

January 19, 2009

Research Update:

Spain's Instituto de Credito Oficial Downgraded To 'AA+' On Sovereign Downgrade; 'A-1+' Affirmed; Outlook Stable

Primary Credit Analyst:

Lorenzo Pareja, Madrid (34) 91-389-6962;lorenzo_pareja@standardandpoors.com

Secondary Credit Analyst:

Trevor Cullinan, London (44) 20-7176-7110;trevor_cullinan@standardandpoors.com

Table Of Contents

Rationale

Outlook

Ratings List

Research Update:

Spain's Instituto de Credito Oficial Downgraded To 'AA+' On Sovereign Downgrade; 'A-1+' Affirmed; Outlook Stable

Rationale

On Jan. 19, 2009, Standard & Poor's Ratings Services lowered its long-term issuer credit rating to 'AA+' from 'AAA' on Instituto de Crédito Oficial (ICO), the Spanish state's financial agency, following a similar action today on the Kingdom of Spain (AA+/Stable/A-1+). The short-term issuer credit rating was affirmed at 'A-1+'. The outlook is stable. At the same time, the long-term rating was removed from CreditWatch, where it had been placed with negative implications on Jan. 12, 2009.

The sovereign downgrade reflects our view that public finances will suffer in tandem with the expected decline in Spain's growth prospects, and that the policy response may be insufficient to effectively counter the related economic and fiscal challenges. For further details about our sovereign rating action, see our Research Update "Kingdom of Spain Long-Term Ratings Cut To 'AA+' On Structural Weakness; Outlook Stable" published today on RatingsDirect.

The ratings on ICO are based on anticipated and continued support for the entity from the Spanish state. This expectation is amply justified, given the state's explicit guarantee and ultimate liability for all of the agency's debt and obligations. It is also supported by ICO's legal status as the state's financial agency and its importance to the Spanish government as a public-service provider.

ICO's main mission is to promote activities in line with national economic policy. It provides financial backing for small and midsize enterprises; long-term loans, chiefly for infrastructure projects; and financial support in the event of economic crises and natural disasters. It also provides and manages financial instruments to back exports and fund official development programs. At the government's request, ICO has committed €5 billion since July 2008 for guarantees on state-promoted securitized mortgage deals--and might commit another €5 billion--in an effort to stimulate Spain's state-promoted housing sector. Together with liquidity lines to several mortgage-backed securitization funds, these commitments mark an extension of ICO's business activities. ICO complements Spain's private financial system, rather than competing with it.

Given that ICO's main public-service role is to support the Spanish economy, its profitability is traditionally weak owing to the large and increasing weight of low-risk mediation loans to local banks in its asset portfolio.

Because of a noticeable increase in ICO's low-risk assets since 2005, the government injected capital into the agency in 2006 and 2007 to underpin ICO's ratio of capital to risk-weighted assets--which stood at 12.2% at end-May

2008, versus 11.2% at year-end 2007. Furthermore, the government formally stated in the 2006 budgetary law that ICO's solvency ratio must not drop below 9.5% once the Basel II capital adequacy agreement comes into force. This measure provides further evidence of the state's strong support for the agency.

Liquidity

ICO's liquidity position is adequate. The agency traditionally maintains a creditor position in the Spanish interbank market, with some €1.65 billion lent at year-end 2007. As ICO is a second-tier public financial institution, customer deposits are not relevant and a significant portion of them are for government payment purposes. ICO mainly covers its treasury needs through its medium-term note program.

Outlook

The stable outlook mirrors that on the Kingdom of Spain. The sovereign credit ratings might come under pressure if the correction in Spain's economic imbalances proceeds slowly, or large fiscal imbalances extend beyond what is necessary for countercyclical measures. Conversely, significant progress in bringing the ratio of government debt to GDP back to the 2008 level, alongside the liberalization of labor and product markets in order to increase productivity growth, improve competitiveness, and reduce unemployment, could put upward pressure on the ratings.

We do not expect any change in the key factors that justify the equalization of our ratings on ICO with those on the sovereign. These include sustained strong support from the Spanish government, the maintenance of the agency's protected legal status, and the state's explicit guarantee of ICO's financial obligations.

Ratings List

Downgraded; CreditWatch/Outlook Action

	To	From
Instituto de Credito Oficial		
Long-term issuer credit rating	AA+/Stable	AAA/Watch Neg
Senior Unsecured*	AA+	AAA/Watch Neg

Ratings Affirmed

Instituto de Credito Oficial	
Short-term issuer credit rating	A-1+
Short-Term Debt*	A-1+
Commercial Paper*	A-1+

*Guaranteed by the Kingdom of Spain.

Additional Contact:

*Research Update: Spain's Instituto de Credito Oficial Downgraded To 'AA+' On Sovereign Downgrade; 'A-1+'
Affirmed; Outlook Stable*

International Public Finance Ratings Europe;PublicFinanceEurope@standardandpoors.com

Ratings information is available to subscribers of RatingsDirect, the real-time Web-based source for Standard & Poor's credit ratings, research, and risk analysis, at www.ratingsdirect.com. It can also be found on Standard & Poor's public Web site at www.standardandpoors.com; select your preferred country or region, then Ratings in the left navigation bar, followed by Find a Rating. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow (7) 495-783-4017.

Copyright © 2009 Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P). S&P and/or its third party licensors have exclusive proprietary rights in the data or information provided herein. This data/information may only be used internally for business purposes and shall not be used for any unlawful or unauthorized purposes. Dissemination, distribution or reproduction of this data/information in any form is strictly prohibited except with the prior written permission of S&P. Because of the possibility of human or mechanical error by S&P, its affiliates or its third party licensors, S&P, its affiliates and its third party licensors do not guarantee the accuracy, adequacy, completeness or availability of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. S&P GIVES NO EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE. In no event shall S&P, its affiliates and its third party licensors be liable for any direct, indirect, special or consequential damages in connection with subscriber's or others use of the data/information contained herein. Access to the data or information contained herein is subject to termination in the event any agreement with a third-party of information or software is terminated.

Analytic services provided by Standard & Poor's Ratings Services (Ratings Services) are the result of separate activities designed to preserve the independence and objectivity of ratings opinions. The credit ratings and observations contained herein are solely statements of opinion and not statements of fact or recommendations to purchase, hold, or sell any securities or make any other investment decisions. Accordingly, any user of the information contained herein should not rely on any credit rating or other opinion contained herein in making any investment decision. Ratings are based on information received by Ratings Services. Other divisions of Standard & Poor's may have information that is not available to Ratings Services. Standard & Poor's has established policies and procedures to maintain the confidentiality of non-public information received during the ratings process.

Ratings Services receives compensation for its ratings. Such compensation is normally paid either by the issuers of such securities or third parties participating in marketing the securities. While Standard & Poor's reserves the right to disseminate the rating, it receives no payment for doing so, except for subscriptions to its publications. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

Any Passwords/user IDs issued by S&P to users are single user-dedicated and may ONLY be used by the individual to whom they have been assigned. No sharing of passwords/user IDs and no simultaneous access via the same password/user ID is permitted. To reprint, translate, or use the data or information other than as provided herein, contact Client Services, 55 Water Street, New York, NY 10041; (1)212.438.9823 or by e-mail to: research_request@standardandpoors.com.