AA-
stable

Rating Committee: 05/27/2019

GBB-Rating

Banco Santander, S.A.

Rating result

Strengths/Opportunities:

- High profitability and efficiency in a peer group comparison; strategic targets set in 2015 were met
- Sound and sustainable strategy
- Updated mid-term plan: focus on substantial investments in digitalization and cost savings
- Strong position in its core markets
- Broad geographical diversification
- Resilient structure of financially autonomous subsidiaries
- Balanced funding profile and comfortable liquidity position

Weaknesses/Threats:

- CET1 ratio (fully loaded) remains on a comparatively low level
- NPL ratio declining, yet elevated in some regions (e. g. Brazil, Spain, Portugal)
- Ongoing low interest rate environment in advanced economies
- Deteriorating economic outlook particularly in Europe

Financial data:

(in EUR m)	2018	2017
Adjusted gross profit	45,966	44,325
Operating result	14,201	12,091
Net income	9,315	8,207
Total assets	1,459,271	1,444,305
CET1 capital ratio*	11.5 %	12.3 %
Total capital ratio*	15.0 %	15.0 %
Leverage Ratio*	5.2 %	5.3 %
LCR	158 %	133 %
NSFR	114 %	105 %

* phased-in

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Based on the information available, the financial standing of Banco Santander, S.A. (hereinafter referred to as "Santander" or "Group") is again evaluated as high. GBB-Rating confirms the rating result of AA- as well as the stable outlook.

The rating reflects Santander's very high financial standing, which is underpinned by its high level of profitability and the low risk business profile focused on retail and commercial banking. The Group's broad geographical diversification is a major advantage over most competitors, as its strong presence in Latin America (especially in Brazil) provides access to markets with comparatively high interest rates and sufficient growth potential. Santander has a leading market position in retail lending in most of its core markets. The marked increase in client numbers in recent years (144 million at year-end, 2017: 133 million) is partly due to the acquisition and integration of Banco Popular (Spain, Portugal), but it also stems from substantial investments in digitalization and the expansion of online services. According to the updated mid-term plan, Santander plans to invest about EUR 20 billion in digitalization and technology over the next four years. Furthermore, the Group plans to cut EUR 1.2 billion of annual costs, largely in Europe. Overall, Santander has a sound and sustainable business model.

In 2018, Santander reported an operating profit before tax of EUR 14.2 billion compared to EUR 12.1 billion in 2017. The main reason for the increase in profit was the significant decline in provisions and impairments on non-financial assets, in particular on intangible assets (EUR 0.1 billion, 2017: EUR 1.1 billion). The Group's net interest income as the main source of earnings remained almost at prior year's level (EUR 34.3 billion) whilst net commission income slightly decreased (-1 %). Administrative expenses (EUR 20.4 billion) remained stable.
Consequently, Santander's earnings indicators remain at a high level. Based on GBB-Rating's profitability ratios, return on equity improved to 13.3 %, compared to 11.5 % in 2017. The cost income ratio (without provisions for credit risks) remains on an exceptionally low level of 49.6 % (2017: 51.9 %).
In Q1 2019, attributable profit to the parent declined by 10.4 % compared to Q1 2018 as lower earnings in

Summary:

	Rating
Financial profile	strong
- Earnings position	strong
- Capital position	adequate
Business profile	strong
- Strategy and market	strong
- Risk profile	adequate
- Capitalization potential	strong

(strong > adequate > acceptable > deficient > problematic > insufficient)

Rating history:

Rating	Outlook	Date
AA-	**stable**	**05/27/2019**
AA-	stable	12/05/2018
AA-	stable	05/16/2018

Rating scale:

Rating	Rating categories
AAA	highest financial standing
AA+ / AA / AA-	very high financial standing
A+ / A / A-	high financial standing
BBB+ / BBB / BBB-	good financial standing
BB+ / BB / BB-	satisfactory financial standing
B+ / B / B-	financial standing scarcely adequate
CCC+ / CCC / CCC-	financial standing no longer adequate
CC / C	inadequate financial standing
D	moratorium / insolvency proceedings

Continental Europe and in the UK and extraordinary effects (net capital losses, restructuring costs) more than outweighed the strong increase in earnings in Latin America.

In a peer comparison, Santander's capital ratios stand at a relatively low level. At Q1 2019, the Group's CET1 capital ratio was 11.2 % (phased-in and fully-loaded), well above the minimum regulatory requirement of 9.7 %. Given Santander's retail-focused, low-risk business model (low earnings volatility, limited dependency on individual markets and regions) the Group's capital resources are assessed as adequate, further underpinned by the results of the "2018 EU-wider Stress Test Exercise".
The Group's funding plan has focused on TLAC/MREL eligible instruments in recent years. Current MREL requirements are already being met.

