REINO DE ESPAÑA

ES SOVEREIGN

A ISSUER RATING
Long term

OUTLOOK
Stable

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Rating Action and Rationale

EthiFinance Ratings upgrades the Kingdom of Spain's unsolicited long-term rating from A- to A, maintaining a Stable outlook.

The rating upgrade reflects a methodological change resulting from the recent update of the EthiFinance Ratings' sovereign long-term rating methodology. In addition, the rating is supported by a favorable macroeconomic environment and a robust socioeconomic and external sector profile. This strength is further bolstered by a strong ESG assessment, affirming the sovereign's capability and commitment to fulfilling its payment obligations. Although significant challenges remain.

The Kingdom of Spain (hereinafter Spain) enjoys a generally favorable socioeconomic situation, with a relatively large and diversified economy. It has shown resilience in the face of a recently deteriorating macroeconomic environment, maintaining above eurozone average growth. The external sector, meanwhile, benefits from Spain's inclusion in the eurozone, which provides the country with a globally recognized and stable currency. Moreover, Spain has maintained current account surpluses. Nevertheless, these strengths are constrained by its international position as a debtor.

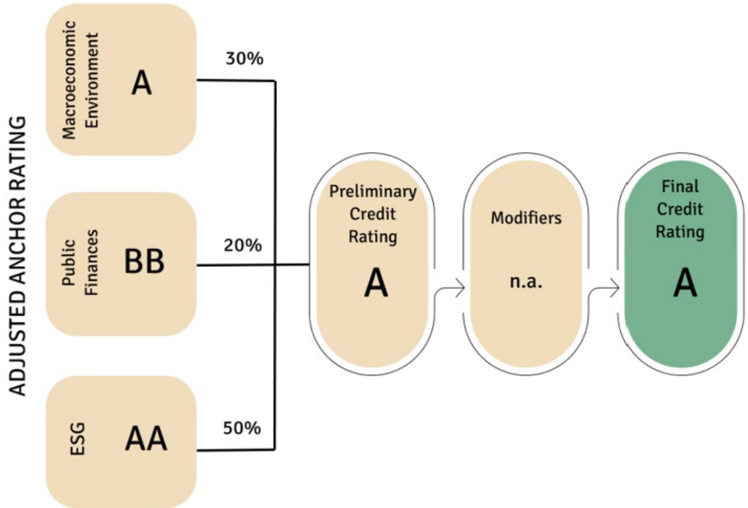
However, Spain continues to face structural challenges such as high unemployment rates and an aging population. Also, the situation of its public finances poses the main constraint on the credit rating. The consistently elevated levels of public sector deficit, which worsened during the pandemic, represent a significant risk, while debt levels –although declining in relative terms- are high.

The financial system is assessed to be adequate, characterized by controlled non-performing loans (NPL) rates and high capitalization levels. However, the overall assessment of the financial and monetary policy situation is unfavorable. This is due to the low profitability of the financial system and the escalation of inflation experienced in recent years.

Spain has a favorable ESG profile, particularly excelling in the realms of social and governance aspects. In terms of social factors, the country benefits from prominent levels of human development and robust social well-being indicators. Regarding governance, the quality of its institutions is noteworthy, although there is concern over increased political uncertainty due to high parliamentary fragmentation. This situation could hamper political predictability and the effective implementation of policies.

Furthermore, the country confronts significant transition risks, stemming from high greenhouse gas emissions and a still modest share of renewable energy in its consumption mix. Nonetheless, Spain is on track to meet the environmental objectives established by the European Union (EU).

FIGURE 1: DERIVING THE CREDIT RATING



Consequently, the country's credit rating is categorized as follows:

Spain's credit rating of A is derived from the individual assessment of three pillars as outlined in our methodology: the *Macroeconomic Environment Pillar* (adjusted anchor rating of A), the *Public Finances Pillar* (adjusted anchor rating of BB), and the *ESG Pillar* (adjusted anchor rating of AA).

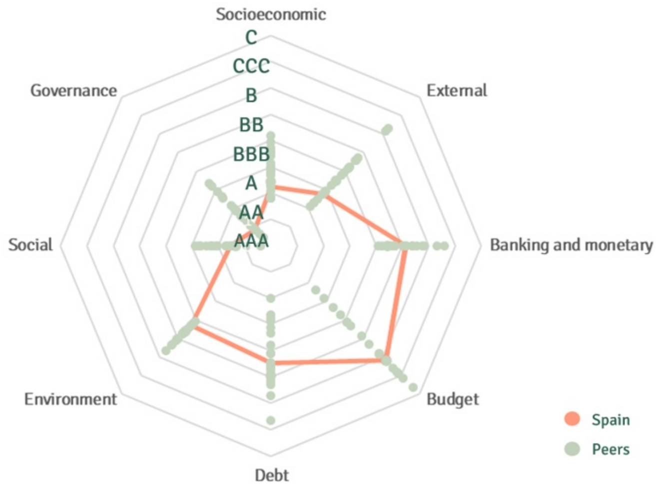
Starting with the *Macroeconomic Environment Pillar,* the assigned credit rating reflects Spain's strong *Socioeconomic* standards and robust *External Sector*. However, the *Financial Sector & Monetary Policy* is negatively impacted by the surge in inflation and low profitability levels, while *Public Finances* are the main constraint due to the high level of fiscal imbalances and public sector debt.

