
Banco Popular acquisition

Creating shareholder value through in-market consolidation

Sencillo | Personal | Justo



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Banco Popular acquisition

Creating shareholder value through in-market consolidation

1

**Overview
strategic and
financial
rationale**

2

**Popular
acquisition:
in-depth
review**

3

Rights offering

4

**Concluding
remarks**

Strong strategic rationale

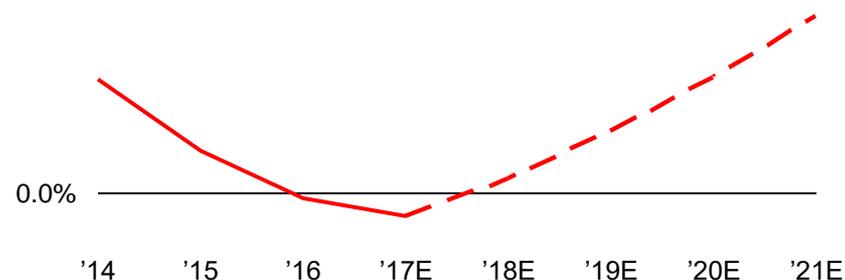
Creating the leading retail and commercial bank in Spain and Portugal

Add-on acquisition in Iberia...

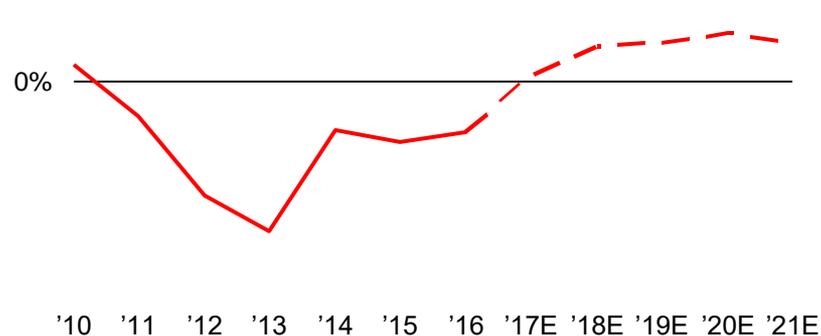
Spain	Portugal
<p>c.6-7% market share</p> <ul style="list-style-type: none"> • 1,644¹ branches • c.4.1m total customers • Cust. Loans²: 89Bn€ • Cust. Funds: 89Bn€ 	<p>c.2% market share</p> <ul style="list-style-type: none"> • 118 branches • c.320k total customers • Cust. Loans²: 6.4Bn€ • Cust. Funds: 5.7Bn€

... at the right point of the cycle

Euribor 12 months (%)



Total Sector Loan Growth (%)



Source: Bank of Spain and Economist Intelligence Unit



**Leading bank
in Spain**

*c.20% loans
market share*



**Leading bank
in Portugal**

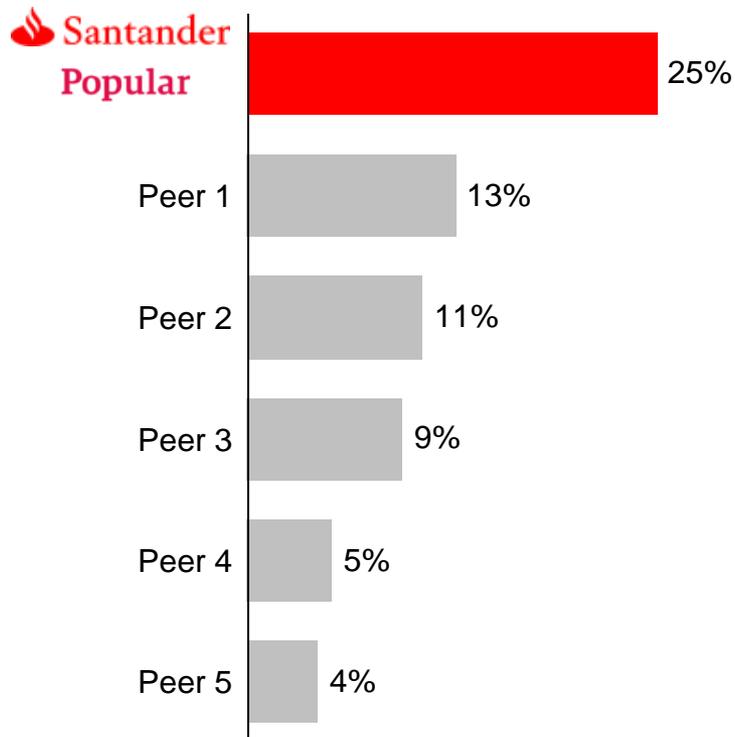
*c.17% loans
market share*

Strong strategic rationale

Complementary franchises

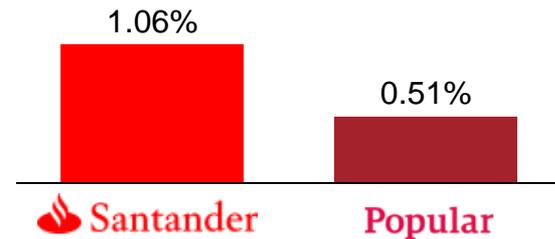
Leading SME franchise

SME Market share in Spain (%)

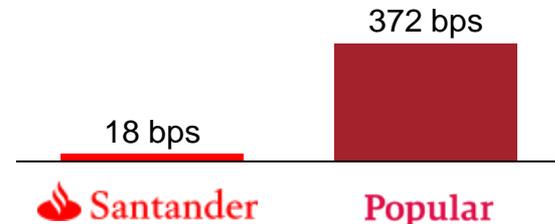


Potential to improve acquired business...