The quality of the loan portfolio has improved significantly in recent years. This is reflected in the decline of the NPL ratio in most regions. However, the NPL ratio remains high in some core markets (Spain, Brazil). Despite the NPL's sensitivity to any adverse economic downturn, the recent improvement of the quality of the loan book indicates an adequate risk management. In conjunction with modest market and operational risks and with regard to the Group's comfortable liquidity position, Santander's risk profile is assessed as adequate.

Rating drivers

Santander's rating result strongly reflects the high level of profitability. The rating would stabilize in a consistent profit situation, and it would benefit from further sustainable in-creases in capital and earnings.

The rating could be adversely affected by a global economic slowdown, with negative consequences on consumer confidence and on credit demand by enterprises and households. A weaker economy would usually deteriorate asset quality and increase loan-loss provisions.

Strategy and market

Strategy

Santander has a sound and sustainable strategy, focused on retail and commercial banking. The Group's retail banking, which accounts for 88 % of total gross income in 2018, comprises a comprehensive range of lending and deposit products, including residential mortgages, vehicle financing and SME finance. Further business activities include wealth management (private banking, asset management) and corporate & investment banking (wholesale banking business), which have been established in recent years. Measured by their profit contribution, both divisions are of minor importance.

The Group's business approach is characterized by broad geographical diversification and its model of autonomous subsidiaries. Santander's core markets as measured by attributable profits and the number of customers are Brazil, Spain, the United Kingdom (UK) as well as Central and Northern Europe (Santander Consumer Finance). The geographical reach in both developed, generally low interest rate markets and in emerging, relatively high interest rate markets helps to reduce Santander's sensitivity to economic downturns in individual regions.

Santander defined a number of main strategic targets, comprising qualitative as well as quantitative objectives (e. g. increase in customer satisfaction, growth in customer numbers, target ranges for profitability and efficiency). GBB-Rating attests an efficient strategic management with view to the following objectives:

- The medium-term targets set in 2015 were all met in 2018.
- The return on tangible equity (RoTE) increased to 11.7 % in 2018 from 10.0 % in 2015. The cost-to-income ratio remained below 50 % during this period, considerably lower than the sector average.
- In 2018, the number of customers grew in all target markets (144 million, 2017: 133 million). The rise was particularly pronounced in Spain, Brazil and Mexico. Furthermore, the number of clients who consider Santander their main bank ("loyal customers") increased by 15 %. Since 2015, the number of "digital" customers (commercial banking customers who used online/mobile banking in the last 30 days) rose by 93 %.
- Santander has a leading market position in retail lending in nearly all of its core markets. In the UK and in Brazil, Santander is the largest foreign private bank. In Brazil, the Group's subsidiary is the only foreign bank with a significant market share (about 9 %). In Spain and in Portugal, Santander benefited from the takeover of Banco Popular Español S.A. (Banco Popular) in 2017 (lending share of 18 % in both markets).

Santander's management updated the mid-term plan and strategic targets in April 2019. Over the next four years, Santander plans to invest about EUR 20 billion in digitalization and technology, in particular in digital global payment solutions. The growth in digital offerings includes the launch of open market apps for international payments in European core markets. It also includes the expansion of "GetNet", a subsidiary of Santander Brazil which provides payment transactions with cards and terminals, in Latin America and Europe. Santander plans to cut roughly EUR 1.2 billion of annual costs, largely in Europe. The updated target range for the underlying RoTE (13-15 %) appears to be ambitious but achievable.

Market

The macroeconomic environment deteriorated in 2018 in view of downward revisions of growth forecasts for advanced economies, the economic slowdown in the Eurozone, and the (post-) Brexit uncertainty. Global trade volumes plummeted in Q4 2018 and industrial production sharply decreased in advanced economies and in China except for the USA. Nevertheless, consumer confidence remains on a very high level on a worldwide scale.

In 2018, GDP of the Eurozone rose by 1.8 % (2017: 2.4 %). In response to the slowdown, the European Central Bank adjusted its forward guidance and is likely to maintain the low level of interest rates until at least 2020. The OECD and IMF revised growth forecasts for the Eurozone down to just over 1 % in 2019. For the USA, the IMF also lowered the expected 2019 growth rate to 2.3 % (2018: 2.9 %).

Growth will remain considerably higher in emerging and developing economies than in advanced economies. According to current forecasts, growth in Latin America is projected to recover in 2019 and 2020, mainly driven by Brazil and Mexico.

