

*Banesto*

Morgan Stanley

April 1<sup>st</sup>, 2008

# Current tougher economic environment requires...

## 1. ...excellence in risk management...

- Business risk
- Credit risk
- Liquidity risk

## 2. ...and best customer management, with focus on...

- Customer funds
- Customer spreads management
- Personalized service

## 3. ...and we have room to improve...

- ...in efficiency and productivity...
- ...in the SME segment...
- ...in the branch network
- ...and in our distribution capacity

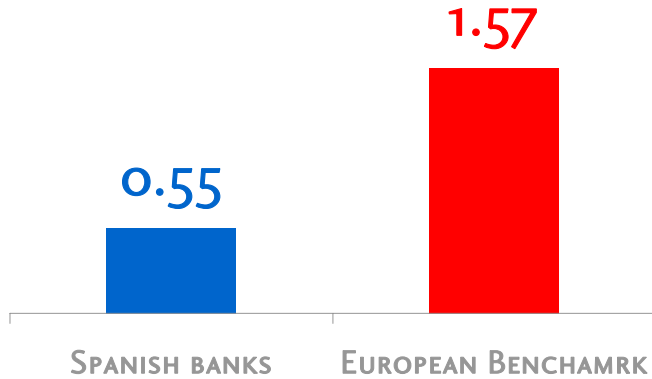
1 Current environment requires excellence in risk management

## Tougher environment...

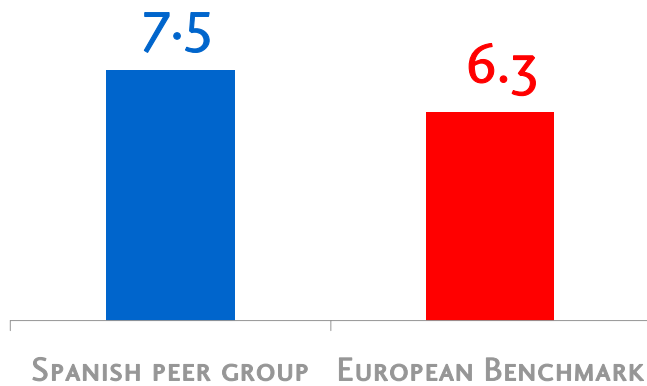
- Rises in credit and liquidity risk premiums.
- General lack of confidence due to financial complexity and lack of transparency.
- ECB committed in supplying enough liquidity.
- Market turbulences add some uncertainties on:
  - Economic growth.
  - Lending activity

# ...in which the Spanish banking system is well prepared...

NPL Ratio (%)



Adjusted core capital (%)\*



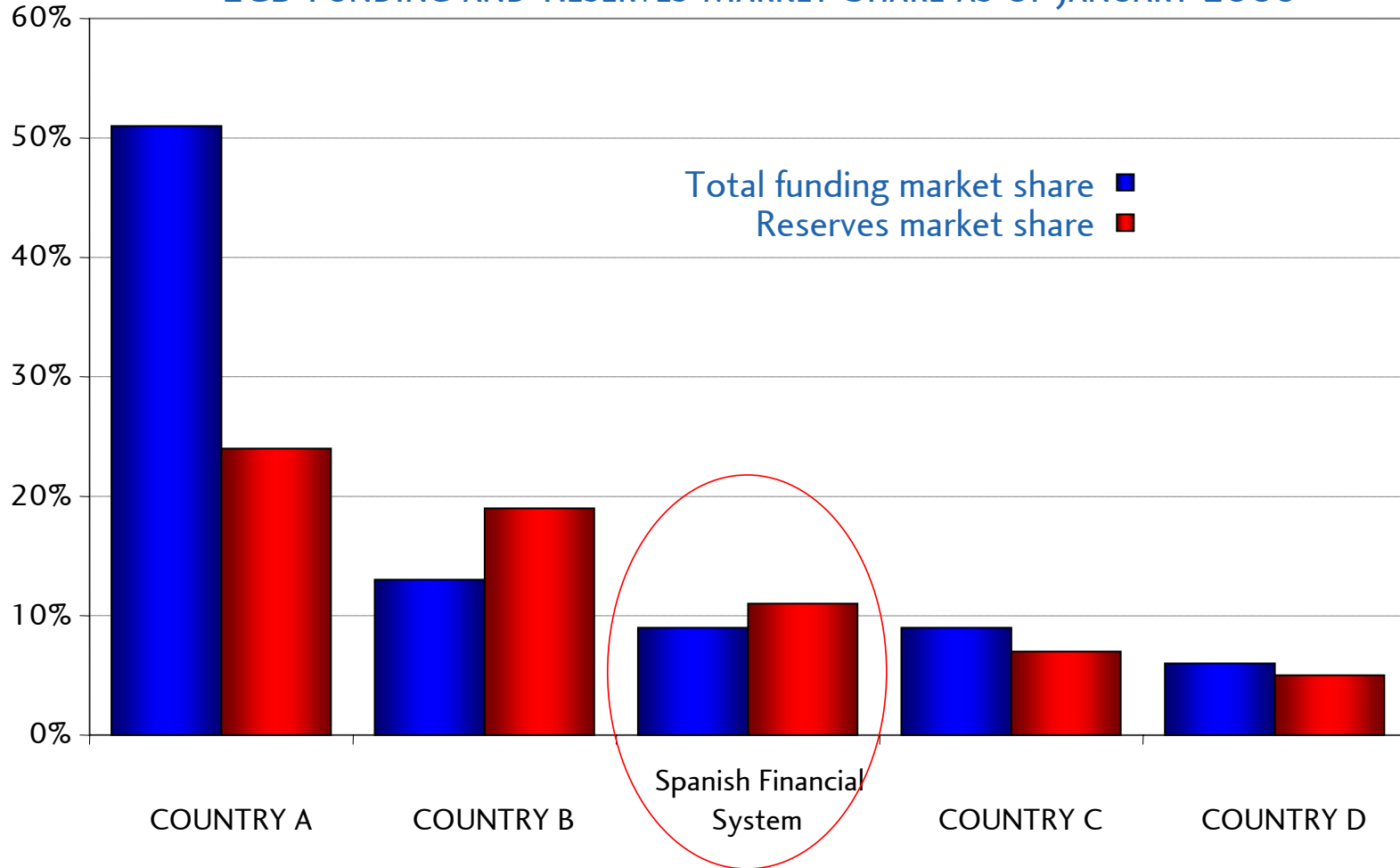
Rating	Average 3 largest banks
Spain	AA
Germany	A/AA
France	AA-/AA+
Italy	A+/AA-
UK	AA-

(\*) Including generic provisions

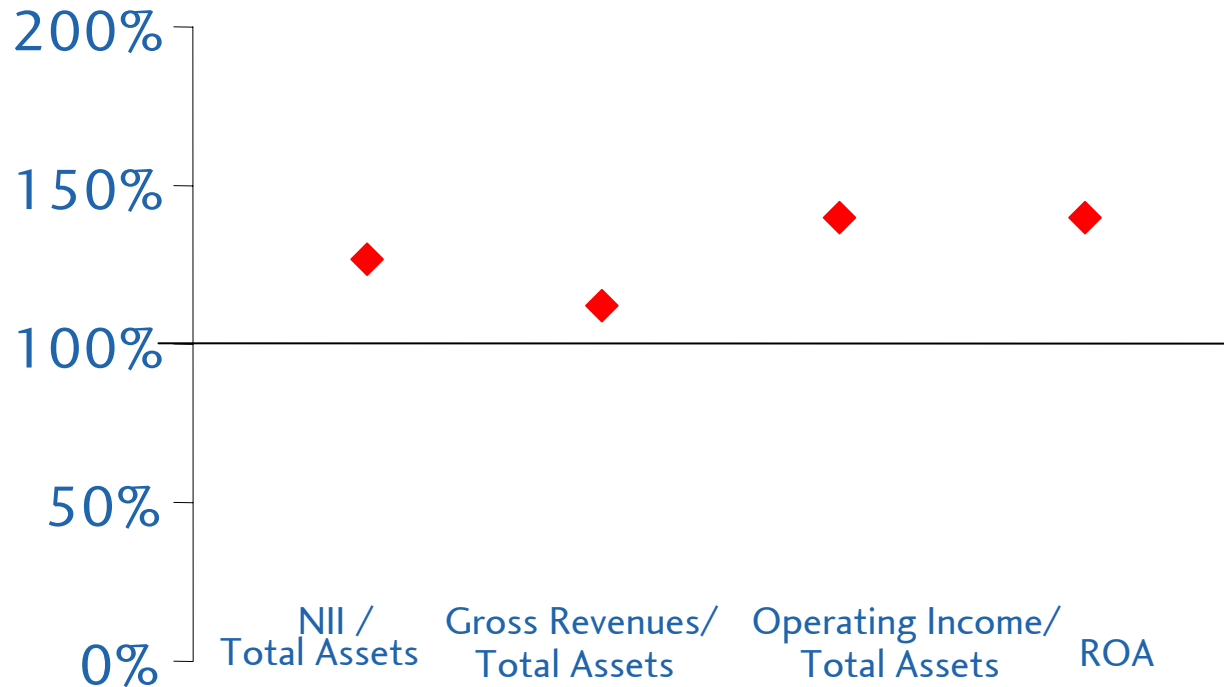
Source: S&P

...also in terms of liquidity...

ECB FUNDING AND RESERVES MARKET SHARE AS OF JANUARY 2008



## Profitability gap between Spanish and EU banking system



Source: Bank of Spain. Stability report Nov. 07. Countries that present their accounts under IFRS

# Banesto is well-positioned to face current environment...

## 1. Business Risk

- Diversified businesses

## 2. Credit Risk

- Prudent risk management policies
- No exposure in assets damaged by the crisis
- Good quality mortgage portfolio
- NPL ratio < Sector avg. + NPL Coverage > Sector avg.

