Spain: BFA-Bankia Group Restructuring, 2012

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Spain: BFA-Bankia Group Restructuring, 2012

Lakshimi Swaminathan

Yale Program on Financial Stability Case Study
March 28, 2024

Abstract

In 2010 and 2011, seven troubled savings banks (cajas) merged to form Banco Financiero y de Ahorros, S.A (BFA), which the government capitalized with EUR 4.5 billion (USD 5.9 billion) in convertible securities, and BFA’s commercial banking subsidiary, Bankia (BFA, together with Bankia, was referred to as the BFA-Bankia Group). As a double-dip recession extended BFA-Bankia Group’s expected credit losses in Spain’s real estate market in 2012, third-party stress tests determined that the Group was deeply insolvent. On November 27, 2012, Fondo de Reestructuración Ordenada Bancaria (FROB), Spain’s newly established national resolution authority, and the Bank of Spain (BoS) approved the further restructuring and government takeover of the BFA-Bankia Group. The restructuring required an additional capital injection of EUR 17.9 billion into BFA, funded by the recently created European Stability Mechanism (ESM) through the issuance of ESM securities to BFA. The restructuring also involved the write-down of the shareholders of Bankia, the partial conversion of BFA’s subordinated debt to Bankia equity, and the transfer of BFA and Bankia’s real estate assets to an asset management vehicle, Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria (SAREB), for EUR 22.4 billion. The restructuring of the BFA-Bankia Group stands out owing to the sheer size of the shortfall of regulatory capital that the bank and its parent faced (EUR 24.7 billion), as well as the gross cost to the government of about EUR 45 billion, including the purchase of assets by SAREB. External pressure from the International Monetary Fund (IMF) and the European authorities, and financial support from the latter were instrumental in the measures the government took. The government retains a 16.1% stake in CaixaBank, which acquired Bankia in 2021. Taking into account the value of that stake and other recoveries, the Bank for International Settlements (BIS) estimated the net cost to the government of the BFA-Bankia Group rescue at EUR 17.2 billion, excluding losses experienced by SAREB on the assets it acquired from the bank.

Keywords: BFA-Bankia, restructuring, SAREB, Spain

1 This case study is part of a Yale Program on Financial Stability (YPFS) selection of New Bagehot Project modules considering bank resolutions and restructurings. A survey of all the cases in this series (McNamara et al. 2024) and the individual cases underlying it are available from the Journal of Financial Crises at https://elischolar.library.yale.edu/journal-of-financial-crisis/vol6/iss1/.

2 Research Associate, YPFS, Yale School of Management. The author would like to thank Carey Mott for his assistance, and Miguel Carcano and Enrique Ezquerra of the Single Resolution Fund for their valuable suggestions on this case.
Overview

This module describes the restructuring of Banco Financiero y de Ahorros, S.A. (BFA, which together with its banking subsidiary Bankia was referred to as the BFA-Bankia Group) in 2012 using the capital injection, bail-in, and asset separation tools. Before the restructuring, Spanish authorities had subscribed to EUR 4.5 billion (USD 5.5 billion)3 in the form of convertible preference shares in December 2010 as part of a broad-based capital injection (known as the FROB I injections), which it converted into equity in June 2012, and EUR 4.5 billion in ordinary shares on September 7, 2012 (Sankar 2021).

As their expected losses grew in the years after the Global Financial Crisis (GFC), seven troubled Spanish savings banks (cajas)4 agreed on June 14, 2010, to merge into a new entity known as BFA and formed its commercial banking subsidiary Bankia (collectively, the BFA-Bankia Group). The two largest cajas in the group, Caja Madrid and Bancaja, accounted for 90% of its assets. The new entity, initially combined through a Spanish process known as an institutional protection scheme (IPS),5 had nearly EUR 340 billion in assets (EUR 223 billion in risk-weighted assets), or 10% of Spain’s financial system assets (Santos 2017).

Key Terms

<table>
<thead>
<tr>
<th>Purpose: “In view of the systemic nature of BFA/Bankia within the Spanish and European financial sector ... for exceptional reasons the BFA Group is to be restructured” (EC 2012e, 14).</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size and Nature of Institution</td>
</tr>
<tr>
<td>Source of Failure</td>
</tr>
<tr>
<td>Start Date</td>
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<tr>
<td>End Date</td>
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<tr>
<td>Approach to Resolution and Restructuring</td>
</tr>
<tr>
<td>Outcomes</td>
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</tbody>
</table>

(continued)

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3 Per FXtop.com, EUR 1 = USD 1.21 on June 1, 2010.

4 Cajas were organised as private charities with banking licenses and could provide the services of commercial and cooperative banks. They were not owned by shareholders but were governed by members. Profits were used for strengthening capital, and the rest of it was used for charity work (EC 2012e).

5 The IPS is a support mechanism among a group of banks that was defined to be “a contractual or statutory liability arrangement which protects those institutions and in particular ensures their liquidity and solvency to avoid bankruptcy where necessary” (Huizinga 2022, 8).
On February 18, 2011, Spain announced that it would require all banks to meet enhanced capital principal requirements of 8% or 10%, depending on certain balance sheet characteristics, by September 30, 2011. BFA’s supervisor, the Bank of Spain (BoS), found a EUR 5.8 billion capital shortfall at BFA (EC 2012e). BFA management decided in July 2011, to raise capital through a public offering, which would allow it both to lower its regulatory capital principal ratio to 8% and to meet that target. In May 2011, 99% of the assets and liabilities of the seven founding cajas were transferred to BFA and 85% of these assets and liabilities were simultaneously transferred to Bankia. EUR 283 billion in assets, remained under BFA’s control outside Bankia (Bankia 2011). Although these transactions took place in May 2011, they were effective as of January 1, 2011 (EC 2012a). BFA floated Bankia on the Madrid Stock Exchange on July 20, 2011, seeking to raise up to EUR 4 billion in equity, but private investors purchased only EUR 3.1 billion (or 47.6% of Bankia’s shares), leaving BFA with the remaining equity (see Figure 3). Few foreign investors participated, creating negative perceptions of the bank’s viability (Bankia n.d.; Santos 2017).