Albeit Brazil's GDP increased by 1.1 % in 2018, it fell short of forecasts (about 2 %), and grew only marginally in Q4 2018. 2019 and 2020 forecasts predict some moderate growth of around 2 % and 2.5 %, respectively. The unemployment rate remains elevated and volatile, standing at 12.7 % in March 2019. The weaker than expected labor market and the rising inflation (March 2019: 4.6 %) may impede the recovery in purchasing power. On the other hand, the Brazilian banking system is highly profitable with a double-digit average return on equity. As in other Latin American countries, the financial system in Brazil is quite resilient to external shocks due to its experience in managing volatility (economic development, foreign exchange risks) during the past decades. It should also be noted that the number of problem assets of private banks have decreased considerably in the past years, and the reduction of the loan-loss provision was a main driver for the increase in profitability. The implementation of the pension reform remains uncertain but is likely to have a positive impact on the economy.

In 2018, real GDP in Spain grew by 2.5 % (2017: 3.0 %) and above the Eurozone average (1.8 %), driven by consumer spending and investment. In the wake of the positive economic environment in recent years, the unemployment rate fell to 14.5 % in Q4 2018, the lowest level since the beginning of the 2008 Financial Crisis. According to current predictions, growth momentum will slightly fade to 2.2 % in 2019 with view to potential impacts from a slowing global economic environment, the UK's withdrawal from the EU and increasing protectionism. The NPL ratio in Spain developed favorably in recent years to 3.7 % in Q4 2018, however, it still remains above the EU average (3.2 %). Demand for consumer credits should be supported by robust growth of the Spanish economy and should remain at high levels, despite a dip in Q1 2019 and tightened credit standards.

The economic development in the United Kingdom is strongly influenced by political uncertainty on the withdrawal from the European Union. At this stage, the EU delayed Brexit until the end of October 2019. In the past two years, investment fell behind the OECD average and consumer confidence declined. The short-term projection for GDP growth stands at 1.0 % to 1.5 %, primarily based on the stable inflation, the robust labor market and growing wages. The fundamental data of the UK's banking sector are sound with historically low NPL ratios and an average CET 1 ratio (fully loaded) of 15.1 % as of Q4 2018, close to the EU average. According to recent stress test results conducted by the British banking supervision (assumptions: "hard" Brexit, recession lasting several years), the long-term fundamental position of British banks may worsen, however, they show a high level of resilience and have sufficient leeway in an adverse economic scenario. Retail Banking is dominated by four large domestic banks (Lloyds, Barclays, RBS, HSBC) and Santander UK. Consumer lending grew strongly in recent years, albeit credit growth slowed down to about 8 % between Q3 2017 and Q3 2018. Positively, mortgage lending increased at about 3 % in the same period. Growth rates are expected to remain at this level in 2019.

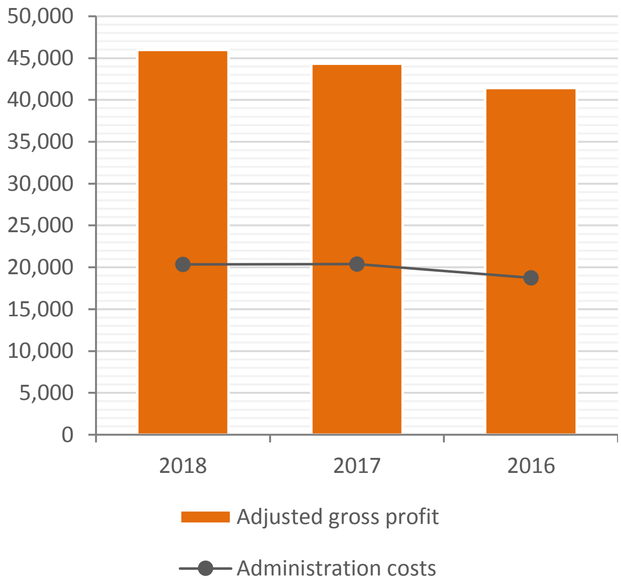
Strong long-term earnings position

Santander's long-term earnings position is assessed as strong. The Group's profitability, which is already at a very high level, continued to improve in 2018. According to GBB-Rating's calculation method (see appendix), the return on equity rose to 13.3 % compared to 11.5 % in 2017. The cost income ratio remains at a remarkably low level in comparison to peers and stood at 49.6 % in 2018 (2017: 51.9 %). Taking into account impairment losses ("cost-income ratio I", see appendix), the ratio also improved to 66.4 % from 67.8 %.