As a double materiality rating agency, we consider ESG factors to be crucial to obtain a complete understanding of a country's credit quality from a medium-to-long term perspective.

We assign to Spain a favorable ESG assessment, explained by the sovereign's high *institutional and governance* quality (adjusted anchor rating of A), complemented by a high level of *social* welfare (adjusted anchor rating of AAA). Nonetheless, our ESG assessment is constrained by the *environmental* pillar (adjusted anchor rating of BBB+), albeit with a positive trend.

Finally, the double-entry table has no impact on the rating, as our methodology determines that the macro fiscal and ESG profiles are aligned.

FIGURE 2: ANCHOR RATING BY SUB-PILLAR. EURO ZONE PEER COMPARISON



Modifiers

For this credit analysis, we have not applied any modifiers as no extraordinary situations with immediate impact on the sovereign credit situation have been identified.

Main Figures

	2020	2021	2022	2023	2024E	2025E
Real GDP (% change)	-11.2%	6.4%	5.8%	2.5%	2.4%	2.0%
GDP per capita (current, €)	24,902	27,531	30,199	33,308	34,788	35,930
CPI (annual change, %)	-0.3%	3.1%	8.4%	3.4%	3.1%	2.3%
Unemployment rate (% labor force)	15.5%	14.9%	13.0%	12.2%	11.6%	11.1%
Dependence ratio (<19 and >65 y/20-64 y)	51.8%	51.6%	51.6%	50.9%	-	-
NPLs	4.5%	4.2%	3.5%	3.55%	-	-
ROA (financial sector)	0.5%	0.5%	0.4%	0.4%	-	-
Current Account Balance (% GDP)	0.6%	0.8%	0.6%	2.6%	2.8%	2.9%
NIIP (% GDP)	-85.5%	-78.3%	-63.8%	-55.6%	-	-
Fiscal Balance (% GDP)	-10.1%	-6.9%	-4.5%	-3.6%	-3.6%	-2.9%
Public Debt (% GDP)	120.4%	118.3%	113.2%	107.7%	105.5%	104.8%
CO2 emissions per capita	4.9	5.3	5.5	-	-	-
Consumption of Renewable Energy	21.2%	20.7%	22.1%	-	-	-
Human Development Index	0.9	0.9	0.9	-	-	-
Gini Index	32.1	33.0	32.0	31.5	-	-
World Governance Indicators *	73.8	74.4	73.2	-	-	-

* Average of the 6 main World Bank World Governance Indicators: rule of law, regulatory quality, voice & accounting, government effectiveness, level of corruption, and political stability.

Fundamentals

Strengths

- Relatively large and diversified economy, demonstrating resilience to shocks such as rising energy prices and interest rates.
- Favorable external sector position due to eurozone membership and sustained current account surpluses, contributing to an improving trend in the net international investment position as a debtor, though this is still elevated.
- Strong social and governance profile, with high social welfare and human development, and a high-quality institutional framework.

Weaknesses

- High dependency rate aggravated by an ageing population, which poses a future risk to public finances.
- Large fiscal deficit and public debt levels, which, although presenting a correction trend, primary deficits will persist, resulting in a continuous growth of debt in absolute terms.
- High exposure to transition risks due to significant per capita greenhouse gas emissions, albeit on a decreasing trend and in line with the trajectory set by the EU to meet environmental targets.
- High level of parliamentary fragmentation and reduced political predictability following the July 2023 general election, with potential difficulties in the adoption of structural reforms.

Outlook

Our Stable outlook is based on our expectation that the fundamentals of the rating will remain broadly unchanged over the next 12 months. There are in some areas positive trends, particularly in terms of economic growth and employment dynamics, alongside the anticipation of increased fiscal consolidation following the reintroduction of EU fiscal rules. However, these factors are counterbalanced by heightened uncertainty in the global landscape, with various geopolitical risks that could fuel persistently high inflation. Also, while ECB monetary policy has begun to be eased, the potential delayed effects of high interest rates could weigh on the macroeconomic environment, alongside a political landscape that may pose governance challenges for the country.