... deepening customer relationships
Fees / Loans (% , 2016)



... through wholesale funding synergies
3-year Senior debt (m/s + spread)¹



¹ Trading level as of May, 2017 Source: Bloomberg

In-market consolidation

Leveraging economies of scale with manageable execution risks

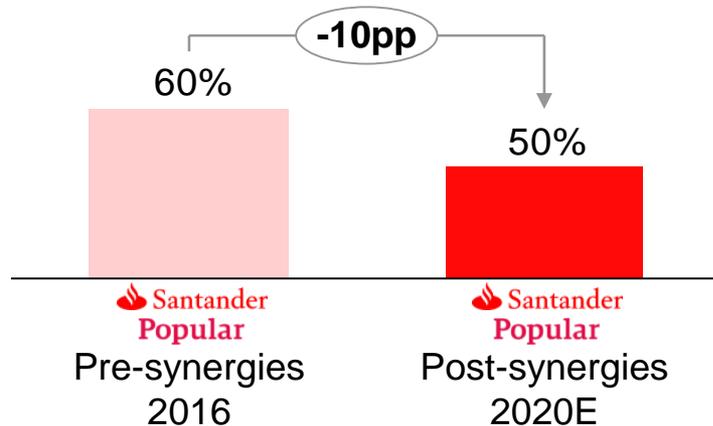
Synergies for best-in-class efficiency

Expected annual cost savings in 2020 pre tax:

EUR c.500m

(c.10% of 2017 combined cost base)

Cost to income



Focus on preserving franchise value



Proven integration track record limiting potential revenue attrition



Sharing of Best Practices and Know-How



Focus on preserving Popular core strengths in retail and SMEs banking

Real estate

Additional provisioning to execute a quick unwind

RE well provisioned after adjustments

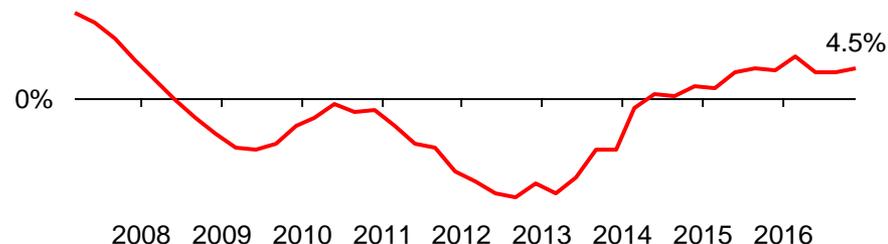
- **€7.2Bn additional provisions** for Real Estate exposure, **achieving coverage well over peers average**

EUR Bn	Addit. provision	Final net value	% coverage	Peers avg.
Total RE	4.7	6.2	65%	52%
- o/w land	2.7	1.2	85%	63%
RE NPLs	2.5	3.0	76%	51%
RE assets + RE NPLs	7.2	9.2	69%	52%

Roadmap for a quick RE unwind

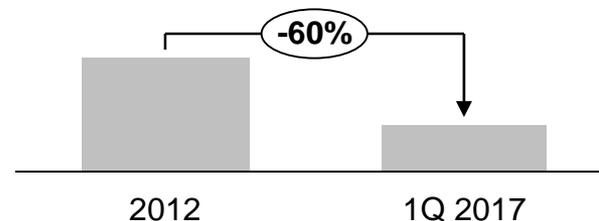
- **Plan in place to reduce Banco Popular RE Assets and RE NPLs to non-material levels in 3 years**

House price change (%)



- **SAN's strong track record in NPA management**

Santander "Real Estate activity in Spain"¹

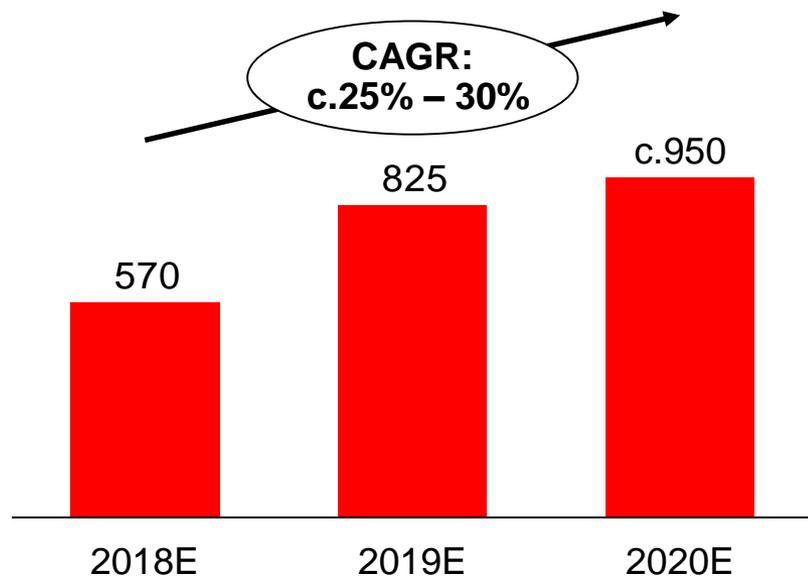


Creating shareholder value

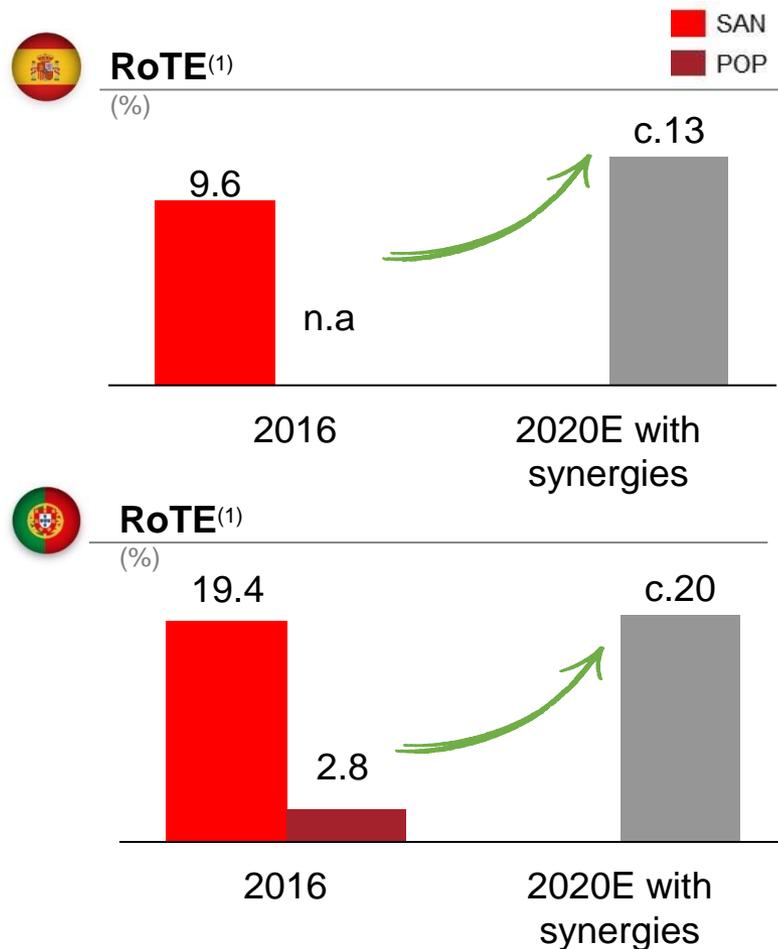
Improving profitability of Spain and Portugal franchise

Enhanced earnings growth profile

Banco Popular Net income targets w/ synergies (m€)



Improving franchises target profitability



Creating shareholder value

Transaction at attractive financial terms to continue delivering on our commitments

Price Paid	€1 for 100% of the capital
Rights offering	7Bn€
Target RoI year 3	13 – 14% <i>already above Cost of Equity in 2019</i>
Target EPS accretion	2019: c.2% 2020: c.3%
Target TNAVPS accretion	2018: c.3%
CET1 FL	Neutral / Slightly positive

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Concluding
remarks

Why are we acquiring Banco Popular?