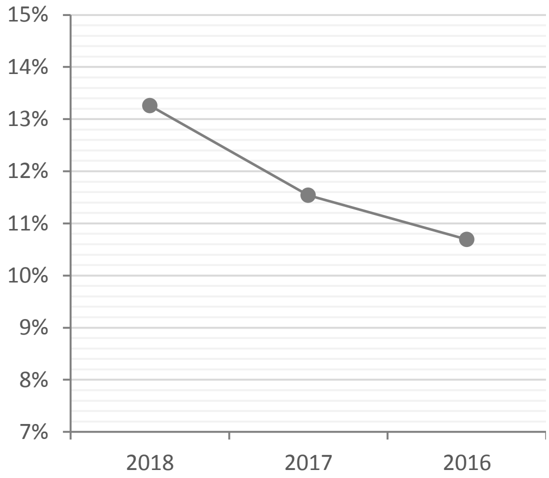
The improvement in the profitability and cost indicators stems mainly from the increase in adjusted gross profit and operating profit which are primarily due to the significant decline in impairment losses on intangible assets to EUR 0.1 billion (2017: EUR 1.1 billion) and lower provisions of EUR 2.2 billion (2017: EUR 3.1 billion). The Group's net interest income as the main source of earnings was virtually unchanged (EUR 34.3 billion). The net commission income slightly decreased (-1 %), mainly due to higher commission expenses. The result from categories of financial instruments rose by EUR 0.9 billion to EUR 2.8 billion, partly due to higher gains on financial assets and liabilities held for trading. The positive developments in provisions and impairments and in the result from categories of financial instruments more than outweighed the losses on exchange differences of EUR 0.7 billion (2017: gain of EUR 0.1 billion) and the sharp decline in gains on non-financial assets to EUR 0.0 billion from EUR 0.5 billion due to the sale of Allfunds Bank in 2007. Overall, the adjusted gross profit rose by nearly 4 %.

Administration costs remained almost unchanged at EUR 20.4 billion as the decrease in staff costs was offset by the rise in IT expenditures. Impairment of financial assets measured at amortized costs further decreased by nearly 3 % to EUR 9.0 billion. As a result, profit before tax grew by EUR 2.1 billion to EUR 14.2 billion.

Development of adjusted gross profit and administration costs (EUR m)



Return on equity (%)



Interim result as of 31 March 2019

In comparison to Q1 2018, total income declined by 0.5 %. Whilst net interest income increased by 2.7 %, it was offset by lower gains on financial transactions and exchange differences, primarily due to higher costs of foreign currency hedging. Compared to Q4 2018, total income was 3.6 % lower, mainly due to weaker net interest income (-4.2 %) from the impact of the revised IFRS 16 and fewer days in the quarter.

Operating expenses stayed flat in comparison to Q1 2018 and declined by 3.0 % compared to Q4 2018.

Falling total income was compensated by a further decline in loan-loss provisions (-4.8 % compared to Q1 2018). As a result, underlying profit before tax was just 0.1 % below the level of Q1 2018, and higher than in Q4 2018 (+3.9 %).

The attributable profit to the parent (-11.0 % compared to Q4 2018; -10.4 % compared to Q1 2018) was negatively affected by a higher tax on profit, restructuring costs (Poland, UK) and capital losses due to property sales.

In Continental Europe, underlying profit before tax fell by 3.4 % compared to Q1 2018, with a marked decline in Spain (-10.5 %, mainly due to lower gains in financial transactions). In the UK, profit before tax declined sharply by 16.8 % since total income was negatively impacted by competitive pressure, lower mortgage margins and lower gains on financial transactions; the attributable profit was even 36.0 % lower than in Q1 2018 because of restructuring costs (branch closures). In contrast, profit before tax rose by 5.5 % in Latin America, with substantial profit growth in Brazil (+8.4 %) and Mexico (+20.0 %).

Interim Results* (EUR m)	**Q1 2019**	**Q4 2018**	**Q1 2018**
Net interest income	8,682	9,061	8,454
Net fee income	2,931	2,956	2,955
Total income	**12,085**	**12,542**	**12,151**
Operating expenses	-5,758	-5,936	-5,764
Net operating income	**6,327**	**6,606**	**6,387**
Net loan-loss provisions	-2,172	-2,455	-2,282
Underlying profit before tax	**3,684**	**3,546**	**3,689**
Underlying profit from continuing operations	**2,358**	**2,369**	**2,409**
Attributable profit to the parent	**1,840**	**2,068**	**2,054**

* Based on Santander's interim accounts without GBB-Rating adjustments

In consequence of the lower attributable profit, the Group's RoTE dropped by 0.8 percentage points to 11.3 % compared to Q4 2018 but remains on a high level. The cost-to-income ratio maintains a comparatively low level (47.6 % in Q1 2019).