Sensitivity Analysis

Detailed below are the factors that individually or collectively would impact Spain's rating:

Positive factors (↑).

The credit rating and/or outlook could be upgraded if inflation maintains a decreasing trend and stabilizes around the ECB's 2% target. Likewise, a significant reduction in fiscal deficit, approaching budgetary balance, would be favorable. While achieving a reduction in public sector debt to below the 60% threshold would have a positive impact, it is considered unlikely due to the necessary adjustments. Finally, improvements in the political landscape that might facilitate reform implementation could also positively affect the rating.

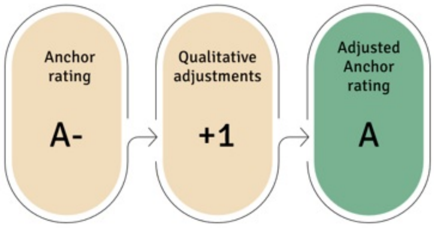
Negative factors (↓).

The credit rating and/or outlook could be downgraded if the risk factors -such as the rise in prices and the monetary tightening- ultimately weigh on the economy and it registers below-potential growth, consequently impacting other rating fundamentals such as the labor market and public finances. Furthermore, further deterioration in public finances, characterized by persistent deficits exceeding the 3% threshold, could also lead to a negative rating action.

Rating Committee

The rating committee agreed to upgrade the rating with a stable outlook. The main issues discussed by the committee included the impact of the new methodology, the macroeconomic performance of the Spanish economy and its impact on the fiscal path and the ESG and government situation, among others.

Macroeconomic environment pillar



The *Macroeconomic Environment Pillar*, anchor rating (A-) assigned is based on the assessment of three sub-pillars as defined in our methodology: *Socioeconomic* (anchor rating of AA-), *External Sector* (anchor rating of BBB+), and *Financial Sector & Monetary Policy* (anchor rating of BB+).

Positive qualitative adjustments bring up the Macroeconomic Environment's adjusted anchor rating to A, as explained below.

Regarding the first sub-pillar, Spain has a continuing favorable **Socioeconomic** profile characterized by: i.) a large and diversified economy; and ii.) the economy's resilience in the face of a tougher macroeconomic landscape, maintaining robust growth levels in 2022 (5.8%) and 2023 (2.5%).

The Spanish economy has maintained robust growth momentum in recent years, returning to pre-pandemic GDP levels by the end of 2022. Despite a complex macroeconomic environment marked by uncertainty, rising inflation, and high interest rates, the economy has progressed favorably. This resilience is attributed to Spain's service-oriented economy, which is less exposed than others to commodity price increases and high interest rates. Additionally, a strong exports performance has been supported by a resilient tourism sector, despite slowdowns observed in other parts of Europe, while, robust employment levels, complemented by expansive fiscal policies, have bolstered household consumption. Thus, the key drivers of Spanish growth have been both external and domestic demand, particularly from public and household consumption, while the industrial sector continues to face challenges.

We anticipate that economic momentum will continue to strengthen through 2024 and 2025. Projections suggest growth will surpass its potential rate of 1.7%. EthiFinance Ratings forecasts annual growth rates of 2.4% for 2024 and 2.0% for 2025. This is driven by strong domestic demand and bolstered by ongoing resilience in the labor market and the gradual easing of financing conditions following initial interest rate cuts. Moreover, the implementation of the Recovery and Resilience Plan (RRP) is expected to stimulate substantial investment growth throughout our forecast period (two years).

Nevertheless, Spain will continue to experience elevated unemployment rates, which, although showing a declining trend, remain above 10%. The nation concluded 2023 with an unemployment rate of 12.2%, down from 13% in 2022, with expectations of a decrease to 11.6% in 2024 and to 11.1% in 2025, according to the European Commission. Concurrently, employment has also shown favorable progress, reaching a historical high with 21.1 million registered workers.

High dependency ratios also represent a negative factor. In 2023, Spain recorded a dependency ratio of 50.9%, which puts downward pressure on its credit quality. An aging population could lead to heightened fiscal challenges, driven by rising expenditure on pensions and healthcare, as well as reduced economic productivity. These factors have the potential to impact the sovereign's long-term ability to fulfill its financial obligations.

Spain's **External Sector**—the second sub-pillar—receives a favorable rating, primarily attributed to its inclusion in the eurozone, which provides it with a globally recognized and stable currency.

Spain consistently registers a current account surplus. Despite experiencing declines during the pandemic, due to reduced tourism and global trade, as well as in 2022 due to an increased energy deficit (see Annex Figure 1), the surplus recovered in 2023, reaching 2.6% of GDP. A continued strong performance of tourism, coupled with the recovery of its key trading partners, is expected to sustain the current account surplus at favorable levels. The European Commission forecasts it to be around 2.8% in 2024 and 2.9% in 2025.