## 3. Liquidity Risk

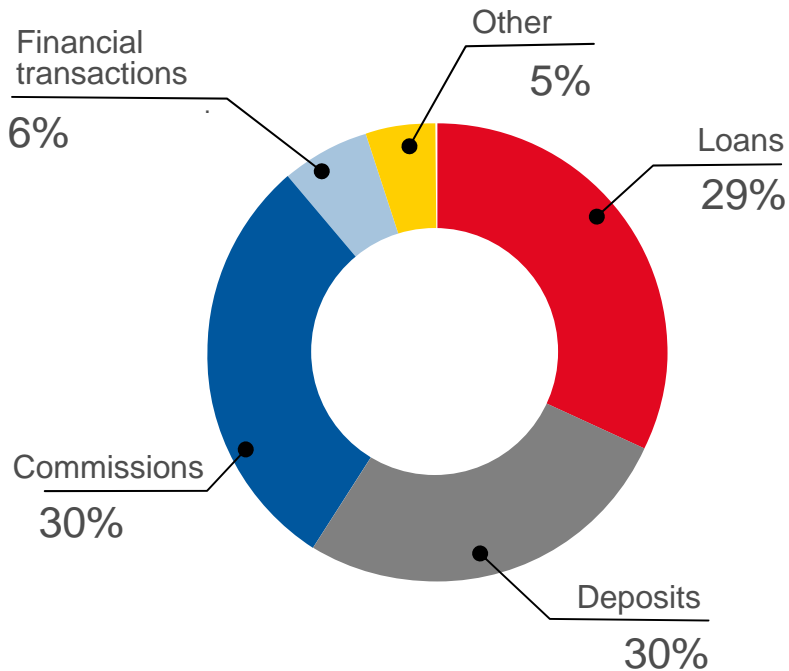
- Positive liquidity position in the S/T and M/T
- Capacity to generate new liquidity



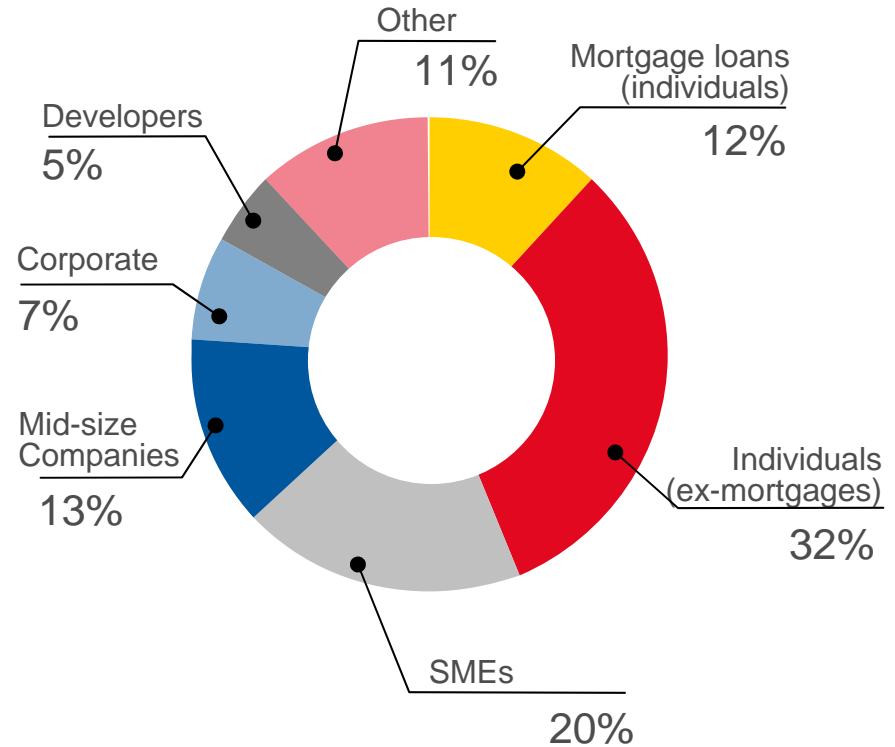
# 1.- Business risk management

A well diversified business profile

Revenues by business line  
Dec 07 (%)



Revenues by client segment  
Dec 07 (%)



## 2.- Credit risk management

- Increasing risk **focus** in the organization
- **Selective** lending growth
- **Active** risk management
- Maximizing **recoveries** process

Asset quality  
above industry  
average

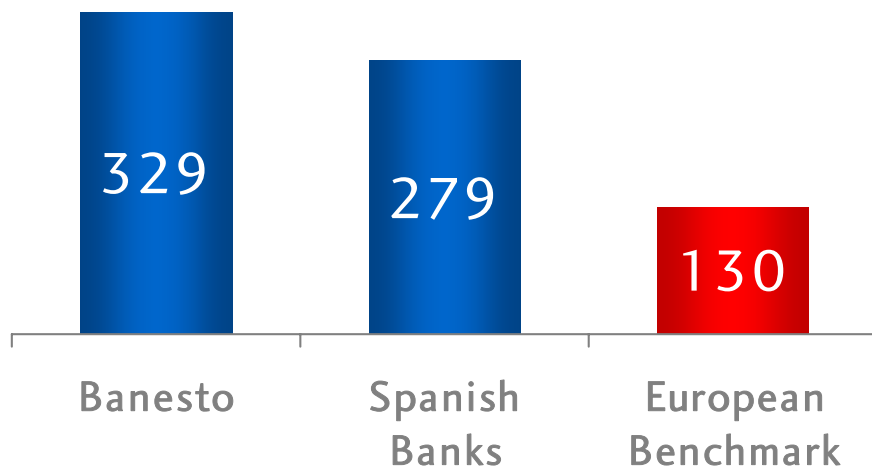
## 2.- Credit risk management (cont)

High credit quality and strong provisions

NPLs



Credit Risk Provisions  
(% NPLs)

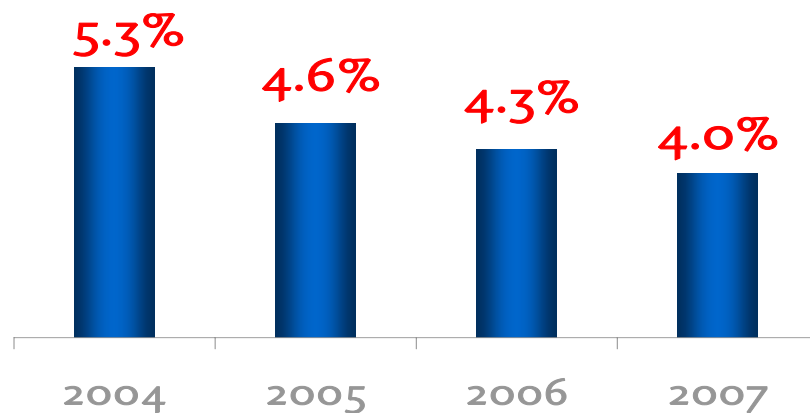


**TOTAL PROVISIONS OF 1.3 BN € 2% LOAN BOOK**

Data as of Dec 07 for Banesto and Spanish banks.  
Last available data for banks included in European benchmark

## 2.- Credit risk management (cont)

A declining real estate exposure relative to the market ...



### Home mortgage loans

### Real estate developers

% First residence	98	% First residence	98
% Loan-to-Value	56	% Debt / GAV(*)	43
% Affordability	32.9	% Pre-sales	47
% NPLs	0.50	% NPLs	0.07
% Expected loss	0.17	% Expected loss	0.24

...and a solid and well-guaranteed mortgage lending risk indicators

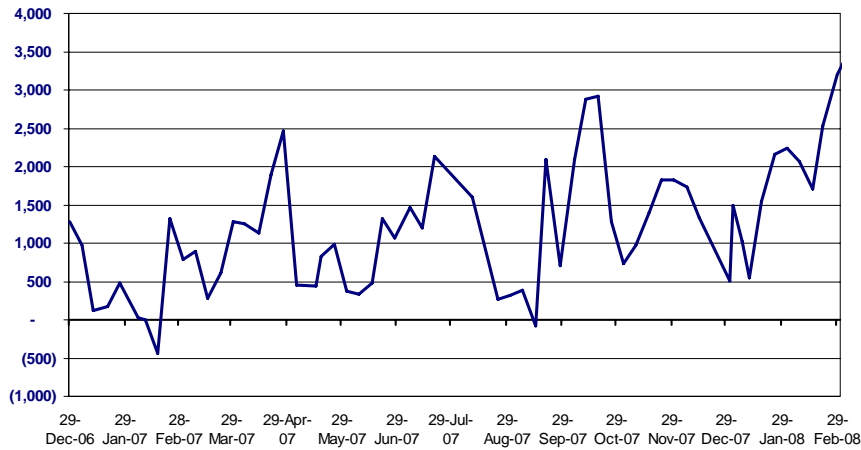
Real estate exposure defined as Loans to real estate activities and market share over total Spanish system.