Adequate sustained capital position

As of 31 March 2019, Santander's CET1 ratio stood at 11.3 %, both on a phased-in and on a fully-loaded basis; the leverage ratio was 5.1 %. The Group targets a CET 1 capital ratio (fully-loaded) between 11 % and 12 % in the medium term. On a fully-loaded basis, total capital increased to EUR 90.0 billion in Q1 2019 (compared to EUR 87.5 billion as of 31 December 2018). The Group applies the transitional arrangements of IFRS 9 according to Article 473a of the CRR, mitigating the impact of the new impairment regime. According to Santander, the fully loaded CET1 ratio would decrease to 11.0 % with full implementation of IFRS 9 (as of March 2019).

Santander's capital ratios clearly exceed the regulatory minimum requirements of 13.2 % for the total capital ratio and 9.7 % for the CET 1 capital ratio (as of March 2019), with a Pillar 2 requirement of 1.5 % and a combined buffer requirement of 3.7 %. In Q1 2019, the buffer to the Maximum Distributable Amount (MDA) was 1.6 percentage points and therefore quite comfortable.

Selected data: Capital structure (EUR m)	**03/31/2019 Phased-in**	**03/31/2019 Fully-loaded**	**12/31/2018 Phased-in**	**12/31/2018 Fully-loaded**
Common equity tier 1 capital	68,230	68,230	67,962	66,904
Tier 1 capital	77,705	75,826	77,716	75,838
Total capital	90,141	89,983	88,725	87,506
Risk-weighted assets	606,300	606,300	592,319	592,319
CET1 capital ratio	11.25 %	11.25 %	11.47 %	11.30 %
Tier 1 capital ratio	13.05 %	12.91 %	13.12 %	12.80 %
Total capital ratio	14.87 %	14.84 %	14.98 %	14.77 %

Compared to its peers, Santander's capital ratios are on a comparatively low level. This is also reflected in the results of the "2018 EU-wide Stress Test" which ranks Santander's fully-loaded CET1 capital ratio lower than those of all other 47 participants. However, the stress test indicated that the adverse scenario resulted in one of the exercise's most contained negative impacts on the fully-loaded CET1 capital ratio between 2017 and 2020, reflecting the Group's sound risk profile. Santander was also one of few participants that were able to generate a cumulative profit in a three-year adverse scenario.

MREL/TLAC

In recent years, Santander's funding plan has focused on MREL/TLAC eligible instruments as part of the resolution strategy. Since the TLAC requirement is requested at each resolution entity, Santander's operating model of legally independent subsidiaries renders multiple points of entry. In consideration of Santander's minimum TLAC requirement of 16.0 % of resolution group RWAs, the G-SIB buffer (1.0 %) and the capital conversation buffer (2.5 %), the Group's TLAC requirement is 19.5 % of RWA as of January 2019.

Santander received formal notification of the MREL requirement in May 2018 for the Banco Santander S.A. Resolution Group at a sub-consolidated level; the minimum required eligible liabilities were set at EUR 114.5 billion, representing 24.35 % of the Resolution Group's risk-weighted assets. These current requirements are met by Santander.

In order to comply with the TLAC/MREL requirements, on a Euro-basis, the Group issued EUR 13.5 billion of eligible instruments (2017: EUR 19.8 billion). This issue volume is dominated by senior non-preferred and other senior debt (EUR 10.3 billion). In Q1 2019, Santander issued TLAC eligible preferred debt in the amount of EUR 1.1 billion.

Strong capitalization potential

In light of Santander's strong earnings position, the Group has a strong and sustainable internal financing capacity. Since 2009, the Group's net operating income never fell below EUR 20 billion, illustrating the sustainability of the bank's profits and its relatively low susceptibility to earnings volatility.

Santander's ability to strengthen its capital resources by way of capital market issues is assessed as strong (see "sustained capital position"). In order to strengthen AT1 capital, the bank recently issued CoCo bonds (February 2019: USD 1.2 billion; March 2018: EUR 1.5 billion).

By market capitalization, Banco Santander is the largest bank in the Eurozone, although the bank's share price fell by more than 27 % in 2018 (market capitalization: EUR 64.5 billion as of 31 December 2018; 2017: EUR 88.4 billion). The decline was in line with the poor general market trend in 2018.

At the end of 2018, Santander had about 4.1 million shareholders. Institutional investors held about 59 % (2017: 61 %) of the share capital; nearly 40 % (2017: 38 %) of Santander's share capital were in the hands of retail investors. The majority of the share capital (> 75 %) is located within Europe. As in previous years, no shareholder (with the exception of custodians) had an ownership interest greater than 3 %. Due to the diversified ownership structure, a shareholder's support in case of need is considered unlikely.

Risk profile

Credit and counterparty risk

The main geographical markets in terms of total lending are Spain, the UK, Brazil and the United States. More than half of the lending volume accounts for secured loans (e. g. mortgage loans).