The demise of BFA and Bankia owed to a capital shortfall that the BFA-Bankia Group never sufficiently filled (EC 2012e). In May 2012, BFA-Bankia replaced the old management through four newly appointed top management officials (CaixaBank n.d.; EC 2012e). Three investment banks carried out a valuation of BFA and estimated its equity was worth negative EUR 13.6 billion. Based on that valuation, Spain’s newly established resolution authority, Fondo de Reestructuración Ordenada Bancaria (FROB) took over BFA on June 25, 2012, becoming the sole shareholder of BFA by converting its preference shares into ordinary equity in BFA and writing down to zero the shares that the cajas held in BFA (Baudino, Herrera, and Restoy 2023; EC 2012e; Santos 2017).

On August 31, 2012, BFA posted a revised EUR 7.3 billion loss for the first half of 2012 because of higher provisions made for real estate and construction portfolios as mandated by Royal Decree-Law 2/2012 (which was implemented on the same day). This led to a further shortfall of regulatory capital (de Cominges 2016; EC 2012e). As this shortfall would have jeopardized BFA-Bankia’s access to liquidity provided via the Eurosystem’s monetary policy operations, on September 4, 2012, FROB injected EUR 4.5 billion in capital into BFA (which BFA then loaned to Bankia) as part of a broad-based capital injection program in the

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**Notable Features**

<table>
<thead>
<tr>
<th>Feature</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Both Bankia and BFA, Bankia’s parent, needed to be recapitalized; the government took 100% equity in BFA, the parent, but private shareholders continued to hold 31% of Bankia, the subsidiary; ESM lent the Spanish government EUR 17.9 billion, which FROB used to fund the injection; the ESM then issued securities that FROB injected into BFA in return for BFA ordinary shares; BFA subordinated debt holders and Bankia equity holders shared in losses, making this an early example of bail-in; however, some equity and debt holders were able to recoup losses through legal challenges; Bankia’s bail-out was the largest bank nationalization in Spain’s history</td>
<td></td>
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</tbody>
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Spanish government, BFA, and Bankia's capital requirements, capital injection, and resolution authority actions.
form of ordinary shares (EC 2012a). (For more information on FROB and its broad-based capital injections, see Sankar [2021]).

On September 28, 2012, the BoS announced the result of a new stress test, which showed a capital need for BFA at the parent level of EUR 13.2 billion in the base scenario and EUR 24.7 billion in the adverse scenario. On November 27 and 28, 2012, the BFA-Bankia Group received approval from the Spanish and European authorities for its 2012–17 restructuring plan. Under the plan, BFA expected to address a capital need of EUR 24.6 billion, a slight adjustment from the shortfall of EUR 24.7 billion identified in the September stress test. Of that amount, it expected to raise approximately EUR 6.5 billion in new capital by converting preferred shares and subordinated debt into equity; and approximately EUR 17.9 billion in public support for BFA at the parent level, including the EUR 4.5 billion that FROB had provided to BFA in September (BFA 2013).

In December 2012, following the restructuring plan, the European Stability Mechanism (ESM) issued EUR 17.9 billion in bonds to FROB: EUR 13.5 billion to enable FROB to acquire new ordinary shares in BFA, and EUR 4.5 billion to replace the Spanish government bonds that FROB had injected into BFA in September (EC 2012e). FROB also agreed to write down to zero the value of the shares it had acquired through the debt-equity conversion in June 2012 (BFA 2013).

The stress test identified Bankia’s capital need at EUR 15.5 billion. To meet that need, BFA transferred EUR 10.7 billion of the ESM bonds to Bankia in return for contingent convertible bonds in Bankia, which counted as Tier 1 capital for Bankia to make it capital compliant. In the first quarter of 2013, Bankia converted those bonds into ordinary shares. Bankia also received EUR 4.8 billion in capital from the bail-in of BFA’s subordinated debt holders (EC 2012e).

On December 31, 2012, all real estate assets in BFA and Bankia were transferred to the asset management vehicle Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria (SAREB) for EUR 22.4 billion using state-guaranteed debt securities issued by SAREB; they carried maturities of one to three years (EC 2012e; Tam and Fulmer 2021). Of the EUR 22.4 billion, Bankia received EUR 19.5 billion in SAREB securities for its assets and BFA received EUR 2.9 billion in SAREB securities for assets owned by it and non-Bankia BFA subsidiaries (BFA 2013).

In May 2013, BFA’s subordinated debt holders were partly written off and partly converted to equity in Bankia and new Bankia capital was raised through common shares (Donnelly and Pometto 2024; Hay and Unmack 2012). A company called Solvia Servicios Inmobiliarios, S.L.U. serviced the real estate portfolio on behalf of SAREB, and Haya Real Estate serviced the loan portfolio of BFA-Bankia. SAREB continues to own some former real estate assets of BFA-Bankia, of which it is in the process of divesting itself (SAREB 2019). In April 2014, Spanish authorities recovered EUR 1.3 billion when BFA sold 7.5% of Bankia, and in 2017, they recovered EUR 0.8 billion when BFA sold 7% of Bankia (CaixaBank n.d.).
December 31, 2017, marked the end of Bankia’s five-year restructuring plan, with the main goals accomplished. On that same date, Bankia merged with Banco Mare Nostrum (BMN); FROB held a 61.8% stake in the new institution (Reuters 2021; Zahid 2017). In 2021, FROB’s stake came down to 17.3% following BMN-Bankia’s merger with CaixaBank; it was diluted to 16.1% at the end of 2022 (CaixaBank 2023; Reuters 2021). Figure 1 provides a summary of the events that transpired in the restructuring of BFA-Bankia. The Bank for International Settlements (BIS) estimated the net cost to the government of the BFA-Bankia rescue at EUR 17.2 billion, taking into account the value of the government’s 16.1% stake in CaixaBank and other recoveries, but excluding losses experienced by SAREB on the assets it acquired from the bank (Baudino, Herrera, and Restoy 2023).