Nevertheless, Spain remains a significant international debtor, with a net international investment position (NIIP) of -70.8% of GDP during the 2020-23 period, stemming from macroeconomic imbalances following the 2008 crisis. While there is an improving trend, supported by both private and public deleveraging, robust growth in service exports and nominal GDP advancement, Spain's high level of international indebtedness remains a concern.

Regarding the third sub-pillar, **Financial and Monetary Policy**, our assessment factors in both financial system and monetary policy situation.

Spain's banking sector remains in a sound position, with a robust level of capitalization with a CET1 ratio of 12.7% in

2023, and a limited NPL ratio of 3.5% of total gross loans for the same year. Moreover, this ratio has remained stable and even declined (from 4.2% in 2021 to 3.5% in 2022) despite the rise in interest rates. However, one of the main challenges has been the banks' limited profitability in an environment until recently of persistently low interest rates. Nonetheless, they have benefited from the recent uptick in interest rates, with return on assets (ROA) rising to 1% in 2023, up from 0.9% in 2022, according to the IMF.

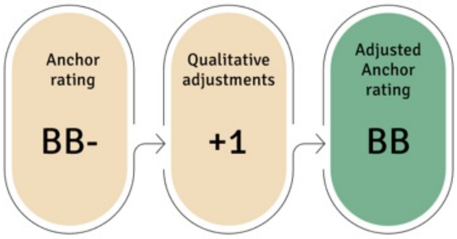
Regarding monetary policy, headline inflation in Spain surged to 8.4% in 2022, exceeding that of neighboring countries. This spike was primarily due to the structure of its electricity market, where variable contracts are predominant, rendering consumer bills highly sensitive to fluctuations in the energy market. Additionally, these price pressures eventually spread to other goods and services, keeping prices elevated into 2023, with a rate of 3.4%.

Despite the stability of the financial system, the assessment of the financial system and monetary policy sub-pillar faces challenges due to persistent inflationary pressures. We anticipate that Spanish inflation will remain high, influenced by sustained high service sector inflation driven by robust demand and secondary effects from wage increases. Also, the base effect from the cessation of certain measures, such as reductions in VAT on energy bills, will contribute to inflationary pressures. Consequently, at Ethifinance Ratings, we expect inflation to stabilize around 3.1% in 2024, aligning more closely with the European Central Bank's (ECB) target by 2025, declining to 2.3%.

The tightening of financing conditions represents a risk, albeit one deemed limited. Expected increases in NPLs due to higher credit costs could potentially be mitigated by enhanced bank profitability. Moreover, in June, the ECB implemented its first interest rate cut of 25 basis points, lowering the rate to 4.25%. Although no significant shifts in monetary policy are anticipated amid persistent inflation, another similar rate cut is projected by year-end, which could slightly alleviate any emerging risks on this front.

Finally, the Macroeconomic Environment's anchor rating (A-) is positively adjusted by one notch (to an adjusted anchor rating of A) due to, among others, three key aspects: i) Spain's large and diversified economy, with growth expectations running above its estimated potential rate; ii) a flexible exchange rate regime, characterized by consistent current account surpluses and a favorable export structure where no sector accounts for more than 25% of Spain's international trade; and iii) a stable financial system anchored by a credible central bank, while inflation is converging to target over the next three years.

Public Finance Pillar



The *Public Finances Pillar's*, with an anchor rating of BB-, reflects the most significant risk to the sovereign's credit quality, primarily due to the poor performance of both sub-pillars: i.) Budget (anchor rating of B+), characterized by persistently high fiscal imbalances; and ii.) Public Debt (anchor rating of BB+), reflecting elevated debt levels, albeit with these showing a decreasing trend in relative terms.

Positive qualitative adjustments bring up the Public Finance's adjusted anchor rating to BB, as explained below.

The **Budget sub-pillar** is constrained by substantial deficits and increased expenditure in recent years. While the Spanish public finances have benefited from the expiration of some pandemic-related measures—the deficit rose to 10.1% of GDP in 2020—and robust revenues growth driven by economic recovery and inflation, deficits remained elevated. This was especially evident with the launch of new assistance packages aimed at mitigating the effects of the price surge, particularly for energy. Consequently, although the deficit is showing a declining trend (see Annex Figure 2), it remains high, at 3.6% in 2023.

However, we anticipate the continuation of the correction trend in the coming years, with the deficit potentially falling below the 3% threshold set by fiscal rules by 2025 (estimated at 3.5% for 2024 and 2.9% for 2025). Additionally, the budgetary situation benefits from the 2023 budget extension, which provide some expenditure containment, while revenue is expected to improve alongside anticipated economic growth.