\* Debt / GAV of 20 largest developers

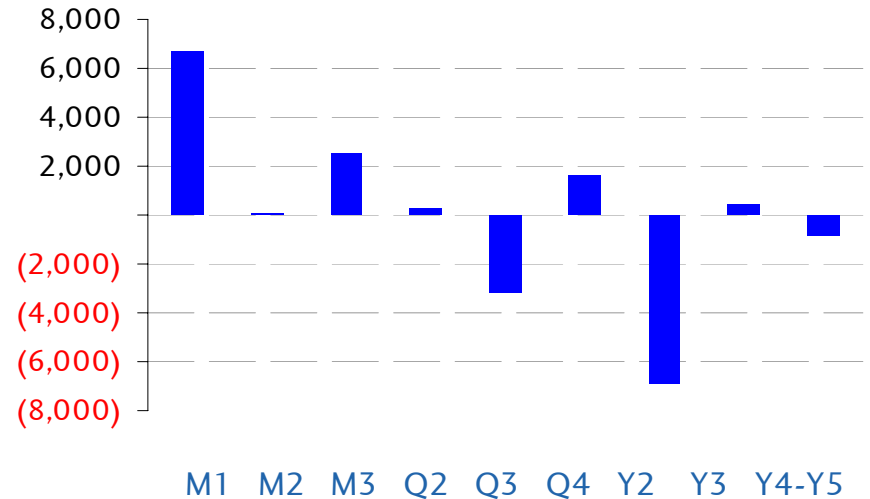
# 3.- Liquidity risk management

## Comfortable liquidity position...

Net positive position in money market



Liquidity gaps in the balance sheet



(EUR million)

### 3.- Liquidity risk management *(cont)*

...that has been reinforced in 1 Q08

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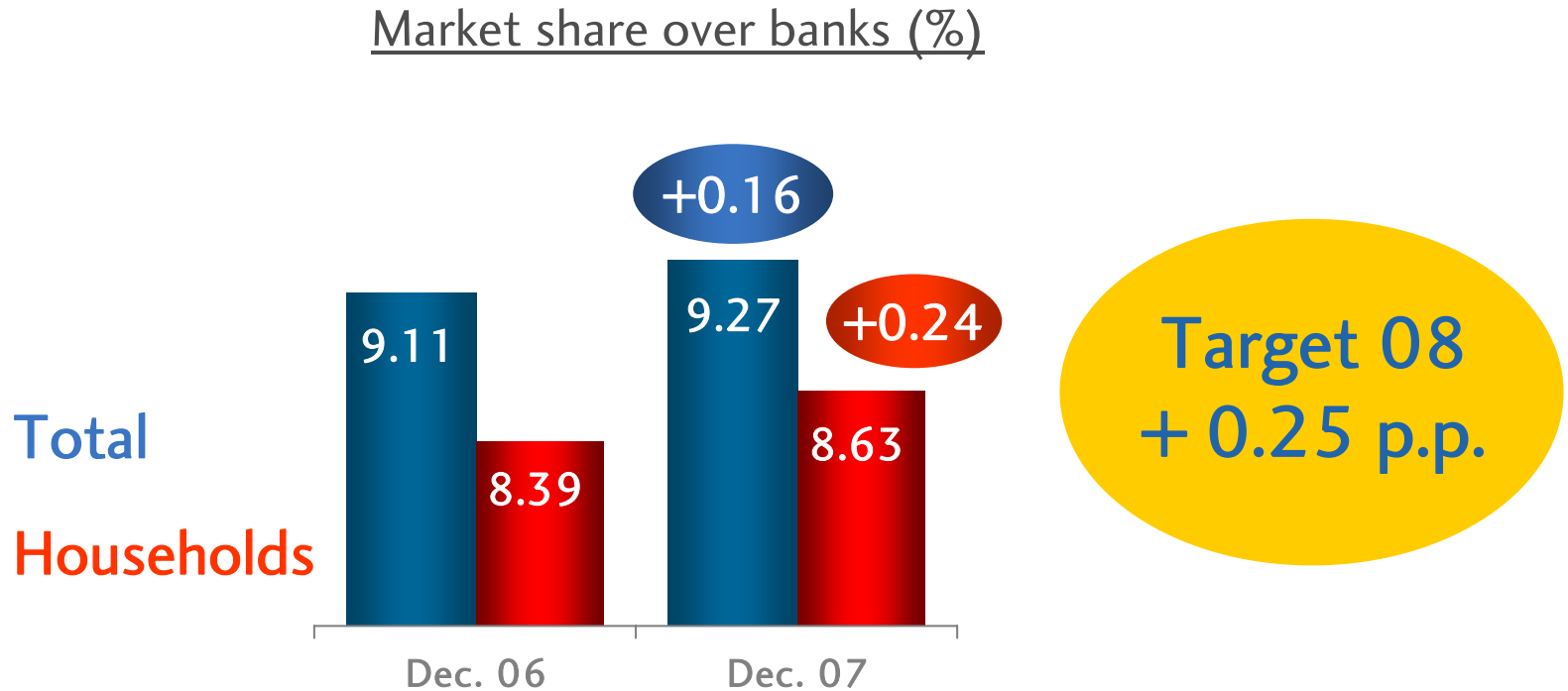
✓ Medium term funding:	+Eur 1.8 bn.
✓ Euro Commercial Paper:	+Eur 2.4 bn.
• Total wholesale funding:	+Eur 4.2 bn.
• Positive net position in Money Market:	+Eur 3.8 bn.

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## 2 Current environment requires best customer management

# 1.- Focus on customer funds

Market share **gains** in customer funds...



...and special focus on deposit growth

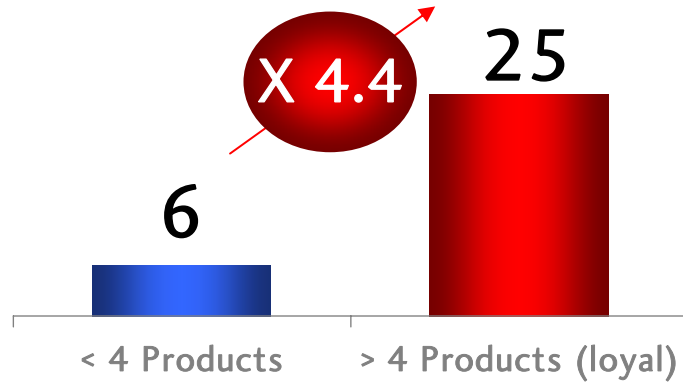
**+1 8% in customer deposits as of Dec 07**



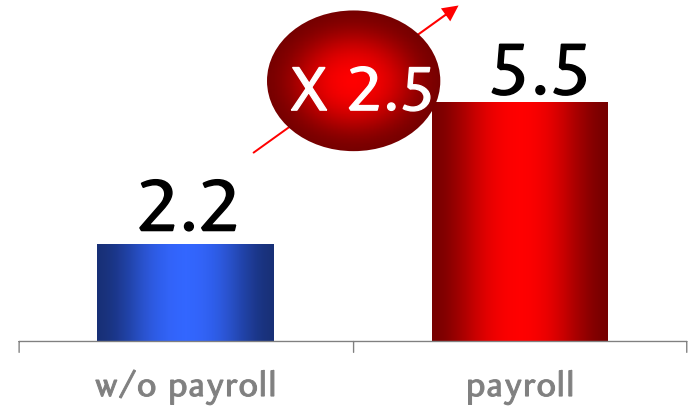
# 1.- Focus on customer funds (cont)

Successful **cross-selling** improves growth in customer funds

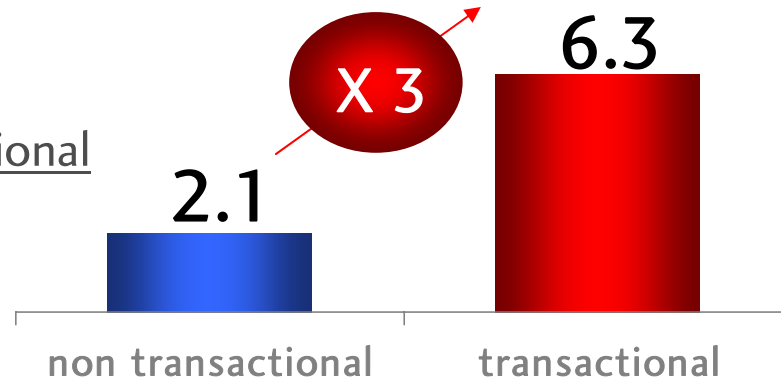
Customer funds in "loyal" customers (> 4 products)



Current account balances in payroll / non payroll customers



Current account balances in transactional vs non transactional customers

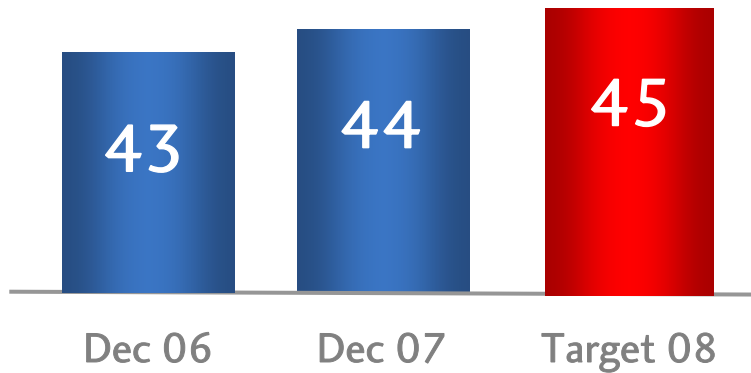


Average balances December  
EUR 000's per customer

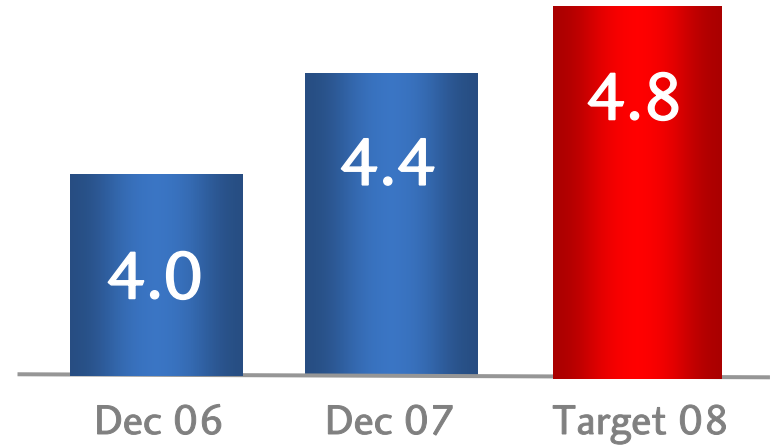
# 1.- Focus on customer funds (cont)