**Figure 1: Timeline of the Restructuring of BFA-Bankia**

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec. 28, 2010</td>
<td>FROB subscribes to EUR 4.5 billion of convertible preference shares in BFA as part of FROB I capital injections (a broad-based capital injection program)</td>
</tr>
<tr>
<td>May 23, 2011</td>
<td>Formation of BFA completed through the merger of seven <em>cajas</em> (savings institutions); the effective date is January 1, 2011</td>
</tr>
<tr>
<td>June 29, 2011</td>
<td>Bankia registers prospectus for an IPO to raise capital privately. Owing to this initiative, it does not receive any capital injections as part of FROB II injections</td>
</tr>
<tr>
<td>July 20, 2011</td>
<td>Bankia floats an IPO to raise up to EUR 4 billion in capital from private sources, following the need to meet enhanced capital requirements established by the BoS; it ends up raising only EUR 3.1 billion through private subscription to shares. BFA now owns 45.54% of Bankia</td>
</tr>
<tr>
<td>May 7, 2012</td>
<td>Rodrigo Rato, chairman of Bankia, resigns owing to disagreement over audited financial statements of 2011</td>
</tr>
<tr>
<td>May 9, 2012</td>
<td>José Ignacio Goirigolzarri (ex-chairman of Banco Bilbao Vizcaya Argentaria) takes charge as chairman of Bankia</td>
</tr>
<tr>
<td>May 25, 2012</td>
<td>The new management announces it will request from FROB an additional EUR 19 billion of capital, of which EUR 12 billion to EUR 14 billion would be needed for Bankia alone. It also restates 2011 earnings to show a loss of EUR 4.9 billion</td>
</tr>
<tr>
<td>June 27, 2012</td>
<td>FROB converts convertible preference shares injected in December 2010 into ordinary shares after a valuation assessment reveals BFA-Bankia’s value to be negative EUR 13.6 billion. The seven <em>cajas</em> cease to own BFA-Bankia. Through its shares in BFA, FROB assumes a 45.54% stake in Bankia</td>
</tr>
<tr>
<td>July 20, 2012</td>
<td>The Kingdom of Spain formulates a Memorandum of Understanding (MoU) on Financial-Sector Policy Conditionality that details Spain’s plans to recapitalize and stabilize its financial sector. The EC plays an important supervisory role in overseeing Spain’s efforts in this regard</td>
</tr>
<tr>
<td>Sept. 4, 2012</td>
<td>FROB injects EUR 4.5 billion in BFA in the form of ordinary shares as part of FROB III capital injections to ensure that BFA-Bankia would be able to maintain its status for Eurosystem monetary policy operations and becomes BFA’s sole shareholder</td>
</tr>
<tr>
<td>Nov. 27, 2012</td>
<td>FROB and BoS announce the decision to restructure BFA-Bankia</td>
</tr>
</tbody>
</table>
Nov. 28, 2012 | European Commission approves the five-year restructuring plan and FROB injects EUR 17.9 billion (in the form of bonds contributed by the ESM) in response to a stress test conducted by Oliver Wyman, as required by the MoU on Financial Sector Policy Conditionality
---
Dec. 31, 2012 | SAREB purchases real estate and development assets for EUR 22.4 billion from Bankia (EUR 19.5 billion) and BFA (EUR 2.9 billion)
---
Dec. 31, 2017 | Bankia’s five-year restructuring plan ends, coincident with Bankia’s merger with BMN
---
2021 | Bankia-BMN merges with CaixaBank and FROB owns 17.3% stake in the merged entity, later reduced to 16.1%; full divestment was expected to happen before the end of 2025 but has been extended at the time of writing the case

Source: Author’s analysis.

**Summary Evaluation**

When authorities unveiled BFA-Bankia’s losses in 2012, the Spanish financial system began to doubt the loss estimates at Spanish banks broadly (Santos 2017). As a result, the financial press referred to BFA-Bankia as “the bank that broke Spain” (Mallet and Johnson 2012).

Bankia’s IPO failed to convince foreigners that it was viable, as the previous efforts had failed to close the crisis. Moreover, since the additional provisioning requirements proved inadequate, the request for eurozone assistance became inevitable. (Santos 2017).

Tano Santos, an academic from Columbia University, has stated that one of the positive outcomes of the Bankia episode and the banking crisis in Spain is that cajas do not exist anymore. This is seen to be a positive outcome, as powerful local politicians had exercised control over a substantial portion of the credit market through these cajas (Santos 2017). An article from the *New York Times* in January 2014 heralded Bankia to be a symbol of Spain’s revival owing to its debt reduction and capital raising strategies (Minder 2014). A scholar in Madrid, de Cominges, concluded that it would be impossible for FROB to recover its investment in Bankia by selling its stake without touching taxpayer money (de Cominges 2016).

