverging from what is desirable, according to socially shared principles. Given that these manifest themselves in many different ways and may have serious consequences, urban governance requires these imbalances to be monitored in order to evaluate them and to orient corrective policies.

To that end, an analysis of the intra-city imbalances in Madrid in 2013 and the changes with respect to 2012 has been carried out, seeking to provide an evaluation based on criteria of cohesion and socio-spatial integration, territorial competitiveness and efficiency, environmental sustainability, quality of life and well-being, socio-spatial equity and environmental justice. The review is based on 18 indicators for districts, relating to major urban components and activities, such as population, economy, housing, transport and the environment. As a synthesis of the findings, the following are worthy of note:

1. Nine indicators (the same number as in 2012) show low intra-city inequalities, as they have a coefficient of variation (CV) < 0.2 while six others are in the range 0.2-0.4, categorized as medium-low or medium. Of the remainder, two (as in 2012) are slightly above 0.4 (medium or medium-high) and only one stands significantly above the rest; this is the proportion of recipients of supplementary benefit, which shows an uneven distribution of economic insecurity among districts and also shows a parallel response to attend them.

2. Comparing the 2013 situation with that of the previous year, it can be seen that of the seventeen indicators, nine have seen little variation in the CV, as the changes are $< |0.01|$. In four of them, internal differences have increased by between one and two hundredths, pointing to somewhat more unbalanced situations. This relates to economic indicators, a reflection of the current crisis. The largest increases in the CV emerge in the air pollution indicators, even though they are improving or already acceptable. Although the imbalances are lower in a few indicators, on the whole the differences between districts have tended to increase (by small amounts), a trend that should be monitored.

¹ Antonio Moreno Jiménez, *Catedrático de Geografía Humana*. Julio Vinuesa Angulo, Rosa Cañada Torrecilla y Pedro Martínez Suárez, *Universidad Autónoma de Madrid*.

TOURISM AT A CROSSROADS AS AN ECONOMIC MOTOR FOR MADRID¹

The autumn of 2013 has elevated tourism into a top priority for the city of Madrid, given the results of a summer marked by further declines in demand and corporate profitability. The situation of tourism in Madrid requires a profound and careful analysis, to promote a set of measures aimed at strengthening its competitive capacity in a comprehensive manner, to achieve better business outcomes and a greater social benefit for Madrid's society as a whole.

The analysis of the information available on tourism in Madrid from 2008 to 2013 allows significant conclusions to be reached, which can guide the current debate on where to focus medium and long-term efforts to convert tourism into one of the pillars of the development of Madrid's economy and society.

Madrid is not taking advantage of all its opportunities to make tourism an economic motor of the city: in the last five years, its performance has been worse than other European cities of the same size and worse than the average for urban tourism in Spain

Decisions with regard to transport infrastructure policy have had a major impact on the recent performance of tourism in Madrid. The deterioration of tourism demand in Madrid has occurred mainly in the past year and a half, coinciding with a complex combination of factors that have affected the logistics of air passenger transportation to the capital.

On the other hand, Madrid's international positioning has hampered the performance of tourism demand and the situation of oversupply in some sub-sectors has led to a reduction in prices, with a direct negative effect on business results.

The chances of success of any proposal seeking to interrupt this trend depends on making decisive progress in the following 8 fields of opportunity for tourism in the capital:

1. **WANTING TO BE A leading world TOURISM DESTINATION.** This means incorporating the tourism dimension into all the decisions that affect its attraction as a tourist destination, from public policies to business decisions and the attitudes of the public.
2. Define the city's offer of tourism **PRODUCTS** and integrate its various service providers, both public and private, to generate excellent experiences.
3. Maintain the commitment to a **LIVEABLE CITY** as the best setting for the enjoyment of a holiday, taking advantage of the opportunities offered by the review of the General Urban Development Plan.

¹ Óscar Perelli del Amo, *Director del Área de Estudios e Investigaciones de Excetur*

4. To make **MOBILITY** another resource in Madrid's tourism offer, opting resolutely for the systems with the lowest environmental impact.
5. Design a **CONNECTIVITY STRATEGY** to invest in effective connections between the airports and high-speed rail lines, incorporate the attraction of priority tourist markets in the aims of airport management and promotion, and analyze the potential implications of the privatization of AENA (the airports authority) for Madrid's tourism.
6. Continue moving toward a more targeted and segmented **MARKETING** based on **DIRECT CUSTOMER CONTACT**.
7. Update the city's system of tourism governance on the basis of integrating the private sector and the principles of increased market orientation and use of technology.
8. Work on the **SOCIAL AWARENESS** of the role of tourism and in the generation and attraction of the **BEST TALENT** to the industry.