Greater share of our individual customers' business

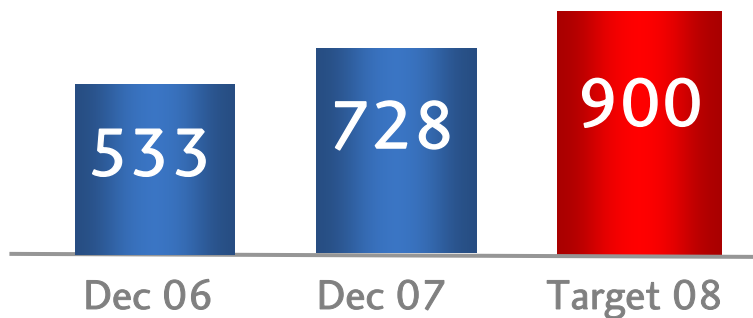
Customers > 4 products (%)



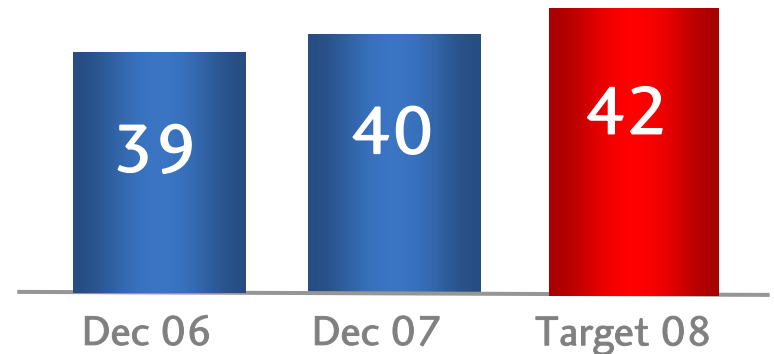
Products per customer



Flat-fee accounts (000s)



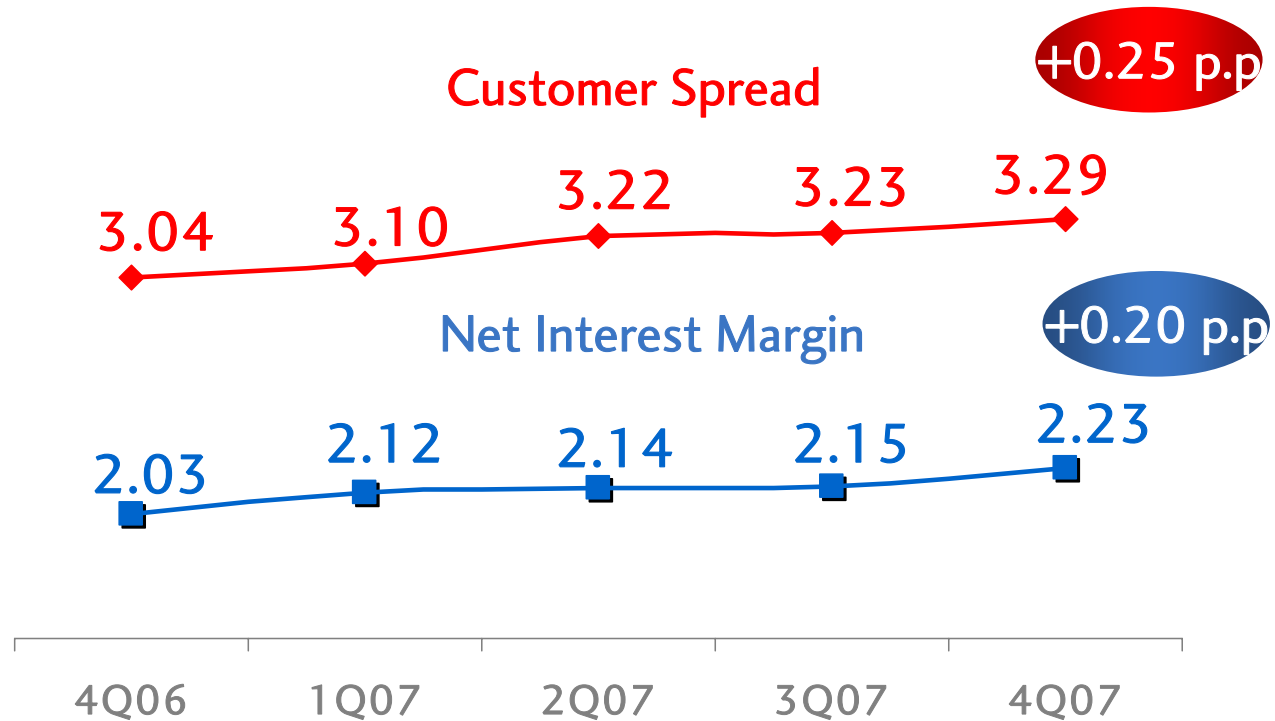
Payroll accounts (%)



# 2.- Customer spreads management

Actively managing customer spreads

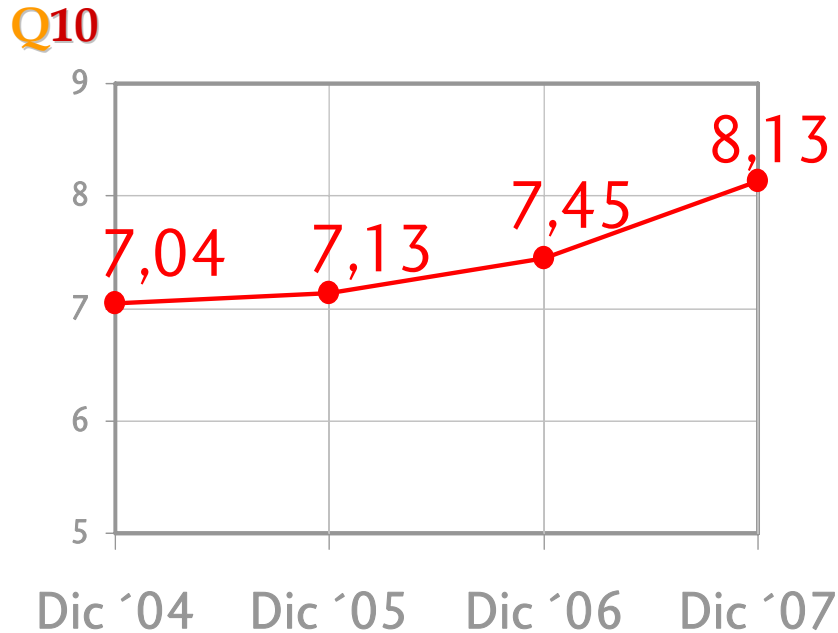
Customer spread (%)



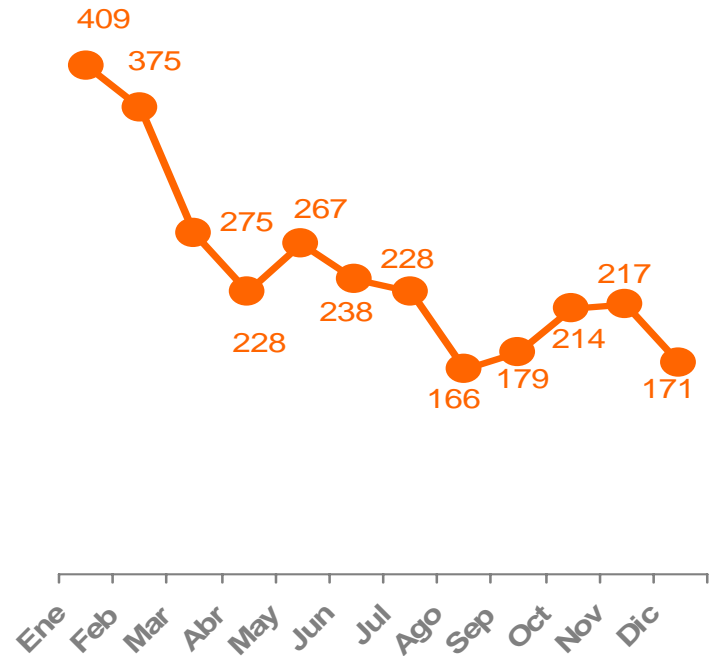
Net Interest Margin = Loans yield minus total cost of funds

### 3.- Personalized service

Customer value added is key for growth + profitability



Internal customer service index **Q10**  
2004-2007



Monthly customers' claims 2007

3 In the current environment we have room to improve

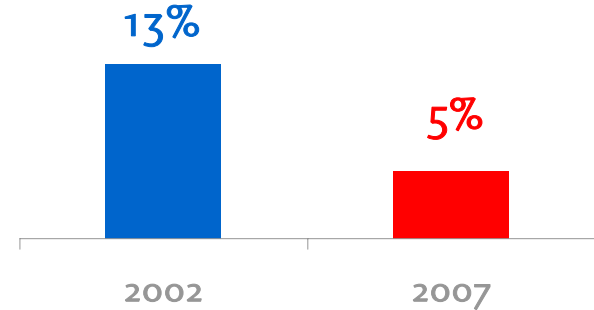
# 1.- Improvements in efficiency and productivity

Building a more productive commercial organization

- More **cost efficient**
- With a **flat structure**
- **Closer** to customers

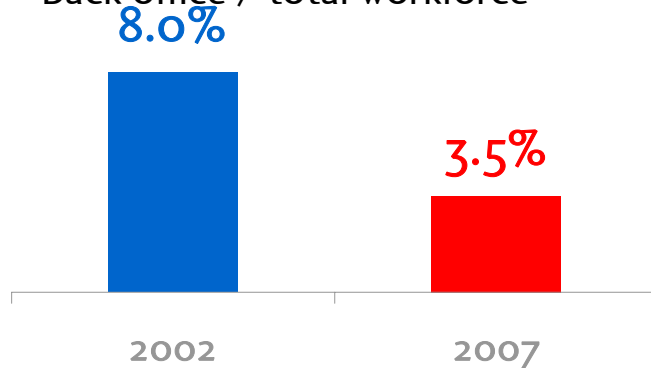
...and at intermediate levels...