A study from the BIS stated that rapid disposal of the stake of the resolution authority in banks under restructuring and resolution was preferred and that the only exception to this was Bankia, since all the other ailing banks at the time were sold off more quickly than Bankia was (Baudino, Herrera, and Restoy 2023).

A report from the Spanish think tank El Real Instituto Elcano summarized the reasons for Bankia’s downfall: (1) political involvement in the governance of the cajas that enabled risky business strategies and slow government action; (2) the perception that the crisis was solely a liquidity issue, rather than a solvency issue as well; (3) the government’s slow response, only after external pressure from the International Monetary Fund (IMF) and European Union (EU); and (4) the scale of the problem being larger than what the authorities were prepared to handle (Otero-Iglesias, Royo, and Steinberg 2016).
### Context: Spain, BFA-Bankia, 2012–2013

<table>
<thead>
<tr>
<th>Category</th>
<th>Details</th>
</tr>
</thead>
</table>
| Assets                       | EUR 28.2 billion as of Dec. 31, 2012  
                                  EUR 25.1 billion as of Dec. 31, 2013    |
| Liabilities                  | EUR 28.2 billion as of Dec. 31, 2012  
                                  EUR 25.1 billion as of Dec. 31, 2013    |
| Deposits                     | No information                              |
| Capital Ratio (Tier 1)       | No information                              |
| Nonperforming Loans          | EUR 19.8 billion as of Dec. 31, 2012  
                                  EUR 20 billion as of Dec. 31, 2013      |
| Market Share                 | 5.97% of lending market as of Dec. 31, 2013  |
| Banking System, % of GDP     | No information                              |

*Source: FDIC 2014.*
Key Design Decisions

1. **Purpose:** FROB decided to proceed with the restructuring of BFA-Bankia on November 27, 2012, as the bank was systemically important in the Spanish and European financial sectors.

As a result of BFA-Bankia Group’s failure to meet solvency requirements owing to a deterioration of asset quality, minimal capital generation, and a high nonperforming loan ratio, among other indicators, on November 28, 2012, the European Commission (EC) approved state support (which had been announced in May 2012) under State Aid rules for BFA and Bankia (EC 2012e; EC 2012a; FROB 2023).

Earlier that fall, on September 28, 2012, the BoS had announced the results of a new stress test conducted by consulting firm Oliver Wyman, indicating a capital need of EUR 13.2 billion for BFA at the parent level in the base scenario and EUR 24.7 billion in the adverse scenario. On November 27 and 28, 2012, BFA-Bankia Group received approval from the Spanish and European authorities for its 2012–17 Restructuring Plan. Under that plan, BFA intended to address a capital shortfall of EUR 24.6 billion, a slight adjustment from the shortfall of EUR 24.7 billion identified in the September stress test. BFA expected to raise EUR 6.5 billion in new capital by converting preferred shares and subordinated debt into equity; and EUR 17.9 billion in public support for BFA at the parent level, including the EUR 4.5 billion that FROB had provided to BFA in September through the FROB I injections, which was a round of broad-based capital injection program that the Spanish authorities administered to rescue banks that were affected by the GFC (BFA 2013).

The stress test identified Bankia’s capital need at EUR 15.5 billion. To meet that need, BFA transferred EUR 10.7 billion of the ESM bonds to Bankia in return for contingent convertible bonds in Bankia, which counted as Tier 1 capital for Bankia to make it capital compliant; in the first quarter of 2013, Bankia converted those bonds into ordinary shares (EC 2012e).

The restructuring plan stated that the BFA-Bankia Group met the conditions of Royal Decree-Law 24/2012 to be placed under resolution: it had a capital shortfall of EUR 24.7 billion, according to the September 2012 stress test, the bank had a substantial amount of unpaid State Aid received since 2010, and it was unlikely to be able to repay that State Aid. However, FROB (Spain’s newly established national resolution authority) and the BoS opted for the restructuring of BFA-Bankia instead of resolving it, as it was systemically important in the Spanish and European financial sector (EC 2012e).

In December 2012, following the restructuring plan, the ESM issued EUR 17.9 billion in bonds to FROB: EUR 13.5 billion to enable FROB to acquire new ordinary shares in BFA, and EUR 4.5 billion to replace the Spanish government bonds that FROB had injected into BFA in September (EC 2012e). FROB also agreed to write down to zero the value of the shares it had acquired through the debt-equity conversion in June 2012 (BFA 2013).
On December 31, 2012, all real estate assets in BFA and Bankia were transferred to the asset management vehicle SAREB for EUR 22.4 billion using state-guaranteed debt securities issued by SAREB; they carried maturities of one to three years (EC 2012e; Tam and Fulmer 2021). Of the EUR 22.4 billion, Bankia received EUR 19.5 billion in SAREB securities for its assets and BFA received EUR 2.9 billion in SAREB securities for assets owned by it and non-Bankia BFA subsidiaries (BFA 2013).

In May 2013, BFA subordinated debt holders were partly written off and partly converted to equity and new Bankia capital was raised through common shares (Donnelly and Pometto 2024; Hay and Unmack 2012). A company called Solvia Servicios Inmobiliarios, S.L.U. serviced the real estate portfolio on behalf of SAREB. The restructuring plan also outlined a splitting of BFA-Bankia into a core unit named the Steady Bank Unit and a legacy unit named the Legacy Unit; while the Steady Bank Unit would include the existing retail, small and medium enterprise (SME), and public sector banking business of BFA-Bankia Group in its core areas, the Legacy Unit would include all those assets and liabilities that were to be sold, discontinued, or held to maturity, most of which were from the noncore areas of BFA-Bankia's business (EC 2012a).

2. Part of a Package: The restructuring of Bankia was preceded by recapitalization measures performed by FROB in June 2010.