1. Popular: unique domestic consolidation opportunity in Spain and Portugal

2. Strong strategic / business fit at an attractive point in the cycle

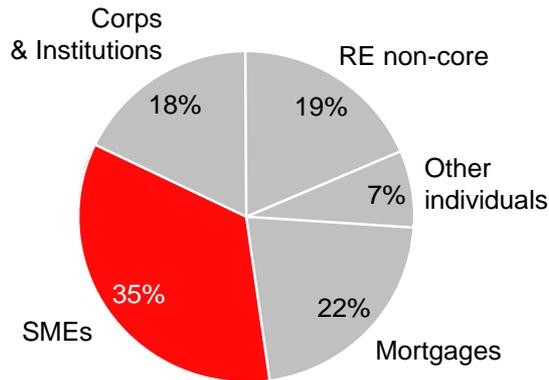
3. Significant cost synergies, real estate assets well provisioned with manageable execution risks

4. Attractive financials (targeting RoI 13-14% and EPS accretive in year 2), enhancing KPIs for Group, Spain and Portugal

Popular: unique domestic consolidation opportunity in Spain and Portugal

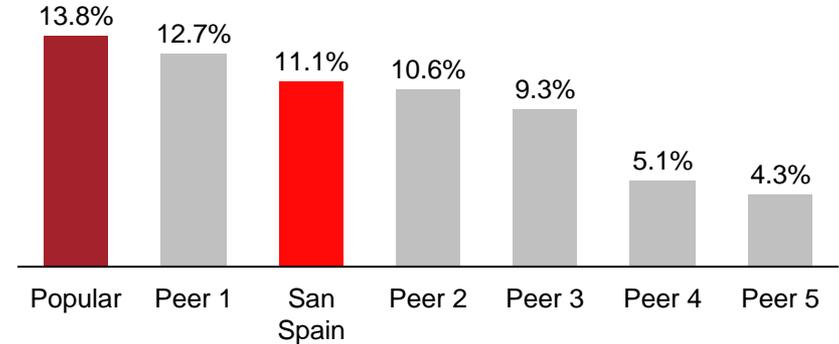
Gross Loans excl. Repos Breakdown

(2016, %)

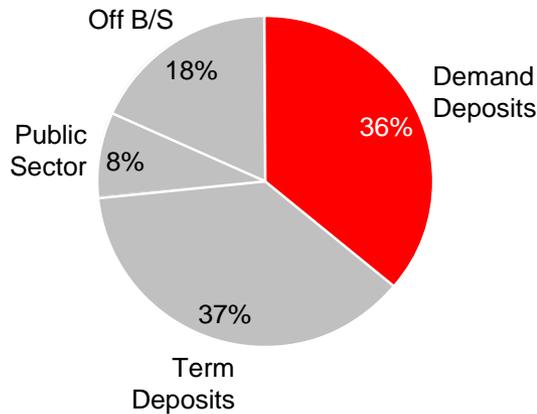


Total Group gross loans:
97.6Bn€

Leader in SMEs in Spanish market⁽¹⁾

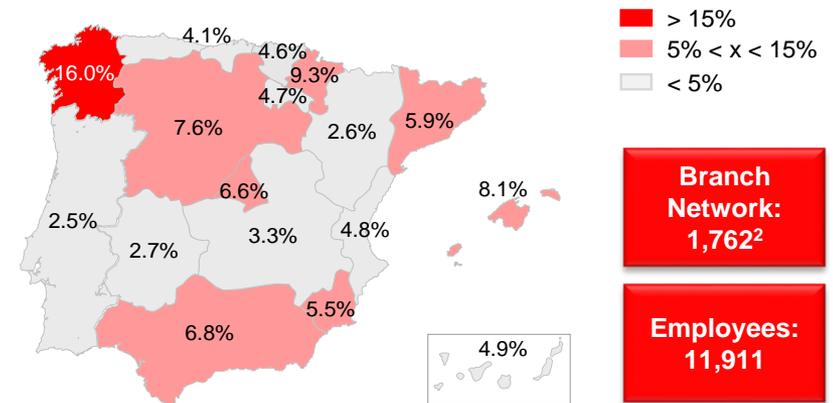


Customer Funds (2016, %)



Total Group customer funds:
96.6Bn€

Branches market share of 6% in Spain and 2.5% in Portugal



(1) SME loans market share as of dic 2015 estimated according to each entity Annual report
(2) Spain and Portugal

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Strong strategic / business fit at an attractive point in the cycle

A

Acquisition in a core market

- Creating the leading bank in Spain with loans market share of c.20%
- A nationwide branch network with heavier weight in the wealthier regions
- Diversifying Santander Spain loan portfolio while maintaining Group's geographic diversification
- Santander Totta: reinforcing our leadership in Portugal

B

Leading SME franchise

- Santander to become the leading player in SMEs with c.25% market share
- Profitable and stable business over the cycle