Intermediate levels / total network



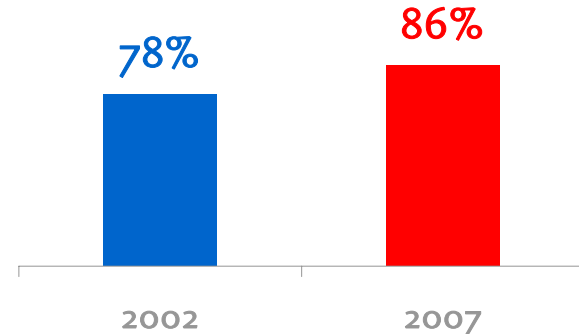
Improving efficiency in the back office...

Back office / total workforce



...while bolstering our sales force...

Sales force / total workforce



# 1.- Improvements in efficiency and productivity (cont)

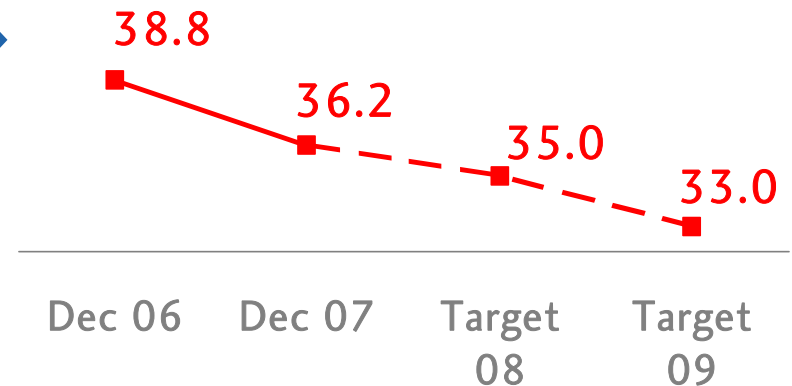
... but we can do it even better

## Menara plan

(Our 06-09 efficiency plan):

- Organizational improvements
- Processes reengineering
- Expanding low cost distribution channels

## Efficiency Cost/income(%)\*



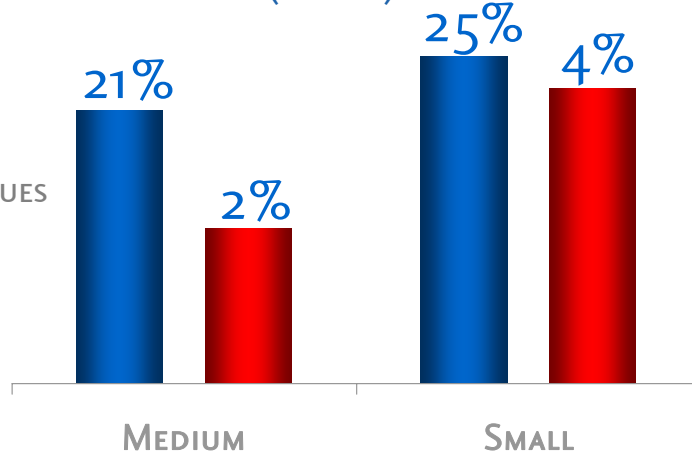
\* Ratio does not include amortizations. Cost/Income including amortizations in 2007 was 40.5%.

# 2.- Improvements in SME segment

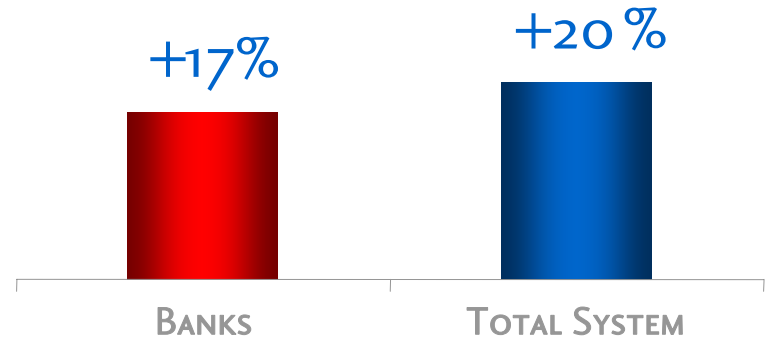
A dynamic and profitable segment...

Outstanding returns...  
(2007)

■ ROE  
■ GROSS REVENUES / EAD



...in a growing market  
(loans to companies 2007)

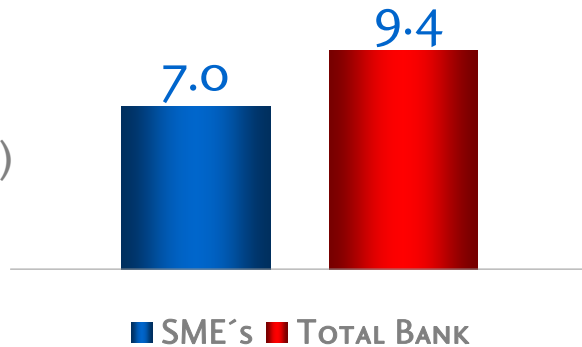


...with room for market share growth

Our strengths

**Focus...** which allows us to have  
 ... highly **specialized teams**, to offer the  
 ... best **personalized service**, and  
 ... **value-added** innovation, thanks to  
 ... strong product and **technology**  
 support

MARKET SHARE (%)  
(2007)



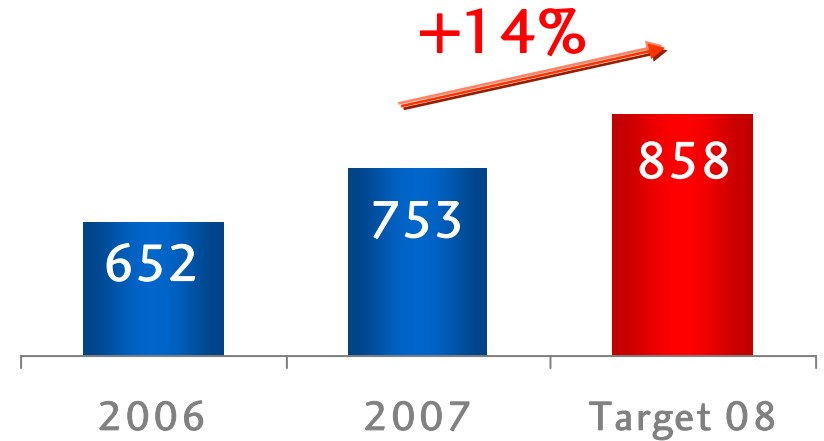
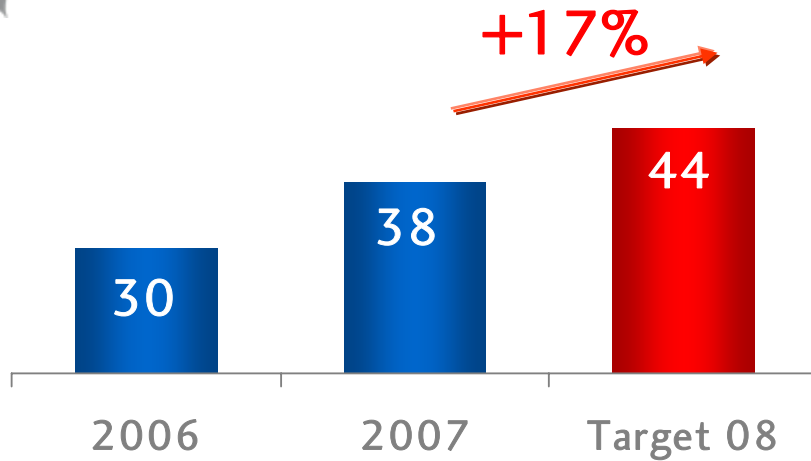