From 2009 until 2013, FROB injected capital into eligible Spanish banks in three phases, FROB I, II, and III. Before the restructuring of Bankia, FROB injected capital worth EUR 4.5 billion in the form of preference shares in BFA in December 2010, as part of FROB I, to stabilize the cajas, which were in the process of being merged (EC 2012e). This was part of a broader effort of FROB to support the mergers of 25 cajas into seven larger solvent banks through the subscription of convertible preferred shares (Sankar 2021). On September 7, 2012, FROB injected EUR 4.5 billion in capital in the form of ordinary shares to ensure that BFA-Bankia would be able to maintain its status for Eurosystem monetary policy operations (EC 2012a). This was part of the FROB III capital injections that took place between 2012–13 for banks that had failed a stress test through the purchase of convertible contingent bonds and subscription to shares. BFA-Bankia did not require any recapitalizations under FROB II between 2011–12, as it raised capital through Bankia's IPO. For the recapitalizations, the MoU on Financial Sector Policy Conditionality had classified the entities into three groups. BFA-Bankia was part of Group 1 along with CatalunyaCaixa, NCG Banco, and Banco de Valencia. Group 1 banks were banks that were already owned by FROB (Sankar 2021). Of these banks, BFA-Bankia received the maximum aid of EUR 17.9 billion (EC 2012a; EC 2012b; EC 2012c; EC 2012d).

For more details on the broad-based capital injections, see Sankar (2021).

3. Legal Authority: The restructuring of Bankia was governed by Spain’s Royal Decree Law 24/2012 on the restructuring and resolution of credit institutions.

The restructuring of Bankia was guided by the Royal Decree-Law (RDL) 24/2012 (Bank of Spain 2012). The RDL on restructuring and resolution of credit institutions was approved by
the Spanish government on August 31, 2012, as Law 9/2012, and became effective immediately. This law aimed to transpose certain measures outlined in the European Directive on Crisis Resolution and the MoU on Financial Sector Policy Conditionality between the Spanish authorities and the ESM (Bank of Spain 2012; World Bank 2016).

The MoU entailed the following:

(1) Identification of individual banks’ capital needs through a comprehensive asset quality review of the banking sector and a bank-by-bank stress test, based on that asset quality review; (2) Recapitalization, restructuring and/or resolution of weak banks …, and, (3) Segregation of assets in those banks receiving public support in their recapitalization effort and the transfer of the impaired assets to an external Asset Management Company (Kingdom of Spain 2012, 3).

The RDL designated FROB and the BoS to be Spain’s official national resolution and restructuring authorities. It laid down the legal authority, governance, powers, functions, structure and system of responsibility and accountability of FROB (Bank of Spain 2012).

Under the decree, restructuring was meant for entities that authorities believed could repay any official support and become viable once more, potentially through the transfer of toxic assets to an asset management company. Resolution, on the other hand, was an alternative to liquidation proceedings for entities that authorities perceived to be unviable (Bank of Spain 2012). Chapter VII of the decree authorized the imposition of losses on shareholders and creditors (Global Regulation n.d.).

The decree recognized the creation of an asset management company, SAREB, to separate impaired assets from the entity in order to facilitate its restructuring and outlined its legal authority (Bank of Spain 2012). Moreover, RDL 9/2012 of November 14, 2012, defined and regulated asset management companies as entities that had to manage impaired assets of entities under restructuring with the goal of long-term value realization (de Cominges 2016).

4. Administration: FROB administered the restructuring of BFA and its Bankia subsidiary.

FROB and the BoS were the designated national resolution authorities, as laid down in RDL 24/2012 (Bank of Spain 2012; de Cominges 2016). The legislative framework and the blueprint dictating the conditions of asset transfer to SAREB and the design of SAREB was prepared by FROB in consultation with the European Commission (EC), the European Central Bank (ECB), the ESM, the IMF, BoS and the Ministry of Economic Affairs and Competitiveness (EC 2012a). The decision to restructure BFA-Bankia was undertaken by FROB on the basis of the results of the stress test conducted by an independent consultant, Oliver Wyman, in the context of the MoU on Financial Sector Policy Conditionality between the Spanish authorities and the ESM (EC 2012e).
5. **Governance:** FROB was managed by a governing committee.

RDL 9/2009 established that FROB would be managed by a governing committee of nine members appointed by the Ministry of Economy and Finance. Of these, four had to be recommended by the BoS (one of whom had to be the deputy central bank governor), two had to represent the Ministry of Economy and Finance, and three had to represent the Deposit Guarantee Fund (de Cominges 2016). FROB was a public law entity with its own legal mandate (FROB 2020).

The BFA-Bankia Group was monitored closely by the Spanish authorities (FROB and BoS) in conjunction with the EC, ECB, European Banking Authority (EBA), and the IMF (EC 2012a). To ensure compliance with the commitments in the restructuring plan, a monitoring trustee to assist the EC was appointed by BFA-Bankia under the guidance of FROB (EC 2012e). There also existed a Strategic Coordination Committee comprising of the Spanish authorities and the EC, ECB, EBA, ESM and the IMF which oversaw the capital needs and issues affecting Bankia (IMF 2012).

6. **Communication and Disclosure:** FROB stated that the restructuring plan would assure the long-term viability of the bank and that it would aim to minimize taxpayer cost while limiting distortions of competition.

The restructuring of BFA and Bankia was heavily covered by the Spanish press, owing to its systemic importance; in fact, the financial press dubbed BFA-Bankia “the bank that broke Spain” (Mallet and Johnson 2012). The information pertaining to the restructuring of BFA-Bankia was publicly communicated at the time by the Spanish authorities through the press release on FROB’s website as well as the EC State Aid document (EC 2012a; FROB 2023).