Over the past few years, the credit quality improved to a significant extent as reflected in the steady decline of the NPL ratio in most markets. As of Q1 2019, the overall NPL ratio amounted to 3.6 % (Q1 2018: 4.0 %). In the same period, the volume of non-performing loans fell by 4.9 % to EUR 35.6 billion. In line with the overall trend, the NPL ratio continuously decreased in Continental Europe in recent years (Q1 2019: 5.2 %; Q1 2018: 5.8 %). However, it remains elevated in Spain (Q1 2019: 6.2 %; Q1 2018: 6.3 %) due to the acquisition of Banco Popular in 2017 and despite the sale of Banco Popular's real estate business; excluding Popular's portfolio, the NPL ratio stood at just 4.7 % at the end of 2017. In the UK, the NPL ratio remains on a considerably lower level (Q1 2019: 1.1 %). Until now, negative impacts on the NPL of the impending Brexit have not been discernible. In the United States, the NPL ratio stayed on an acceptable level (Q1 2019: 2.4 %; Q1 2018: 2.9 %). In Brazil, which is the Group's key market in Latin America, the NPL ratio remains high (Q1 2019: 5.3 %, at previous year's level). The same applies to the cost of credit which dropped to 3.9 % in Q1 2019 (Q1 2018: 4.4 %), but remains high compared to the Group level.

As to the coverage ratio, there was a downward trend in Continental Europe over the past years (Q1 2019: 52.1 %; 2015: 64.2 %), whereas it increased in Latin America (Q1 2019: 97.7 %). In the USA, the ratio remained well above 100 %. In Spain and in the UK, the coverage ratio remains low (44.1 % and 31.0 %, respectively) as a result of the dominant mortgage portfolios. In this context, it should be noted that more than 80 % of the residential mortgage portfolio in Spain has an LTV below 80 %; in the UK, the average LTV is about 40 %.

In view of the bank's progress in credit risk mitigation, GBB-Rating evaluates the risk management and risk monitoring systems to be appropriate and effective. Nevertheless, it remains to be monitored how a possible economic downturn may effect credit quality.

Market risk

The Group faces limited interest and exchange rate risks arising from the banking book; market risks resulting from trading activities are of minor importance.

In line with the BCBS standards for Interest Rate Risks in the Banking Book (IRRBB), Santander conducts six interest rate scenarios, measuring the interest rate risk on both economic values (EVE) and earnings (NII). As in the previous year, a parallel downward shock would have the most severe impact on the change in economic value of equity (EUR 8.0 billion as of 31 December 2018); however, the "early warning signal" according to the IRRBB guidelines released by EBA (threshold: decline in economic value greater than 15 % of Tier 1 capital) is not exceeded.

A rise in interest rates would have opposite effects in the Group's core markets: in Europe and in the USA, where interest rates are at a very low level, a rise in interest rates would positively affect net interest income and the economic value of equity; in Latin America, earnings and economic values would decrease.

Since the structural VaR was considerably higher than the trading risk VaR (EUR 568.5 million vs EUR 9.7 million as of 31 December 2018), the main drivers for market risks derive from the banking book. Regarding Santander's capital base and its profitability, market risks are deemed manageable.

Funding and liquidity

The majority of Santander's total assets account for net loans to customers with a long-term maturity; the Group's funding is based on predominantly short-term customer deposits and, to a lesser extent, medium- and long-term financial instruments. Due to the high extent of retail and commercial banking, the Group has a sufficiently large and stable base of customer deposits.

As of 31 December 2018, the LTD ratio was at 113 % (2017: 109 %; target: below 120 %), well in line with the European average[1].

The regulatory liquidity ratios indicate a comfortable liquidity position. As of end-2018, the Group's LCR stood at 158 % and the NSFR was at 114 %. In all legal entities, both ratios were above 100 %.

In view of the sound balance sheet structure, the diversified funding structure and the robust liquidity ratios, the Group has in place a sound and effective liquidity risk mitigation.

Operational and legal risks

The provisions for customer remediation account for 12 % of total provisions for taxes and other legal contingencies and mainly include the estimated redress payments relating to the sale of Payment Protection Insurance (PPI) policies in the UK. The deadline for PPI complaints is 29 August 2019. With respect to the mis-selling of PPI, Santander UK plc raised provisions of EUR 275 million for PPI and EUR 406 million for related costs.

Provisions for employment-related proceedings in Brazil amount to EUR 859 million at year-end 2018. These legal proceedings have been mainly initiated by trade unions, associations and former employees to claim overtime pay, retirement benefits and compensation associated with other employment rights. Such proceedings are common practice in Brazil, and provisions are similarly high as in previous years.