## 2.- Improvements in SME segment (cont)

...in which we are closing the gap

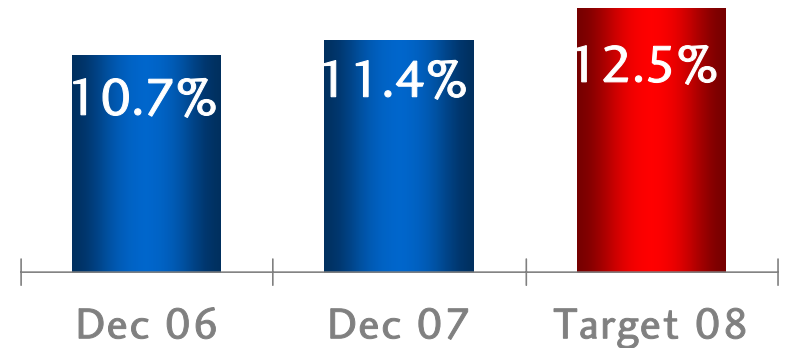
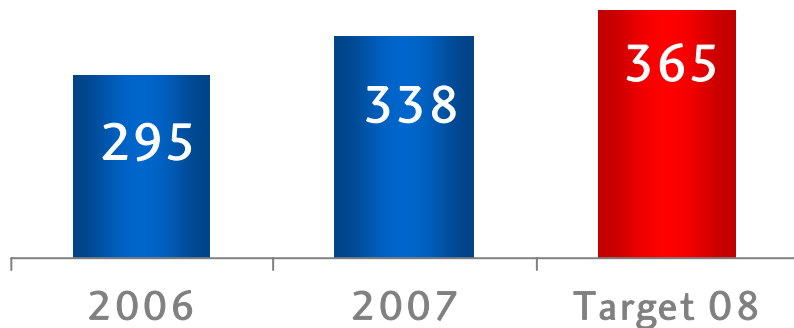
Business volume (€bn)

Gross operating income (€mn)



Customers (000's)

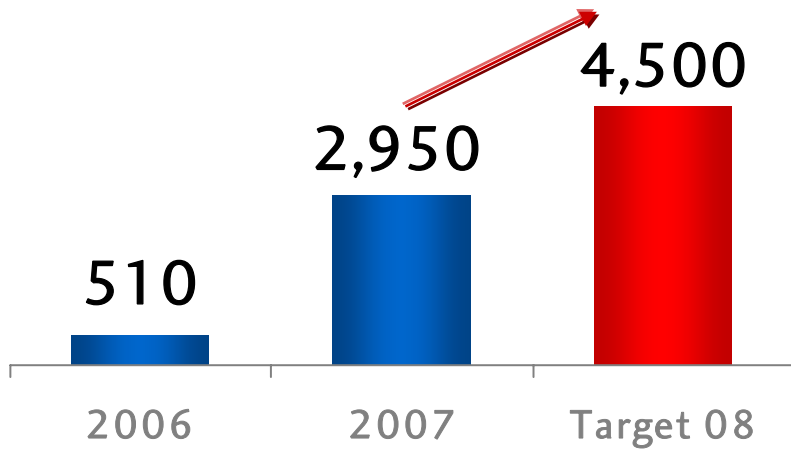
Medium size Co's:  
% market share of customer risk assets



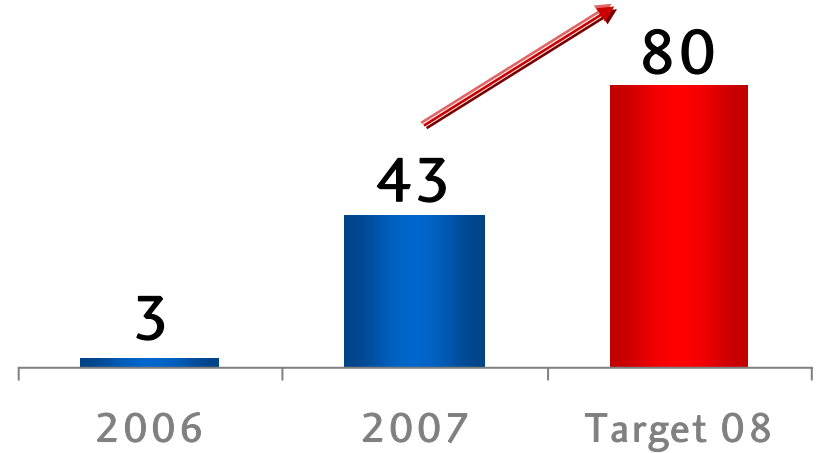
# 3.- Improvements in the branch network

New branches set to deliver higher revenues

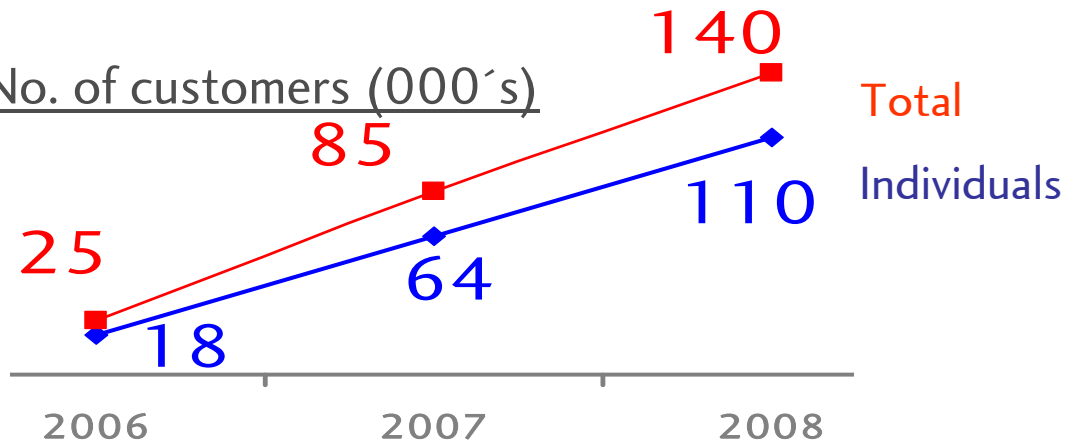
Business volume (€mn)



Gross operating income (€mn)



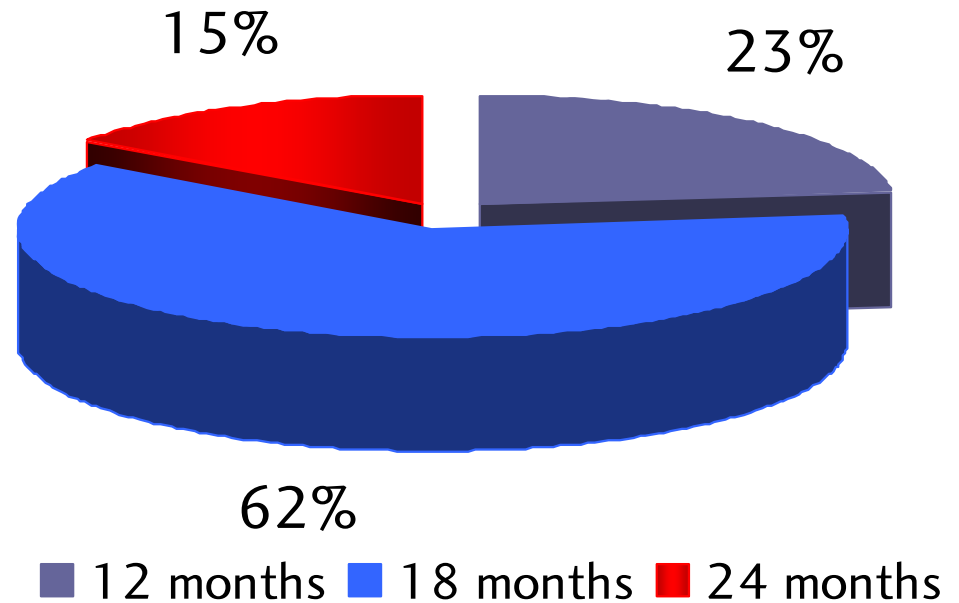
No. of customers (000's)



### 3.- Improvements in the branch network (cont)

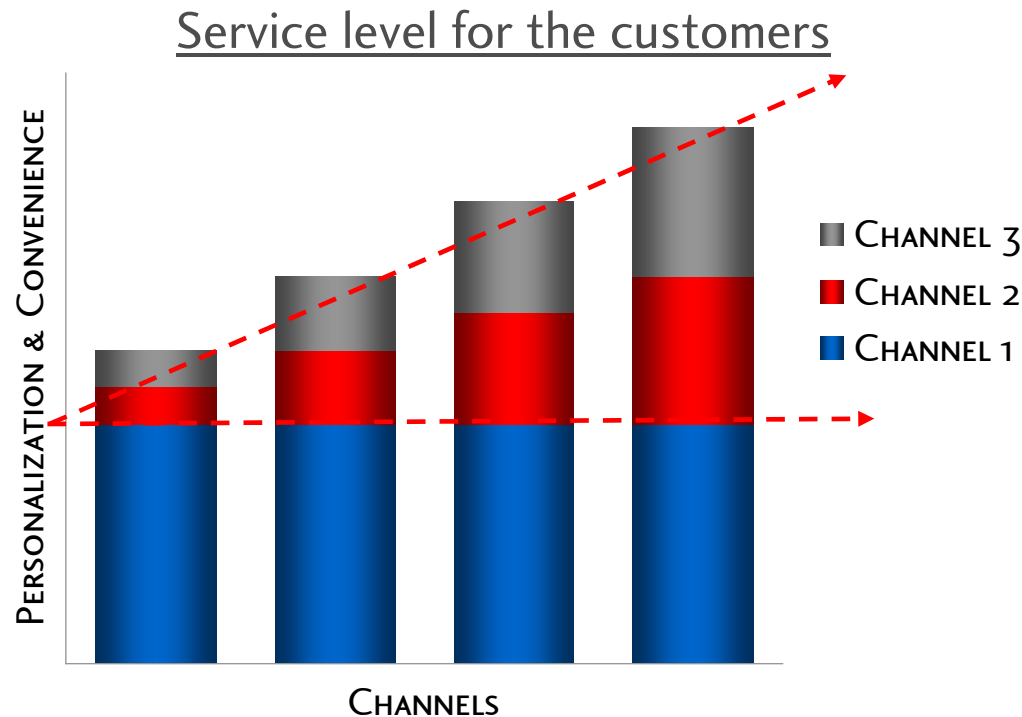
...reaching **break-even earlier** than expected