C

Opportunity to improve combined franchise

- Development of deeper customer relationship
- Wholesale Funding Cost reduction

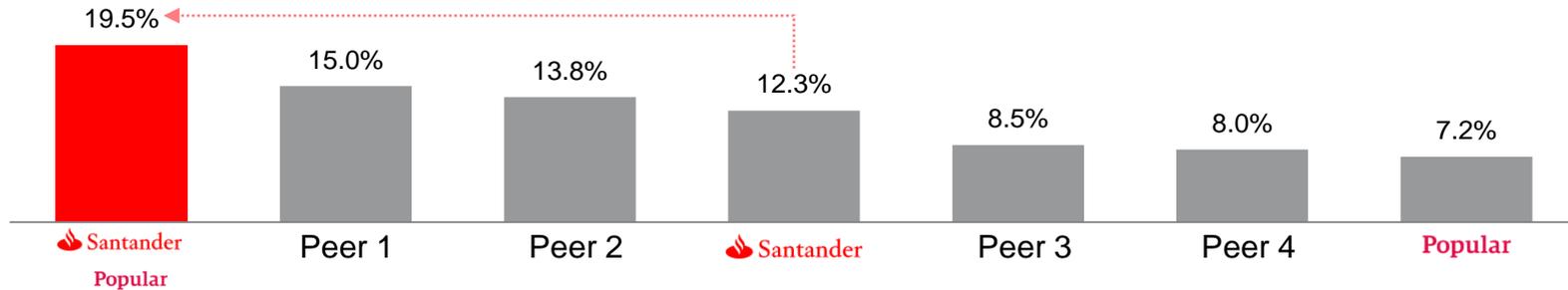
D

An attractive point in the cycle

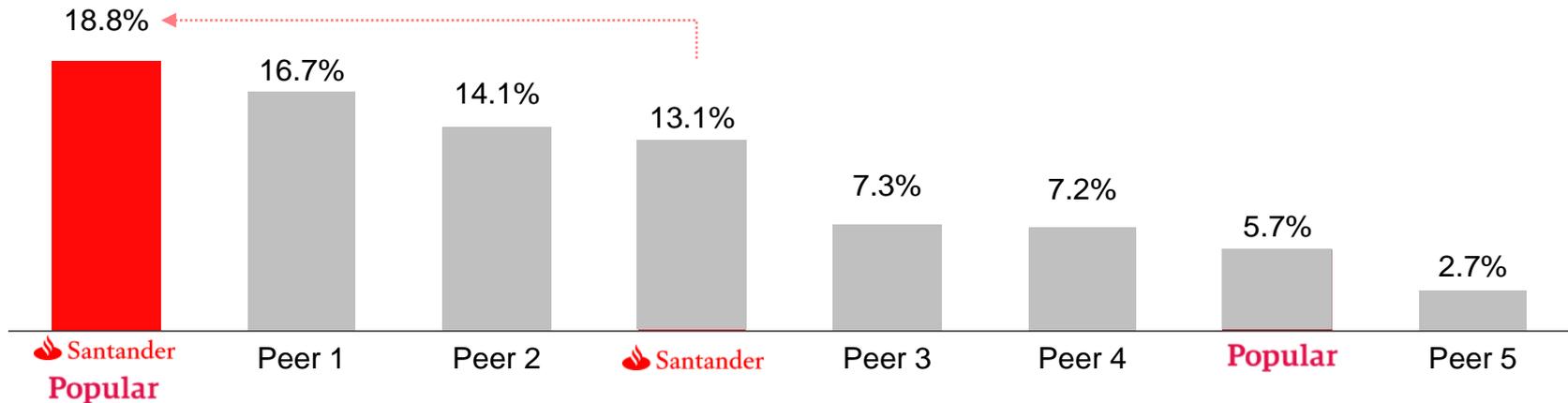
A Acquisition in a core market

Creating the leading bank in Spain: c.20% market share

Loans Market share (%)



Customer funds Market share (%)

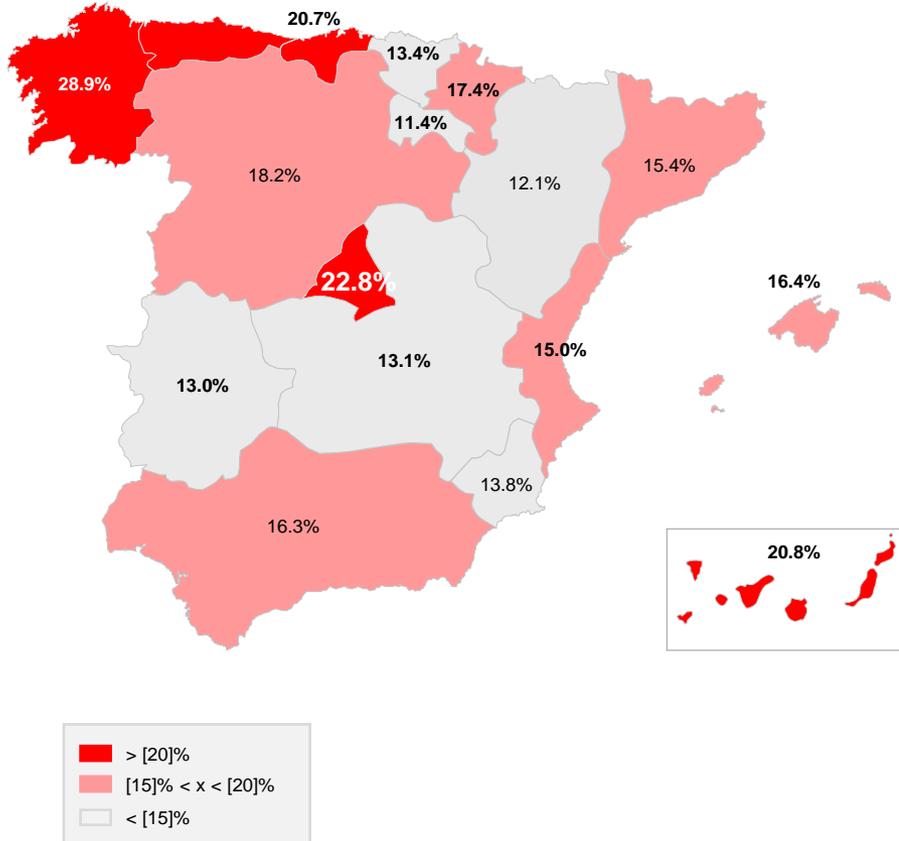


Note: Data for Santander refers to all domestic business. Source: Estimates based on companies disclosure as of 2016, Bank of Spain