A FROB communiqué dated August 31, 2012, stated that the restructuring plan would assure the long-term viability of the bank and that it would aim to minimize taxpayer cost while limiting distortions of competition (FROB 2012). Some of the details of the restructuring were also published on Bankia’s website (CaixaBank n.d.).

The information pertaining to changes in subordinated obligations was published on FROB’s website, as well as in the Official State Gazette. The official statement from FROB mentioned that investors affected by the restructuring of BFA-Bankia would need to be made aware of their position via disclosure by FROB, both in the aforementioned sources and on the website of the National Markets Securities Commission (FROB 2023).

FROB disclosed information pertaining to the restructuring of BFA-Bankia in its annual reports, as well as in the annual reports of SAREB (FROB 2014; SAREB 2014).

7. **Source and Size of Funding:** The European Stability Mechanism lent the Spanish government EUR 41.3 billion to restructure BFA-Bankia. FROB was funded by the state budget and the loan from the ESM.

FROB, which financed the restructuring of BFA-Bankia, was funded by the state budget (EC 2012e). The total cost of restructuring BFA-Bankia amounted to EUR 45 billion (including
the EUR 22.4 billion SAREB bonds subscribed to by BFA-Bankia) and of this, FROB was able to recover EUR 4.9 billion through the sale of Bankia shares for EUR 2.1 billion and receipt of dividends worth EUR 2.8 billion by 2019 (Bank of Spain 2019; SAREB 2021). The cost of nationalizing BFA, Bankia’s parent company, amounted to about EUR 22.4 billion (Gutiérrez 2020). FROB I (EUR 4.5 billion) and FROB III (EUR 17.9 billion) capital injections collectively amounted to EUR 22.5 billion (EC 2012a). Of this total, the Spanish government, through FROB, utilized EUR 17.9 billion to fund the December 2012 capital injection; the ESM then issued securities that FROB injected into BFA in return for BFA ordinary shares. FROB utilized EUR 17.9 billion for the recapitalization of BFA-Bankia, out of the EUR 39.4 billion loan provided by the ESM to recapitalize the other banks in Group 1 as classified by the MoU, CatalunyaCaixa, NCG Banco, and Banco de Valencia (ESM n.d.a). These loans carried a maximum maturity of 15 years (ESM 2012). Of the total loan of EUR 41.3 billion taken from the ESM, the Spanish government repaid EUR 17.6 billion between 2014 and 2018 (ESM n.d.a; ESM n.d.b). SAREB purchased the assets with state-backed bonds with a one- to three-year maturity, paying a yield equal to the lower of the Spanish government bond yield for the same maturity (EC 2012e; SAREB 2019). Figure 2 displays the summary of capital injections administered by the government into BFA-Bankia in 2012.

Figure 2: Summary of Government Capital Injections into BFA-Bankia, as of Year-End 2012

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<thead>
<tr>
<th>ESM</th>
<th>Assets</th>
<th>Liabilities</th>
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<tbody>
<tr>
<td></td>
<td>~EUR 18 bn equity in BFA</td>
<td>~EUR 18 bn ESM equity held by FROB</td>
</tr>
<tr>
<td></td>
<td>~EUR 18 bn owed to ESM</td>
<td>(Early EUR 4.5 bn stake in BFA written off)</td>
</tr>
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<thead>
<tr>
<th>FROB</th>
<th>Assets</th>
<th>Liabilities</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>~EUR 18 bn loan to Spanish government</td>
<td>~EUR 18 bn ESM debt securities</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>BFA</th>
<th>Assets</th>
<th>Liabilities</th>
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<tbody>
<tr>
<td></td>
<td>~EUR 7 bn ESM debt securities</td>
<td>~EUR 18 bn equity held by FROB</td>
</tr>
<tr>
<td>Earlier EUR 4.5 bn equity in Bankia</td>
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<table>
<thead>
<tr>
<th>Bankia</th>
<th>Assets</th>
<th>Liabilities</th>
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<tbody>
<tr>
<td></td>
<td>~EUR 11 bn ESM debt</td>
<td>Earlier EUR 4.5 bn equity held by BFA</td>
</tr>
</tbody>
</table>

Source: Author’s analysis.
8. **Approach to Resolution and Restructuring:** After injecting EUR 17.9 billion of capital into BFA-Bankia, Spanish authorities wrote down the value of BFA’s shareholders and subordinated creditors and transferred nonperforming assets to SAREB, a state-backed asset management company.

The restructuring of BFA-Bankia, which commenced in November 2012, entailed the following: capital injection of EUR 17.9 billion to BFA, of which BFA downstreamed EUR 10.7 billion to Bankia; wiping out all of Bankia’s shareholders; imposing losses on subordinated debt holders; and transferring the impaired assets to an asset management vehicle, SAREB (EC 2012a). Figure 3 shows the structure of BFA-Bankia.

**FROB III Capital Injection into BFA and Bankia**

The MoU on Financial Sector Policy Conditionality between the Spanish authorities and the ESM required banks to undergo a stress test to determine their capital needs. Following the completion of the stress test, FROB injected EUR 17.9 billion into BFA-Bankia in November 2012 (Sankar 2021). FROB contributed bonds issued by the ESM6 in this measure (EC 2012a). BFA-Bankia Group transferred EUR 10.7 billion of this capital to Bankia in the form of contingency convertible bonds (CoCos) qualifying as capital principal so that Bankia could meet its solvency requirements. Bankia converted these CoCos into ordinary shares in the first quarter of 2013 (EC 2012a).