85% of new branches will reach break-even in < 18 months



## 4.- Improvements in distribution capacity

Banesto aims at increasing **global customer service** levels through a **multichannel** strategy whilst growing sales in a **cost efficient** way



- Higher service level = Higher loyalty
- More cost efficient selling opportunities
- Free time in Branches to focus on sales

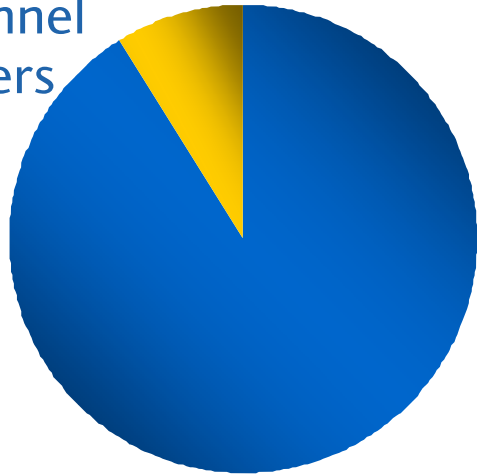
## 4.- Improvements in distribution capacity *(cont)*

Banesto

### %Multichannel customers

2007

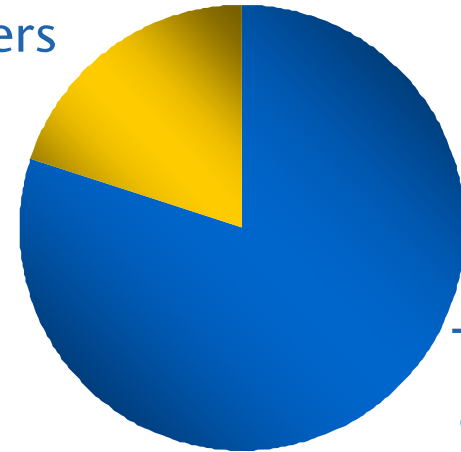
Multichannel  
customers  
9%



Traditional  
customers  
91%

2010

Multichannel  
customers  
20%



Traditional  
customers  
80%

### Objectives

- Maximize customer growth potential
- New customer acquisition through remote channels
- Improve customer satisfaction and loyalty

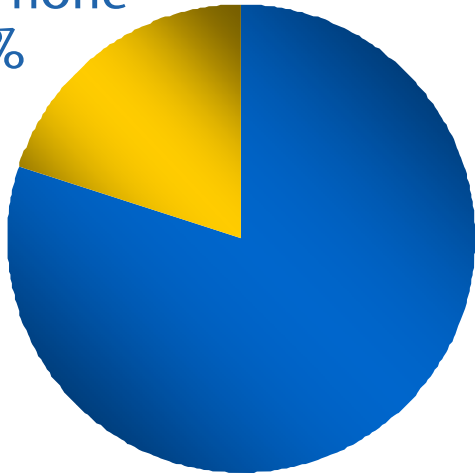
## 4.- Improvements in distribution capacity *(cont)*

Banesto

% Transactions

2007

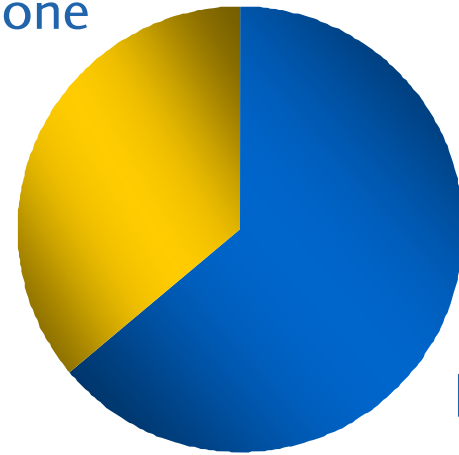
Web + Phone  
20%



Branches  
80%

2010

Web + Phone  
36%



Branches  
64%

### Objectives

- Increase customer transactions through remote channels
- Increase the number of transactional customers
- Support sales through traditional channels

## 4 Conclusions

Banesto is well prepared to outperform its peers in the new tougher environment:

- **Clear vision and strategy:** proven execution
- **A customer focused** business model
- **Diversified and balanced** sources of revenues
- **Low-cost producer**
- **Conservative risk** management culture



*Banesto*

Morgan Stanley

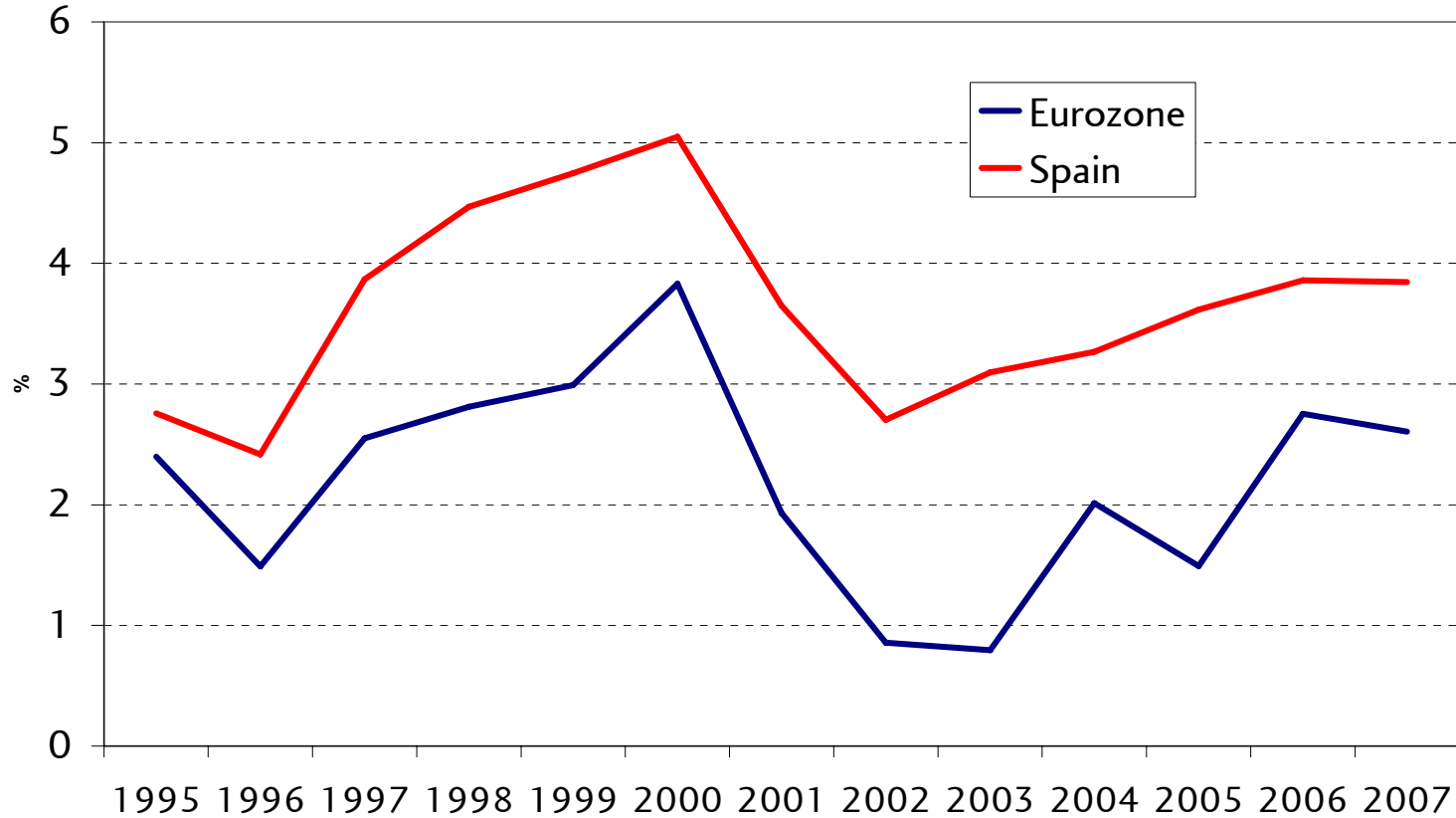
April 1<sup>st</sup>, 2008

*Addendum:* Economic  
environment

# Economic environment

The Spanish GDP has consistently outgrown the Eurozone ...