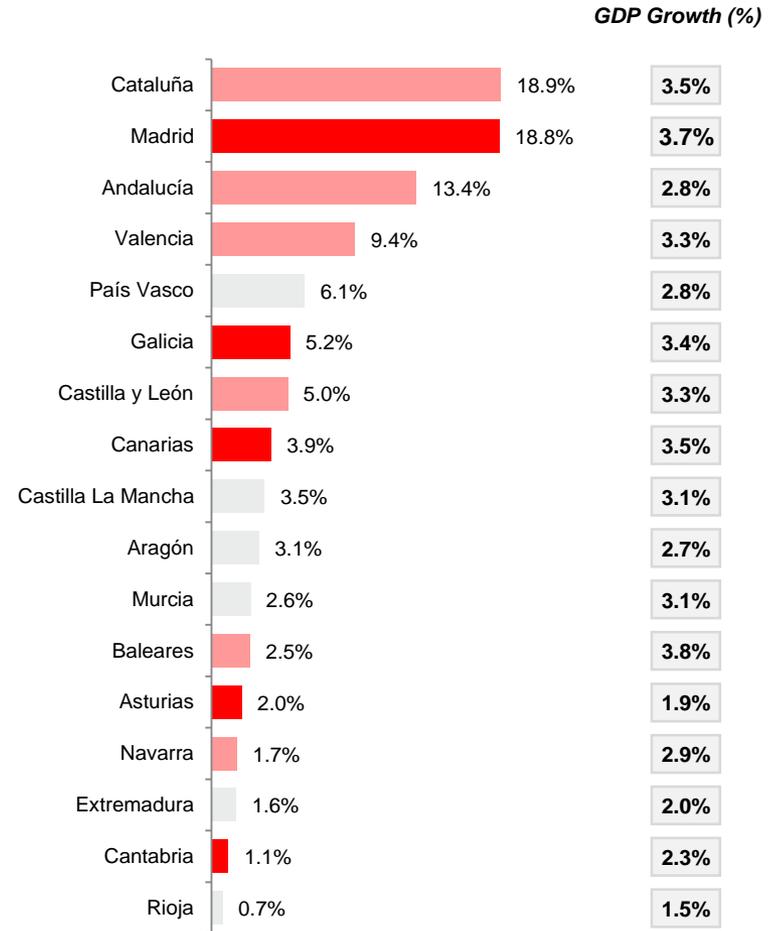
A Acquisition in a core market

A nationwide branch network with heavier weight in the wealthier regions

Post transaction branch market share



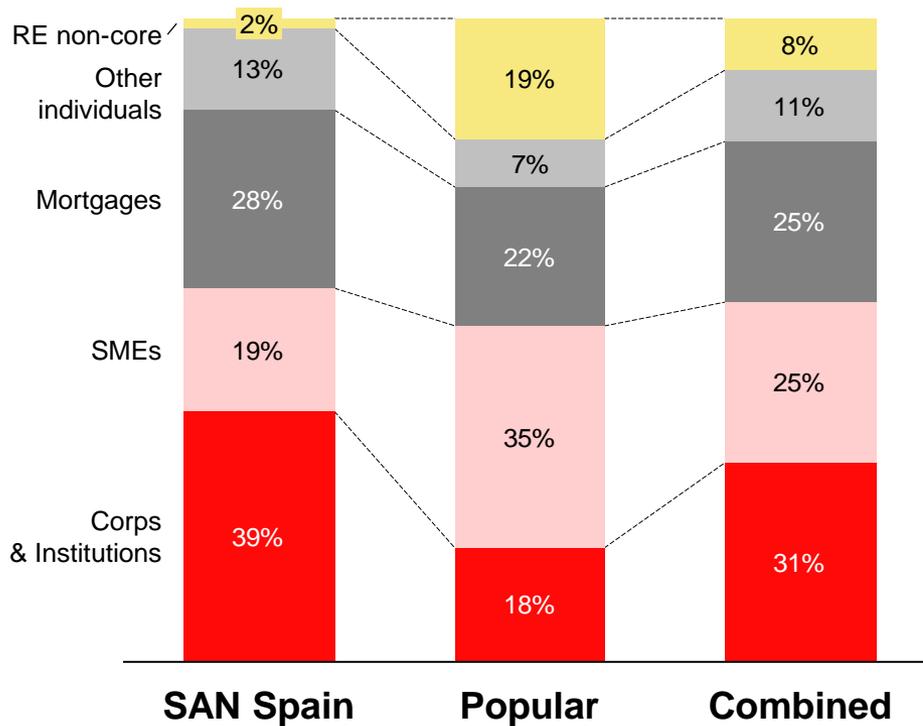
GDP contribution per region (%)



A Acquisition in a core market

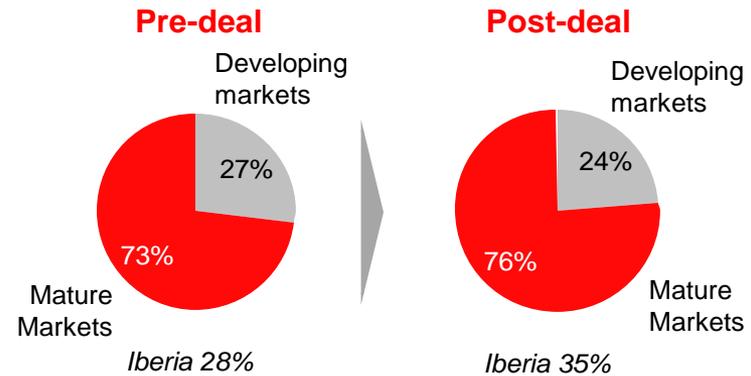
Diversifying Santander Spain Loan Portfolio while maintaining Group Geographic diversification

Loan portfolio breakdown (2016)

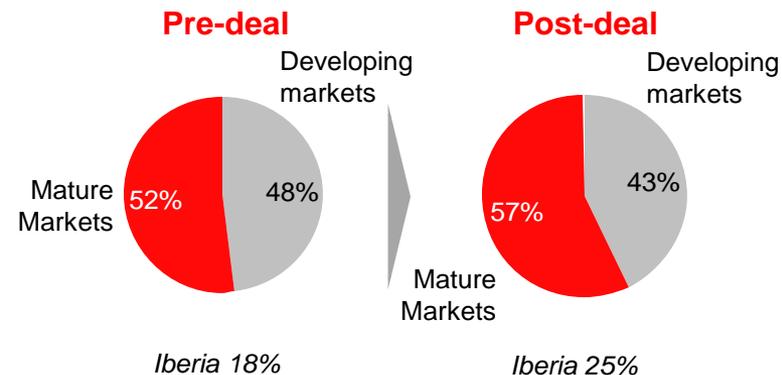


Group geographic diversification

Asset distribution



Attrib. income distribution (1Q 2017¹)