Thus, although fiscal rules are reinstated, they do not pose a serious risk to the sovereign rating in the short term, as fiscal consolidation is expected to continue at a steady pace, closely aligned with adjustments outlined by the EU.

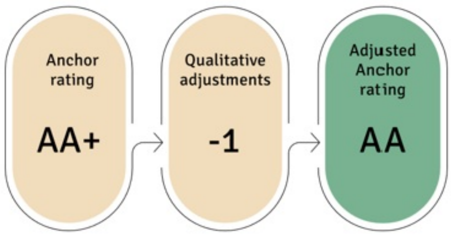
Assessment of the second sub-pillar, **Public Sector Debt**, reflects the persistently high levels, albeit here too there is an improving trend in relative terms.

With the onset of the pandemic, the Spanish debt surged to 120.4% of GDP, driven by increased deficits and GDP contraction. Since then, there has been some normalization, with the percentage declining to 107.7% in 2023. This trend is expected to continue, albeit gradually, with debt estimated by the Commission to reach 105.5% in 2024 and 104.8% in 2025. This is primarily based on anticipated nominal GDP growth, while volume growth is expected to persist due to ongoing primary deficits.

Although the country demonstrates elevated short-term debt issuance (6.1% in 2022), within the ranges defined in our methodology, this risk is offset by sufficient market access and a lengthy average maturity of approximately 8 years. Furthermore, despite increased expenditure due to the rise in interest rates, the sustainability ratio remains manageable, and is expected to hover around 6% of current revenues for the 2024-25 period, buoyed by robust revenues.

Lastly, our qualitative assessment underscores a 1 notch positive impact to an adjusted anchor rating of BB, supported by: i) the country's strong debt allocation capacity, with adequate market access and low foreign currency debt issuance; ii.) adequate liquidity levels, with liquid assets exceeding 10% of GDP; and iii.) expectations for sustained fiscal consolidation, with adherence to budgetary objectives anticipated over the next five years.

ESG Pillar



Our favorable *Environmental, Social, and Governance (ESG) Pillar* assessment (anchor rating of AA+) is supported by the country's robust social welfare system (anchor rating of AAA) and is enhanced by high-quality institutional and governance standards (anchor rating of AA+). However, the ESG assessment is limited by the environmental pillar (anchor rating of BBB-), due to significant transition risks associated with high levels of emissions, although it is anticipated that Spain will meet the main EU environmental targets for 2030.

The *ESG pillar* overall anchor rating is negatively adjusted to an adjusted anchor rating of AA due to political uncertainty and parliamentary fragmentation, as we detail below.

The **Environmental sub-pillar's** anchor rating (BBB-) reflects Spain's substantial transition risks due to high greenhouse gas emissions, posing challenges to economic stability and public finances. Despite this, Spain's emission reduction efforts and growing renewable energy consumption are promising, aligning with EU objectives. The country's high levels of environmental protection and robust risk management capabilities further enhance its environmental stability.

Spain's greenhouse gas emissions were recorded at 5.5 metric tons per capita in 2022. This presents a potential downside to its sovereign rating, stemming from economic impacts and public finance challenges linked to green transition investments or the failure to meet environmental objectives outlined in international agreements such as the Paris Accord and EU directives. Additionally, businesses are poised to encounter additional challenges as they will cease to receive free emission allowances starting in 2026.

Nevertheless, the country's trajectory in reducing emissions is on track, with a 19.7% reduction already achieved in 2022 (from 2005 levels) in the sectors involved under the Effort Sharing Regulation. Moreover, it is projected that with current policy measures and additional actions outlined in its National Energy and Climate Plan, the nation will exceed its target for reducing greenhouse gas emissions in these sectors, namely a reduction of 44.7% by 2030, surpassing the initial target of 37.7%. However, reductions in Land Use, Land Use Change, and Forestry (LULUCF), measured as net GHG removals in Mt. CO_2 eq., are expected to fall short of the 43.6 removals target, currently estimated at 34. Overall, the latest projections indicate that transition risks are expected to remain manageable, mitigating concerns over potential deviations from set emission reduction targets.

Spain's current energy mix presents a moderate risk, with renewable energy accounting for 22.1% of total energy consumption in 2022. Although the current figure may seem modest, the growth trajectory—from 17.8% in 2019—demonstrates alignment with the EU's long-term objectives for renewable energy adoption. Furthermore, it is projected that Spain will not only meet but exceed its 2030 goal of 43% renewable energy, with estimates suggesting it will reach 47.9%. Consequently, the trend for this indicator is considered to be positive.