Further legal risks may arise from the acquisition of Banco Popular, which had concluded a high number of transactions with floor clauses ("Clausula Suelo"). In the past years, resulting from several rulings of the EU Court of Justice and of Spanish courts, borrowers have been able to lodge complaints for overpaid amounts due to the floor clauses. Provisions used for refunds in 2017 and 2018 amounted to EUR 357 million. As of end-2018, provisions amount to EUR 104 million.

As the successor entity to Banco Popular, Santander is exposed to legal risks resulting from claims of investors of Banco Popular against the EU’s Single Resolution Board (SRB) decision (resolution of Banco Popular, redemption and conversion of capital instruments). Santander estimates compensation payments to shareholders at EUR 680 million.

[1] According to EBA, the EU average for the LTD ratio for households and non-financial corporations was 117 % (Dec. 18)

In 2018, about 60 % of net losses resulting from operational risks refer to the risk category "practices with customers, products and business practices", which include customer complaints for improper marketing and inaccurate information on products. In addition, external fraud, in particular the fraudulent use of debit and credit cards and incidents related to the execution, delivery and process management are of relevance. By geographical distribution Brazil accounts for 45 % of net losses, employee litigation not included.

Appendix

Assets – selected data (EUR m)	**12/31/2018**	**12/31/2017**	**12/31/2016**
Cash and cash balances at central banks	113,663	110,995	76,454
Financial assets held for trading	92,879	125,458	148,187
Financial assets at fair value through profit or loss	68,190	34,782	31,609
Financial assets at fair value through other comprehensive income	121,091		
Financial assets available-for-sale		133,271	116,774
Financial assets at amortized cost	946,099		
Loans and receivables		903,013	840,004
Investments held-to-maturity		13,491	14,468
Hedging derivatives	8,607	8,537	10,377
Fair value changes of the hedged items in portfolio	1,088	1,287	1,481
Investments accounted at equity / in associates	7,588	6,184	4,836
Intangible assets	3,094	2,914	2,697
Goodwill	25,466	25,769	26,724
Tangible assets	26,157	22,974	23,286
Assets held for sale	5,426	15,280	5,772
Tax assets	30,251	30,243	27,678
Other assets	9,672	10,107	8,778
Total assets	**1,459,271**	**1,444,305**	**1,339,125**

Liabilities – selected data (EUR m)	**12/31/2018**	**12/31/2017**	**12/31/2016**
Financial liabilities held for trading	70,343	107,624	108,765
Financial liabilities designated at fair value through profit or loss	68,058	59,616	40,263
Financial liabilities at amortized cost	1,171,630	1,126,069	1,044,240
Hedging derivatives	6,363	8,044	8,156
Fair value changes of the hedged items in portfolio	303	330	448
Provisions	13,225	14,489	14,459
Tax liabilities	8,135	7,592	8,373
Other liabilities	13,853	13,708	11,722
Equity	107,361	106,833	102,699
Total liabilities and equity	**1,459,271**	**1,444,305**	**1,339,125**

Income statement (EUR m)	**2018**	**2017**	**2016**
Net interest income	34,341	34,296	31,089
Net fee and commission income	11,485	11,597	10,180
Dividend income	370	384	413
Realized gains and losses on financial assets & liabilities not measured at FVtPL, net	604	386	800
Gains (losses) on financial assets and liabilities held for trading, net	1,515	1,252	2,456
Gains (losses) on financial assets and liabilities at FVtPL, net	274	-85	426
Gains (losses) from hedge accounting, net	83	-11	-23
Gains (losses) from insurance business	51	57	63
Other net operating income	-2,824	-3,551	-4,000
Impairment on goodwill	67	0	22
Adjusted gross profit	**45,966**	**44,325**	**41,426**
Administration costs	-20,354	-20,400	-18,737
Depreciation	-2,425	-2,593	-2,364
Impairment	-8,986	-9,241	-9,557
Operating result after provisions for credit risks and valuation adjustments	**14,201**	**12,091**	**10,768**
Income (expenses) related to extraordinary events	0	0	0
Gross result at year-end	**14,201**	**12,091**	**10,768**
Tax expenses related to profit or loss from continuing operations	-4,886	-3,884	-3,282
Net income	**9,315**	**8,207**	**7,486**

Credit and Counterparty risk cluster	2018	2017	2016
Gross profitability 1 Adjusted gross profit / Average Total assets	3.2 %	3.2 %	3.1 %
Gross profitability 2 Net interest income and net credit risk provisions / Average risk-weighted exposure amounts [1]	5.0 %	4.8 %	4.4 %
Net profitability 1 Operating result after provisions for credit and valuation adjustments / Average total risk exposure amount	2.4 %	2.0 %	1.9 %
Net profitability 2 Gross annual profit / Average adjusted total assets [2]	0.9 %	0.8 %	0.8 %
Return on equity 1 Operating result after provisions for credit risks and valuation adjustments / Average total capital	13.3 %	11.5 %	10.7 %
Return on equity 2 Gross annual profit / Average total capital	13.3 %	11.5 %	10.7 %
Cost income ratio 1 Administration costs and provisions for credit risks / Gross profit	66.4 %	67.8 %	69.4 %
Cost income ratio 2 Administration costs / Adjusted gross profit	49.6 %	51.9 %	50.9 %