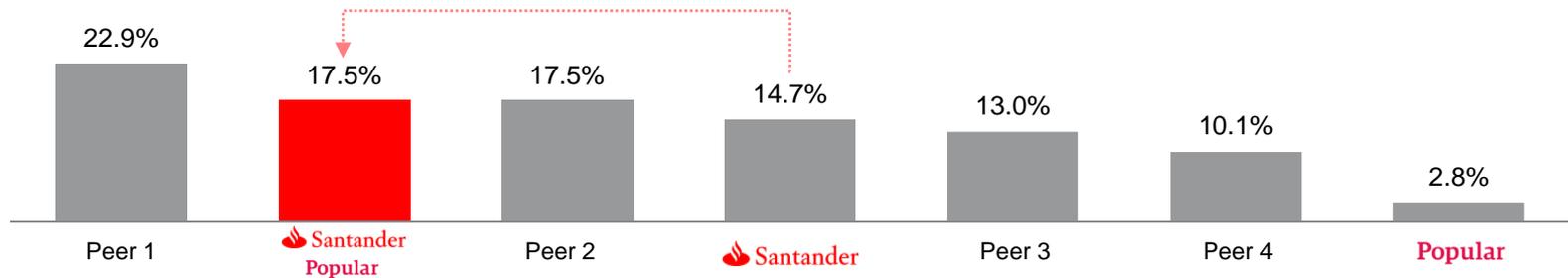
(1) Santander Operating Areas attributable income as of 1Q 2017 annualized.

Note: Mature markets include Spain, UK, US, SCF and Portugal. Emerging markets include Poland and LatAm. Estimated Net Income for Banco Popular after synergies.

A Acquisition in a core market

Santander Totta: reinforcing our leadership in Portugal

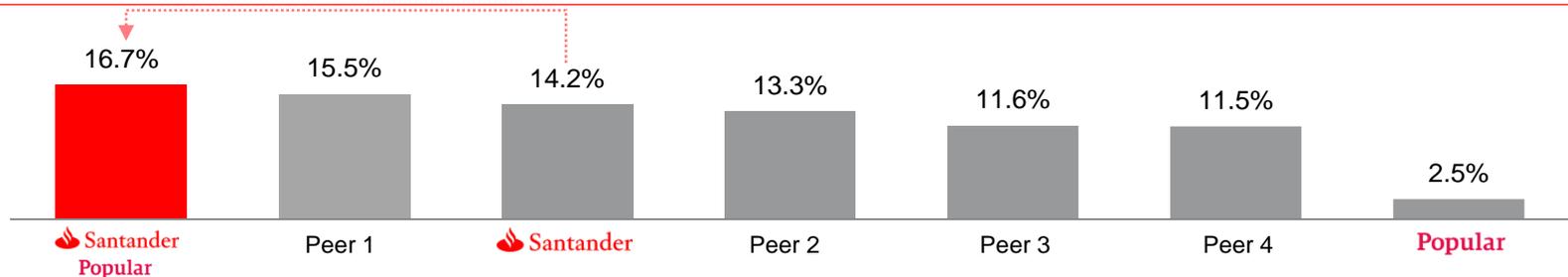
Loans market share (%)



Deposits market share (%)



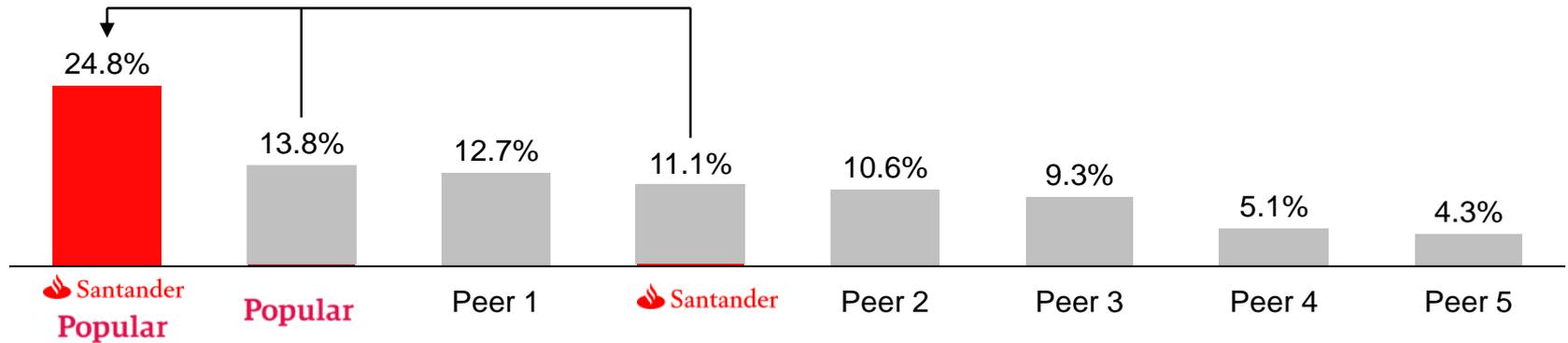
Branches market share(%)