TABLE 1: MAIN ENVIRONMENTAL ACTIONS

Rating Category	Main Actions	EthiFinance's Assessment
Transition risks	Measures including the **PREE** or **CRECE** program, tax deductions, and regional subsidies have been put in place to improve building efficiency.	In progress but challenges remain
	Various measures have been implemented to reduce emissions in transportation, including economic incentives such as the MOVES III Plan, low-emission zone laws for municipalities with over 50,000 inhabitants, and a hydrogen investment strategy under the RRP. Nevertheless, the country would benefit from increased investments in public transportation, particularly in rural areas.	In progress but challenges remain
Energy	Spain has made significant progress in the development of renewable energies, with wind power being the primary source. It is expected that renewable energy generation will reach 81% of total electricity generation in the country by 2030.	In progress
Protected areas	The level of biodiversity protection is adequate, although the country has presented environmental investment below its needs (estimated at EUR 18.6 billion compared to the reported EUR 7.7 billion) in the past.	Some challenges remain
Physical risks	Spain is implementing several policies to mitigate physical risks from climate change, integrating mitigation, adaptation, and nature restoration measures into its energy and climate planning. These actions include green infrastructure projects, riverbed expansions, and forest planning to enhance resilience against extreme weather events.	In progress but challenges remain

Environmental risks are partially mitigated by a high level of environmental protection. As of 2023, 28.1% of terrestrial areas are protected, and there is an expected increase in protected marine areas from 12% to 21% in 2024, following the latest expansion of marine spaces included in the Natura 2000 network—a European Union-wide network aimed at conserving biodiversity. In addition, Spain boasts the largest terrestrial Natura 2000 network in the EU. These proactive conservation measures contribute to sustainable environmental management, thereby enhancing the country's environmental stability.

Likewise, Spain's exposure to physical risks from climate change is mitigated by the relatively low significance of its primary sector, accounting for an average of 2.6% of GDP between 2019 and 2022, coupled with its high capacity to manage such risks.

Although an increase in the frequency of extreme weather events is anticipated, and Spain's geographic location renders it particularly susceptible to phenomena such as rising temperatures, wildfires, droughts, and flooding, these factors are not considered significant short-term determinants of credit quality. This is due to Spain's limited reliance on the primary sector and its robust risk management capabilities, as evidenced by the INFORM Risk Management Index, one of the indicators considered in our assessment.

However, these risks are recognized as contingent liabilities in our credit rating framework. Spain's response mechanisms include the *Consorcio de Compensación de Seguros* (CCS), a public reinsurer that covers damage from extreme natural events like wildfires or floods. Moreover, the Spanish government subsidizes agricultural insurance premiums through the *Entidad Estatal de Seguros Agrarios* (ENESA), which means that heightened climate-related risks could translate into increased expenditure. Therefore, although the impacts of physical risks on the real economy are contained, they may exert additional pressure on public finances, a concern given Spain's already limited fiscal room to manoeuvre.

Regarding the **Social sub-pillar**, the anchor rating (AAA) is positioned in the top quintile according to our methodology. This top-tier rating reflects the presence of an efficiently functioning welfare state and substantial economic development, contributing to elevated social well-being and human development.

In terms of the Human Development Index (HDI), Spain ranks 27th among the 193 countries assessed by the United Nations, classified within the "very high" category. This reflects a high life expectancy, which stood at 83.9 years in 2022. Additionally, there has been notable improvement in wealth levels, although they still trail behind other major economies in the eurozone (see Annex Figure 3). Regarding education, the average expected years of schooling and mean years of actual schooling are high (17.8 years and 10.6 years, respectively, in 2022), yet a significant disparity between these figures is observed.

Likewise, the level of vulnerable unemployment is low, around 10.5% of employment in 2022, and has been on a downward trend, albeit one temporarily disrupted by the pandemic—spiking to 11.5% in 2020. The decreasing trend in unemployment has been supported by successive increases in the minimum wage, from €645.3 per month in 14 payments in 2014, to €1,134 in 2024.

However, income and gender inequality levels slightly weaken Spain's social profile, which is also reflected in the SDG 10 -reducing inequalities- assessment (see Table 2). In this regard, Spain recorded a Gini Index of 0.32 points (with 1 representing the highest level of inequality) during the period from 2020 to 2023, although the Index shows a decreasing trend. Moreover, gender disparities continue to exist, with a gap of 16.7 percentage points between men and women in employment during the same period.