GDP growth : Spain vs. Eurozone

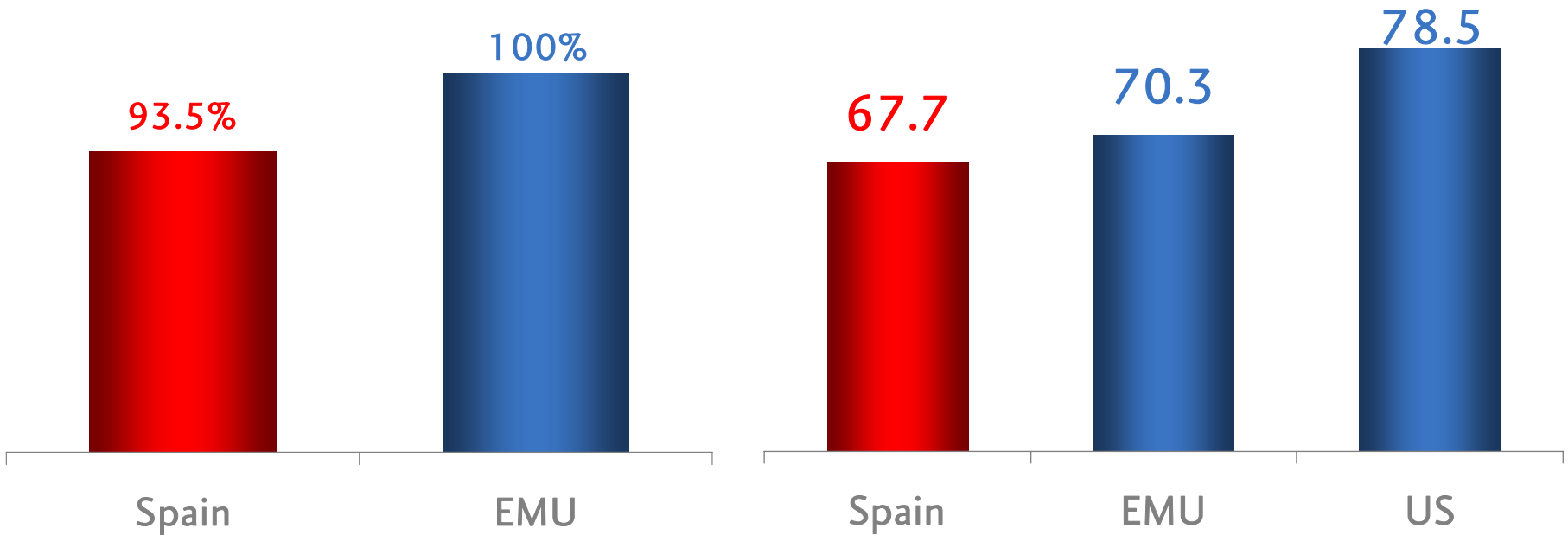


# Economic environment

... and there is still a GAP with European and US economies in services

GDP per capita

Services %/GAV 2006



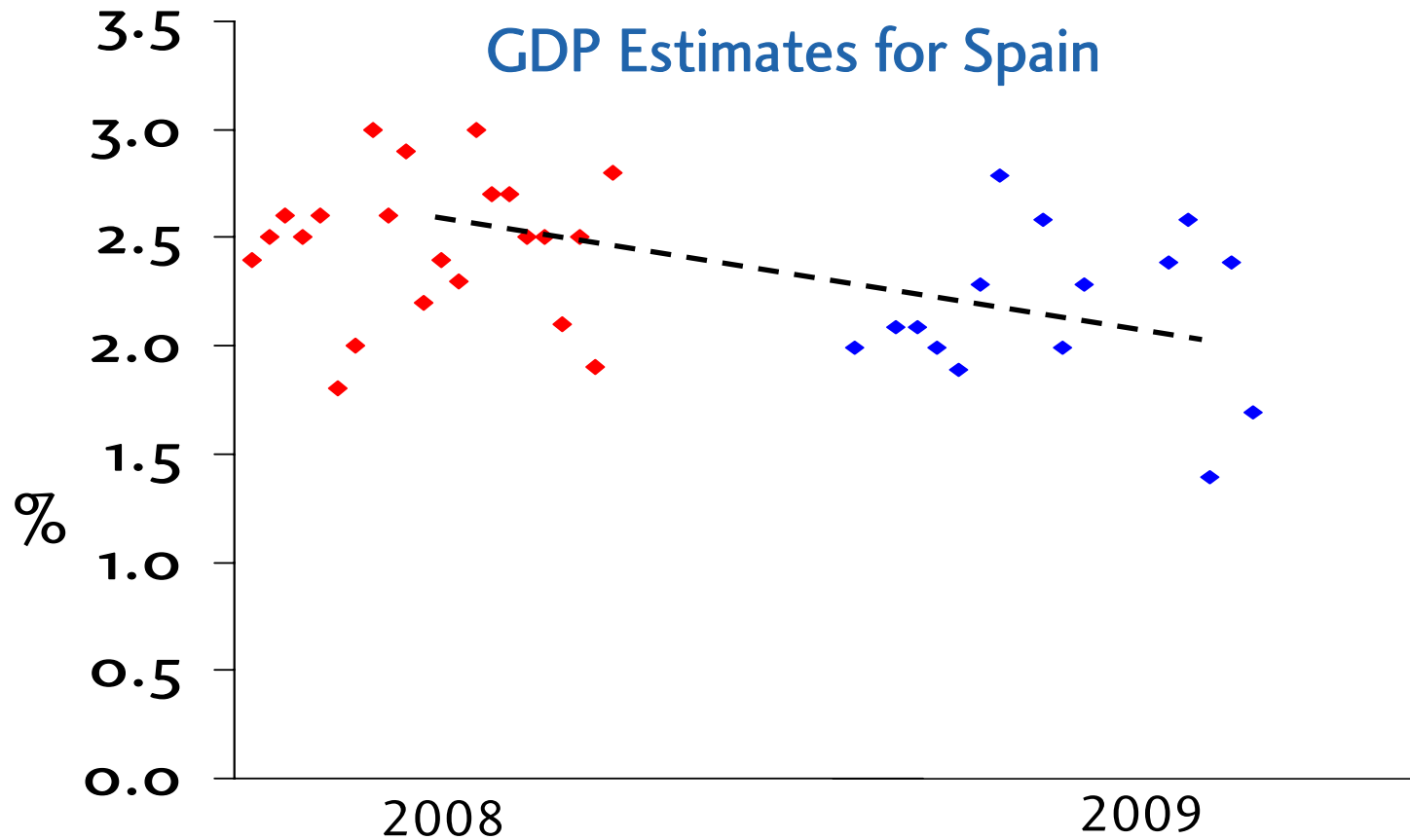
Source : Bank of Spain Purchase Power Parity as of 2007  
Gross added value at cost

# Economic environment

The Spanish economy today is in better shape than in 1990

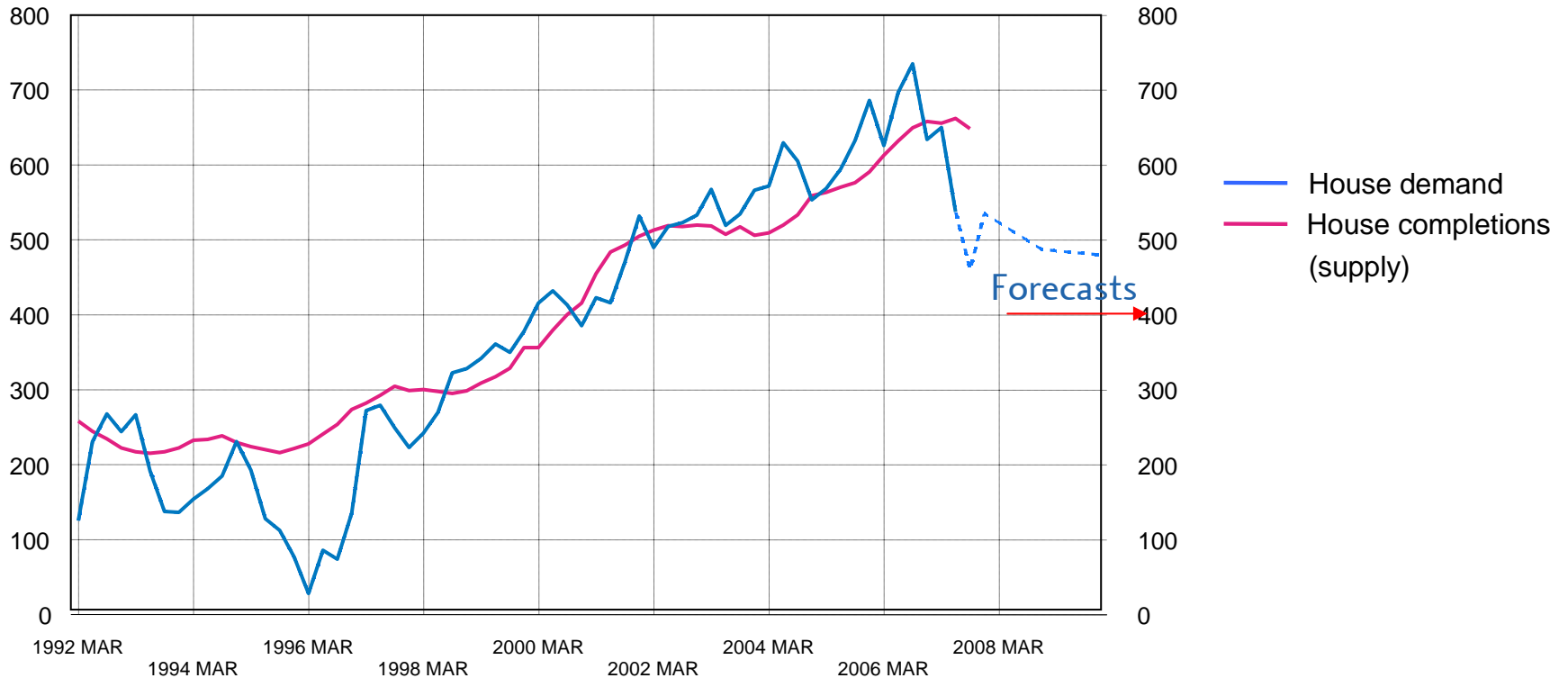
	<u>1990</u>	<u>2007</u>
CPI (avg. chg)	6.7	2.8
Unemployment (%)	13.0	8.1
> 2Y Unemployment (%)	36	12
Interest rates	14.7	4.0
Public sector surplus (% GDP)	-3.9	2.2

GDP growth estimates predict lower growth,  
but not a recession



Despite slowdown in real estate, there is still a significant projected structural demand for housing

## House demand vs. house completions (thousands)



# Economic environment

Slowdown in residential construction, not in non-residential  
Large construction companies are widely diversified

- Construction contribution to GDP: 9.8% in Gross Added Value
- 52% of construction is Residential
- 48% of construction is Non Residential

% EBITDA LARGE CONSTRUCTION COMPANIES