Source: Estimates based on companies disclosure as of 2016, Bank of Portugal

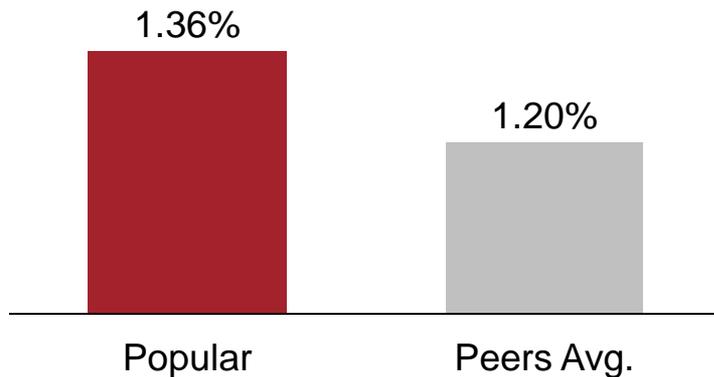
B Leading SME franchise

Strong market share in SMEs



That results in higher NIM

2016



SME franchise with scale

SMEs
customers
c.620k

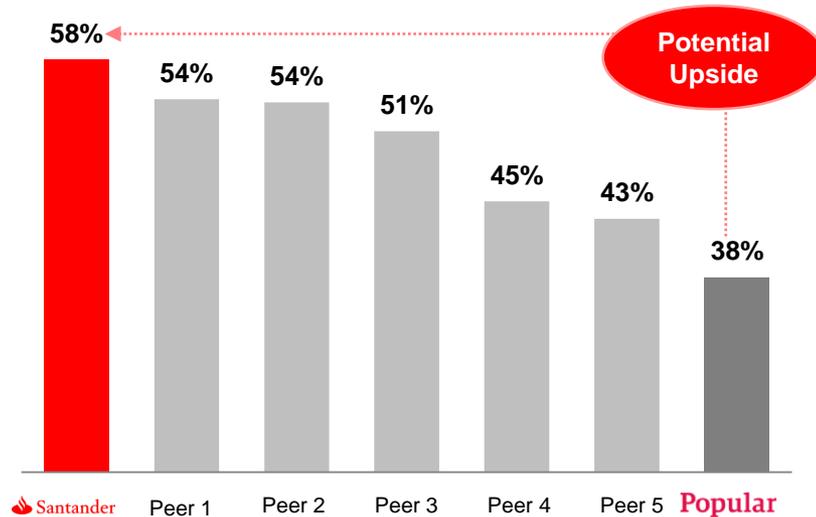
c.920 SMEs
& Corps
specialized
managers

C Opportunity to improve the combined franchise

Development of deeper customer relationships

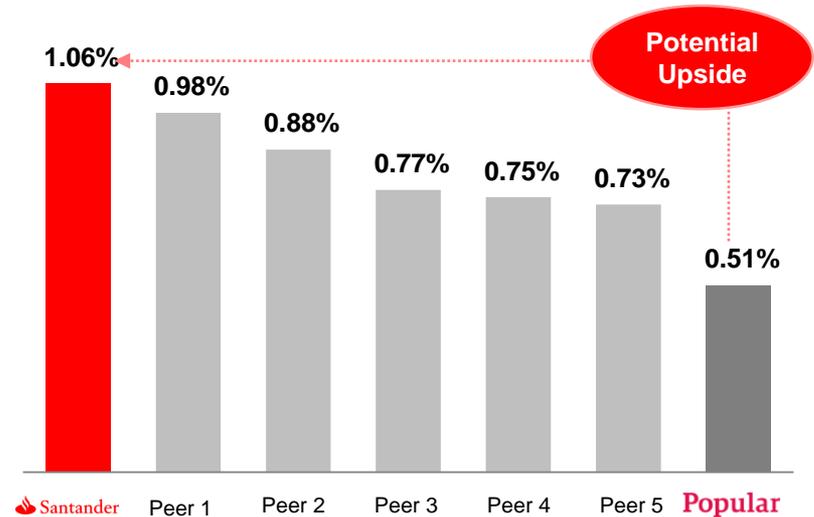
Recurrence Ratio (%)

(1Q 2017, % of Net Fees over Total Operating Expenses)



Fees over Loans (%)

(2016, % of Net Fees over Average Loans)



SMEs:

- Credit driven relationships
- Potential to selling products (FX, comex, renting, Factoring...)

Individuals:

- Second bank relationship
- Low penetration in active customers of other products; funds, insurance, cards (20-30% penetration)

Potential additional revenues: EUR 100-200 m (not included in our estimates)

C Opportunity to improve the combined franchise Wholesale Funding Cost Reduction

	 Santander	Popular	
FitchRatings	A- / F2 (Stable)	B / B (Negative)	
MOODY'S	A3 / P-2 (Stable)	B2 / NP (Negative)	
STANDARD & POOR'S RATINGS SERVICES	A- / A-2 (Positive)	B / B (Negative)	

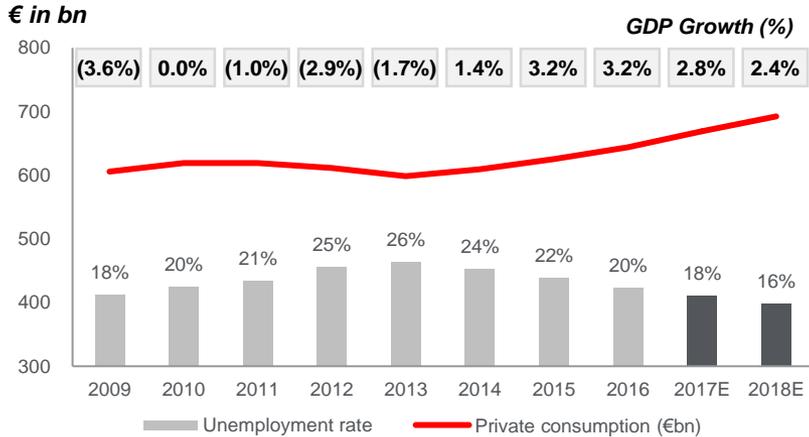
	 Santander <u>m/s + Spread</u>	Popular <u>m/s + Spread</u>	<u>Volume</u>
3-year Senior Debt	+18bps ⁽¹⁾	+372bps ⁽¹⁾	1Bn€
Covered Bonds			
Maturing in:			
2018	(10.7bps) ⁽¹⁾	+11bps ⁽¹⁾	12Bn€
2020	(13.4bps) ⁽¹⁾	+40.6bps ⁽¹⁾	
AT1	+ 511 - 561bps ⁽¹⁾ (Coupon: 6 ^{1/4} - 6 ^{3/4})	+1,982 - 2,726bps ⁽¹⁾ (Coupon: 8 ^{1/4} - 11 ^{1/2})	1.25Bn€
Tier 2	+157 - 168bps ⁽¹⁾ (Coupon: 2.5 - 3.25%)	+930bps ⁽¹⁾ (Coupon: 6.873%)	0.72Bn€