**Analytical Separation of BFA and Bankia’s “Legacy Unit”**

For analytical purposes, Spanish authorities required Bankia to split its assets between a Steady Bank Unit focused on retail banking and SME lending and a Legacy Unit focused on businesses, assets, and liabilities that were going to be sold, discontinued, or held to maturity. The Legacy Unit consisted of the noncore subsidiaries and equity stakes that were to be divested. The authorities then transferred Bankia’s nonperforming assets to a state-backed asset management company, SAREB (EC 2012a). BFA-Bankia Group continued to manage both units under one legal entity (EC 2012e).

Between 2012 and 2017, authorities planned to shrink the Legacy Unit’s balance sheet by 30–40% and close all remaining bank branches not associated with the Steady Bank Unit’s business lines (EC 2012e).

**Conversion of Debt into Equity**

In June 2012, just three months after FROB became the sole shareholder of BFA and wiped out the existing shareholders, FROB had to inject EUR 4.5 billion into the holding company. However, Bankia, the banking subsidiary, was only 52.4% owned by BFA (which in turn was then owned by FROB), and the remainder was held by private investors. The restructuring

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6In June 2012, the Spanish government sought assistance in the form of a loan from the ESM to cover the capital shortfall noted in several Spanish banks at the time. On December 11, 2012, the ESM transferred funds collectively worth EUR 39.7 billion for the recapitalization of BFA-Bankia, CatalunyaCaixa, NCG Banco and Banco de Valencia. FROB utilized close to EUR 37 billion from this source of funding (ESM n.d.a).
plan dictated that any further capital injection in Bankia would be borne by these private shareholders, and not FROB (EC 2012e).

FROB converted EUR 3.2 billion in BFA’s preference shares (haircut 20–30%), EUR 0.4 billion in BFA’s perpetual instruments (haircut 10–20%), and EUR 3.3 billion in BFA’s subordinated debt (also haircut 10–20%) into Bankia’s ordinary shares in view of the losses incurred by the BFA-Bankia Group. Some dated subordinated debtholders were offered the opportunity to convert into equity or senior debt (EC 2012e).

Thus, in May 2013, subordinated debt holders were partly written off and partly converted to common equity (Donnelly and Pometto 2024; Hay and Unmack 2012).

**Asset Transfer**

BFA-Bankia transferred EUR 22.4 billion in real estate assets, close to half of their EUR 46.4 billion book value, to an asset management company, SAREB, created in 2012 (for more information on SAREB, see (EC 2012a; Tam and Fulmer 2021). Some of these assets were highly impaired, with a market value of EUR 15.9 billion. SAREB absorbed all real estate assets (both performing and impaired) from all banks with State Aid (EC 2012e). SAREB purchased the assets with state-backed bonds with a one- to three-year maturity, paying a yield equal to the lower of the Spanish government bond yield for the same (EC 2012e; SAREB 2019). Of the EUR 22.4 billion, Bankia received EUR 19.5 billion in SAREB securities for its assets and BFA received EUR 2.9 billion in SAREB securities for assets owned by it and non-Bankia BFA subsidiaries. Figure 3 shows the ownership structure of Bankia in December 2012.
9. **Treatment of Creditors and Equity Holders:** Equity shareholders of Bankia were wiped out, and BFA wrote off FROB’s 2011 equity injection. The conversion of BFA’s convertible shares into ordinary shares made FROB the sole shareholder of BFA in 2012. In 2013, the hybrid instruments were converted to ordinary shares.

After independent valuers established a negative economic value for BFA-Bankia Group on June 25, 2012, FROB decided to convert all of its convertible preference shares in BFA into ordinary equity. This action materialized since the restated accounts of the BFA-Bankia Group posted losses amounting to EUR 5 billion and the negative valuation of EUR 13.6 billion accorded to the BFA-Bankia Group made it impossible for the company to buy back the convertible preference shares issued by FROB. The conversion of convertible preference shares into ordinary shares made FROB the sole shareholder of the ordinary shares of BFA. On September 3, 2012, FROB injected EUR 4.5 billion into BFA so that it could meet regulatory capital requirements; as these proceeds were lent to Bankia, BFA’s stake in Bankia remained unchanged (EC 2012a).

Ultimately, 45.54% of Bankia’s equity was held by FROB through BFA while the remaining 54.46% was held by shareholders who participated in the July 2011 IPO and by other holders of hybrid instruments, which were converted into ordinary shares in 2013. The MoU required

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7 Although the EC and other sources cite the division of equity as 45.54% to FROB and 54.46% to the private shareholders, the 2011 Bankia annual report gives the percentages as 68.4% to FROB and 31.6% to private shareholders (Bankia 2013; EC 2012a).
that all losses be borne by the shareholders in proportion to their stake prior to any new capital injection by FROB. Consequently, holders of preference shares (EUR 3.2 billion) and perpetual dated subordinated debt instruments (EUR 3.4 billion) were subjected to deep discounts on the nominal values of their instruments which were bought back by the BFA-Bankia Group; the proceeds of these buybacks were automatically converted to ordinary shares in Bankia with the sole exception of dated subordinated debt, whose holders were given the opportunity to convert these instruments into more senior debt instruments and ordinary shares or equivalents to ordinary shares (EC 2012a).

Consequently, existing private shareholders were subjected to a 99.5% haircut (Philippon and Salord 2017).

There was little bail-in-able senior debt left in Bankia since the Spanish law mandated that senior debt was at the same level of priority as deposits and in any case, there was no appetite at the European level for losses to be imposed on senior debt (Santos 2017).

Spanish media reported that close to 350,000 shareholders were affected by FROB’s move to wipe them out through the valuation of each share at EUR 0.01. Most of these shareholders were small savers who were not aware of these risks when Bankia had marketed its offerings to them before it went into its IPO (Tremlett 2013).