In addition, we identify certain areas where improvements could be made:

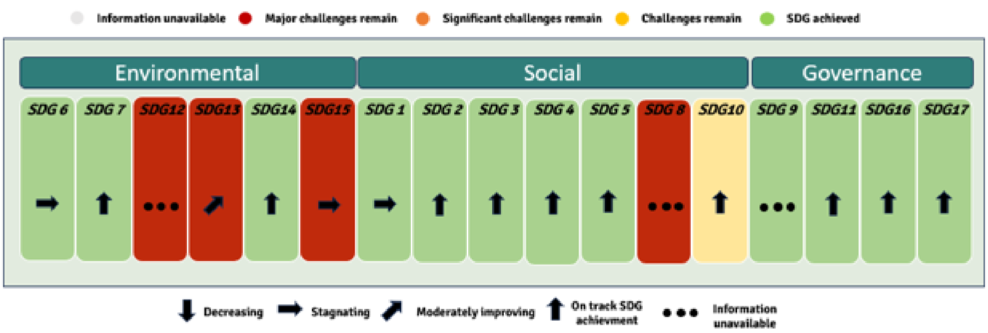
Firstly, poverty risk levels are high relative to the country's development, exacerbated by the challenges in housing accessibility. Spain had the highest AROPE rate in the eurozone in 2023, at 26.5%. These socioeconomic issues are intensified by escalating living costs and the difficulties associated with housing access and high unemployment rates. There is a significant loss of purchasing power, regular increases in rental prices, and higher mortgage payments, all of which have worsened affordability issues, especially for vulnerable households.

Moreover, regional disparities are pronounced, with significant variations in income, unemployment, and access to services between regions (see Annex Figure 4). Regions such as Andalusia and Extremadura face higher poverty and unemployment rates compared to more affluent regions like Madrid and Catalonia. These disparities contribute to uneven economic development and social cohesion across the country.

Third, education remains a potential risk area. Spain has one of the highest school dropout rates in the EU, recorded at 13.7% in 2023, although this rate has decreased from 17.3% in 2019. Furthermore, the latest PISA report shows Spanish students performing below the OECD average in mathematics and only close to average in reading, highlighting the need for improvements in academic performance. Additionally, there is a mismatch between the labor market's needs and educational outcomes, with the proportion of STEM graduates being below the EU average (19.5% of university graduates compared to 26%).

Finally, the **Governance sub-pillar** assessment is generally favorable, with an assigned anchor rating of AA+. This is primarily attributed to Spain's high score on the World Bank's Governance Indicators, reflecting the country's strong institutional quality and governmental standards, albeit in the context of broad international comparison. When compared to European peers (see Annex International Comparison), Spain's assessment falls below average.

TABLE 2: SGD ACHIVEMENTS



Source: SDG report ranking.

Furthermore, attention is drawn to the recent deterioration in the Political Stability indicator. While Spain typically scores lowly in this area, averaging 55 in recent years, there was a temporary improvement post-2019, the score surpassing 60, before declining to 53 in 2022. This decline correlates with our qualitative assessments, reflecting Spain's trend towards political polarization, notably evident in the fragmented composition of the Congress of Deputies.

Following the July 2023 elections, parliamentary fragmentation became even more pronounced, with no single bloc securing a clear majority. This led to the continuation of Socialist President Pedro Sánchez's tenure, supported by the far-left Sumar party, albeit reliant on ad-hoc alliances -sometimes with pro-independence parties- for investiture and lacking guaranteed support. This has hindered the implementation of structural measures such as unemployment subsidy reforms and approval of the 2024 budget, leading to the extension of the 2023 budget.

In light of these developments, the ESG Pillar anchor rating (AA+) is adjusted downward by one notch to an adjusted anchor rating of AA following EthiFinance Ratings' qualitative analysis. This adjustment reflects diminished policy predictability and effectiveness in the current political landscape following the 2023 general election.