Financial data (EUR m)	12/31/2018	12/31/2017	12/31/2016
Net interest income	34,341	34,296	31,089
Net interest income and net provisions for credit risks	25,355	25,055	21,532
Gross profit	47,845	47,575	44,178
Adjusted gross profit	45,966	44,325	41,426
Administration costs	-22,779	-22,993	-21,101
Administration costs and provisions for credit risks	-31,765	-32,234	-30,658
Operating result after provisions for credit risks and valuation adjustments	14,201	12,091	10,768
Gross annual profit	14,201	12,091	10,768
Average risk-weighted exposure amounts[1]	509,390	525,926	493,548
Average total risk exposure amount	593,822	613,714	581,748
Average total assets	1,451,788	1,391,715	1,339,693
Average adjusted total assets[2]	1,616,153	1,463,661	1,407,942
Average total capital	107,097	104,766	100,726

[1] Risk weighted exposure amount for credit, counterparty credit and dilution risks and free deliveries
[2] Comprises on-balance sheet total assets, contingent liabilities and loan-loss allowances

Indicators of sustained capital position	12/31/2018	12/31/2017	12/31/2016
Total capital ratio Own funds / Total risk exposure amount	15.0%	15.0%	14.7%
Tier 1 capital ratio Tier 1 capital / Total risk exposure amount	13.1%	12.8%	12.5%
Common equity Tier 1 ratio Common equity tier 1 capital / Total risk exposure amount	11.5%	12.3%	12.5%

Financial data (EUR m)	12/31/2018	12/31/2017	12/31/2016
Own funds	88,725	90,706	86,337
Tier 1 capital	77,716	77,283	73,709
Common equity Tier 1 capital	67,962	74,173	73,709
Total risk exposure amount	592,319	605,064	588,088

Regulatory disclosure requirements

Name and function of the analysts:

- Daniel Sebastian Bittner, Lead Rating Analyst GBB-Rating, Cologne
- Angelika Komenda, Rating Analyst GBB-Rating, Cologne

Company address:

- GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH, Kattenbug 1, 50667 Cologne

Members of the Rating Committee:

- Stefan Koll, Manager GBB-Rating, Cologne
- Christina Weymann, Senior Manager GBB-Rating, Cologne
- Volker Jindra, Senior Manager GBB-Rating, Cologne

Date	Rating Commitee	Notification	Issue
First rating	12/19/2013	12/20/2013	02/26/2014
Current rating	05/27/2019	05/27/2019	

Validity:

- Rating: 12 months
- Outlook: 24 months

Subsequent rating changes after notification to client:

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Major sources of information for the rating:

- Annual report as at 12/31/2018
- Quarterly Report Q1 2019
- Conference calls
- Further disclosures and company specific information

Statement about the quality of information available (including potential restrictions):

- The quality and extent of information (interviews and documents) were suitable to obtain a comprehensive picture of the bank and to assign an objective, transparent and professional credit rating

Applicable rating methodology, rating type and release:

- Solicited rating
- Methodology for Rating 3.0.03 Banks – credit and counterparty credit risk (CCR)
- www.gbb-rating.eu/de/presse/eu-veroeffentlichungen/Seiten/default.aspx

Meaning of the rating category:

- www.gbb-rating.eu/en/ratings/ratingskala/Pages/default.aspx

Business relationship:

- Besides the rating mandate there are further business relationships within the group

Legal remarks

GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH does not make any guarantees regarding the accuracy, completeness or timeliness of the present rating or the data, values and other information presented (including ERI) or the eligibility of this information for specific purposes nor for losses arising from the use of the information or in confidence in the information. The current rating report is not an investment recommendation.

Future events are uncertain. Ratings are based on predictions of these and thus inevitably rely upon estimates. Therefore they solely represent statements of opinion rather than statements of fact or investment advice.

Credit ratings are performed with proficiency and due professional care. Ratings are based on the data and information provided by the applicant. This information is used in reaching an opinion about the future viability as well as the strengths and weaknesses of the rated company as of the date of rating issuance.

GBB-Rating puts focus on sustainability and is a signatory of the UN Global Compact since 2018. We support the 10 principles of the UN Global Compact relating to human rights, labor standards, the environment and anti-corruption.

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