Consequently, a group of 660 small investors filed a class action lawsuit demanding reimbursement amounting to EUR 6.3 million in 2016. The suit accused Bankia of having a misleading prospectus (Agence France Presse 2016). Ultimately, by 2020, Bankia set aside EUR 1.9 billion in provisions to pay retail investors in several separate civil lawsuits. Although former Bankia chairman Rodrigo Rato was acquitted of wrongdoing pertaining to Bankia’s listing in 2020, he was sentenced in October 2018 to 4.5 years in prison by Spain’s High Court and later by the Supreme Court for embezzlement of Bankia’s funds. (Aguado and Pinedo 2020; Sanz, White, and Aguado 2017).

10. **Treatment of Clients: Affected customers were transferred to the nearest core branch.**

As far as the divestment of assets in the Legacy Unit was concerned, the activities at such branches ceased three months before their closure. The bank informed all the affected customers and clients personally and via mail about the closure and offered the possibility of transferring their accounts to the nearest core branch (EC 2012a).

11. **Treatment of Assets: Real estate assets were transferred to the asset management vehicle, SAREB, at a transfer price of EUR 22.4 billion.**

Real estate assets were transferred to an asset management vehicle named SAREB. This asset management vehicle was set up by FROB in consultation with the EC, ESM, IMF, BoS, ECB and the Ministry of Economic Affairs and Competitiveness. The maximum amount of impaired assets that could be transferred to SAREB was capped at EUR 90 billion (taking into consideration the portfolios of all the other institutions being restructured in Spain at the time, not just BFA-Bankia) (EC 2012e). SAREB was set up as a limited liability company with
its own funding amounting to approximately 8% of the volume of its total assets. The majority holding was to be held by private investors while the rest of the stake (45%) was held by FROB (EC 2012e; Sankar 2021). SAREB paid EUR 22.4 billion for these assets (EC 2012e). These assets were purchased by SAREB on December 31, 2012, using state-guaranteed debt securities issued by SAREB; they carried a one to three-year maturity (EC 2012e; Tam and Fulmer 2021). These bonds, which BFA and Bankia subscribed to, deferred the payment of the difference between the transfer price and the value of the bonds for a period of 36 months (with a possibility of it being offset by SAREB with any amount owed to it by BFA-Bankia under the asset transfer contract). SAREB awarded the servicing of the real estate portfolio of Bankia to Solvia Servicios Inmobiliarios, S.L.U. and the loan portfolio of BFA-Bankia to Haya Real Estate between November and December 2014 (SAREB 2019).

12. Treatment of Board and Management: The restructuring process was overseen by a new management.

In May 2012, Bankia appointed four new top management officials: a new chairman, a new president who would look into financial and risk management strategies, an official in charge of people, media, and technology, and another official to lead the retail division (CaixaBank n.d.; EC 2012e). This appointment followed the resignation of chairman Rodrigo Rato who resigned over disagreements over the audited financial statements and proposed José Ignacio Goirigolzarri, a former chief executive of Banco Bilbao Vizcaya Argentaria (BBVA), as the successor (Barrón 2012; Minder 2012). The change in management accelerated the bank's restructuring, because the new chairman announced a capital shortfall of EUR 4.3 billion as opposed to a surplus that Rato had reported. Goirigolzarri promptly requested a bailout from the government and submitted to stress tests conducted by the BoS and Oliver Wyman (Donnelly and Pometto 2024).

13. Cross-Border Cooperation: The restructuring of BFA and Bankia involved the cooperation of the EC, ECB, EBA, IMF and the ESM.

The restructuring of BFA and Bankia involved cross-border cooperation since the IMF, EC, ECB, EBA, and the ESM monitored Bankia in connection with the Spanish authorities. Moreover, the design of SAREB was influenced by discussions the Spanish authorities had with the ESM, EC, ECB and the IMF (EC 2012a).

14. Other Conditions: FROB implemented several behavioral restrictions on BFA and Bankia during the restructuring period as a result of receiving State Aid.

FROB imposed several restrictions on BFA and Bankia during its restructuring. This included a ban on acquisitions, a ban on coupon payments made to preference shareholders and subordinated debt holders, a ban on using resources received from the aid towards advertising, restrictions on dividend payments and a ban on undertaking aggressive commercial practices (such as having competitive interest rate offerings). Authorities restricted the bank's lending activity, prohibiting lending to any new regions, real estate developments, and some wholesale and international activity (EC 2012e).
15. **Duration:** The bank’s 2012–17 restructuring plan ended in 2017 with most goals accomplished. As of the writing of this case, the Spanish authorities have postponed to 2025 their deadline to divest their stake in the merged institution that the erstwhile Bankia was part of.

The EC approved the restructuring plan for Bankia on November 28, 2012, which outlined that by 2017 the balance sheet of Bankia would shrink by more than 60% relative to 2010 (FDIC 2014). FROB held an indirect stake (owned via BFA) of 61% in Bankia which it intended to divest by December 2021 through a merger with BMN (Sankar 2021). In December 2017, FROB merged Bankia with BMN, with BMN ceasing to exist and the FROB holding a 61.8% stake in the resulting institution, through BFA (Reuters 2021; Zahid 2017).

The period of the bank’s 2012–17 restructuring plan ended on December 31, 2017 (CaixaBank n.d.; EC 2012a). In February 2021, the Spanish authorities decided to extend the deadline of divesting their stake in BMN-Bankia to 2023 (which has now been extended to 2025); at the time of writing this case, FROB still holds a 17.3% stake in CaixaBank, after BMN-Bankia was merged with CaixaBank in 2021 (CaixaBank 2023; Reuters 2021).
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