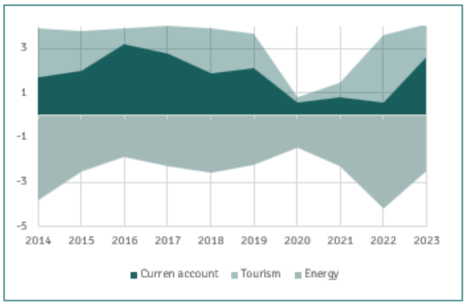
Annexes

Main Figures: International Comparison

	Year	Spain	Portugal	France	Italy	Ireland
Real GDP (% change)	2024[E]	2.0%	1.7%	0.7%	0.9%	1.2%
GDP per capita (current, €)	2023	33,308	25,733	40,799	35,349	95,285
HCPI (interannual change, %)	2024[E]	3.1%	2.3%	2.5%	1.6%	1.9%
Unemployment rate (% labour force)	2024[E]	11.6%	6.5%	7.7%	7.5%	4.4%
Dependency rate (% 20-64 yo population)	2023	50.9%	58.4%	62.5%	57.4%	52.7%
NPL	2022	3.5%	3.3%	2.3%	2.8%	2.3%
ROA	2022	0.9%	0.7%	0.4%	0.7%	1.2%
Current Account Balance (% GDP)	2024[E]	2.8%	0.8%	-1.4%	-1.3%	9.1%
NIIP (% GDP)	2023	-55.6%	-75.9%	-29.1%	5.7%	-109.1%
Fiscal Balance (% GDP)	2024[E]	-3.5%	0.4%	-5.3%	-4.4%	1.3%
Gross Public Debt (% GDP)	2024[E]	105.5%	95.6%	112.4%	138.6%	41.3%
CO2 emissions (metric tons per capita)	2022	5.5	5.3	5.7	6.7	13.1
Consumption of Renewable Energy (% total final energy consumption)	2022	22.1%	34.7%	20.2%	19.1%	13.1%
Human Development Index	2022	0.91	0.87	0.91	0.90	0.95
Gini Index	2023	31.5	33.7	29.7	31.5	27.4
World Governance Indicators	2022	73.2	80.1	80.2	67.4	91.5

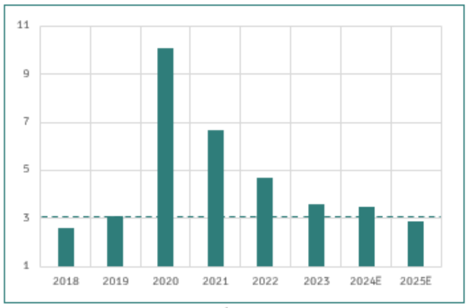
Figures

FIGURE 1. EVOLUTION OF CURRENT ACCOUNT, ENERGY BALANCE, AND TOURISM BALANCE (2014-2023, % OF GDP)



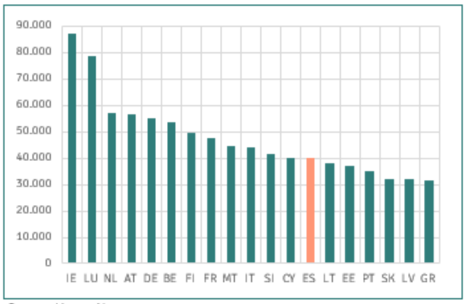
SOURCE: BANK OF SPAIN

FIGURE 2. PUBLIC DEFICIT EVOLUTION (2018-2025E, % OF GDP)



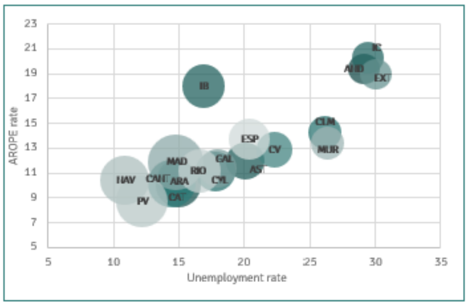
SOURCE: AMECO & ETHIFINANCE RATINGS' FORECASTS

FIGURE 3. GROSS NATIONAL INCOME PER CAPITA (2022, CURRENT €)



SOURCE: UNITED NATIONS

FIGURE 4. SOCIOECONOMIC DISPARITIES IN SPANISH REGIONS 2022: UNEMPLOYMENT VS. POVERTY (BUBBLE SIZE: GDP PER CAPITA)



SOURCE: INE

Sources of information

The credit rating issued in this report is unsolicited. The main sources of information used are the following:

1. Public information from public access sources, mainly official statistics institutes, central banks, and other government sources, in addition to the OECD, Eurostat, World Bank, European Central Bank and International Monetary Fund, among others.
2. Own information of EthiFinance Ratings.

The information was thoroughly reviewed to ensure that it is valid and consistent, and is considered satisfactory. Nevertheless, EthiFinance Ratings assumes no responsibility for the accuracy of the information and the conclusions drawn from it.

Level of the rated entity participation in the rating process

Unsolicited Credit Rating	
With Rated Entity or Related Third Party Participation	NO
With Access to Internal Documents	NO
With Access to Management	NO

Additional information

- The rating was carried out in accordance with Regulation (EC) N°1060/2009 of the European Parliament and the Council of 16 September 2009, on credit rating agencies. Principal methodology used in this research are :
  - Sovereign Rating Methodology : https://www.ethifinance.com/download/sovereign-rating-methodology?wpdmdl=32015
- The rating scale used in this report is available at https://www.ethifinance.com/en/ratings/ratingScale.
- EthiFinance Ratings publishes data on the historical default rates of the rating categories, which are located in the central statistics repository CEREP, of the European Securities and Markets Authority (ESMA).
- In accordance with Article 6 (2), in conjunction with Annex I, section B (4) of the Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009, it is reported that during the last 12 months EthiFinance Ratings has not provided ancillary services to the rated entity or its related third parties.
- The issued credit rating has been notified to the rated entity, and has not been modified since.