Additional TLAC issuance cost offset by wholesale funding cost synergies

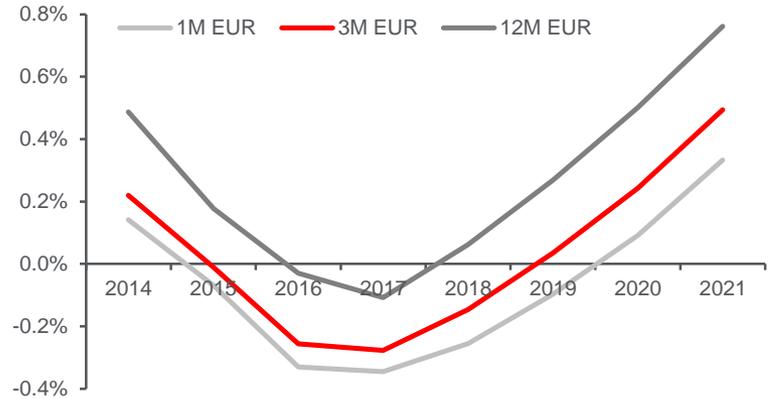
D An attractive point in the cycle

The Spanish market faces a positive banking cycle

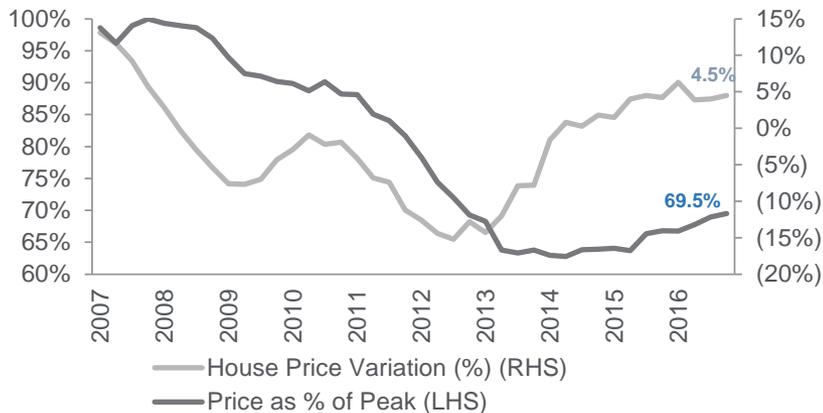
Key drivers improving with further upside



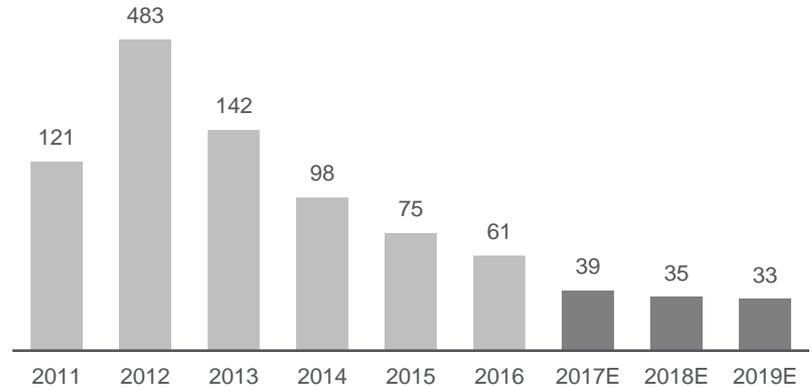
Low interest rate environment



House price Evolution



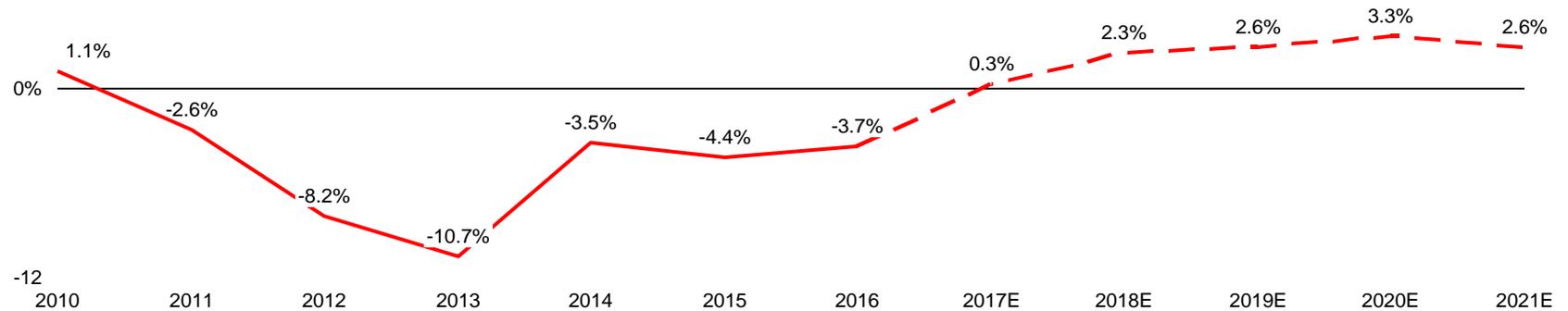
Cost of risk evolution (bps)



D An attractive point in the cycle

Business growth supported by private consumption and RE sector trends

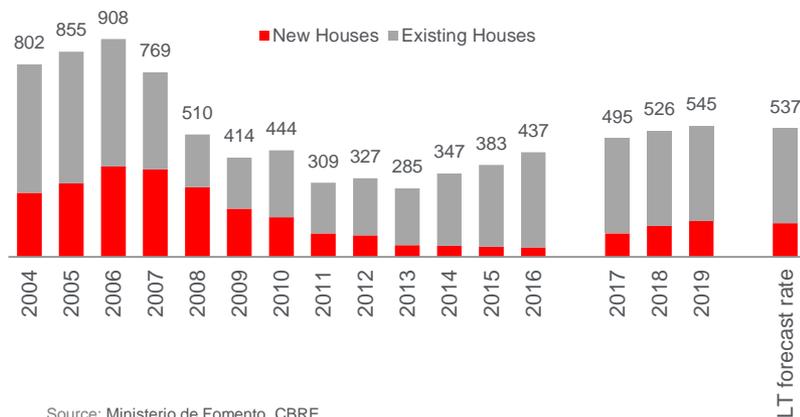
Total Sector Loan Growth (%)



Source: Bank of Spain, EIU.

Robust Sector Trends

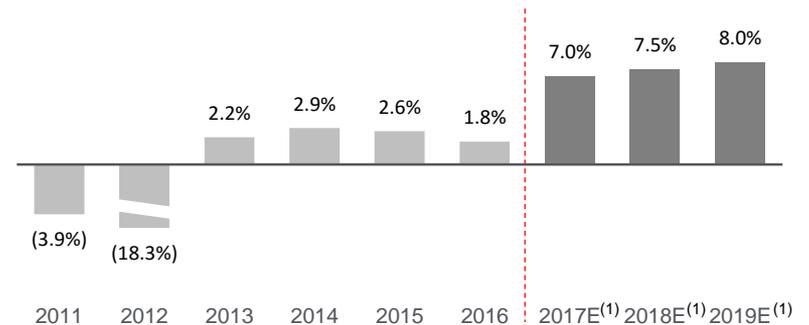
Overall Home Sales in Spain Growing since Early 2014
Units of Houses ('000)



Source: Ministerio de Fomento, CBRE.

Earnings Momentum

Spanish Banks RoE (%)



Source: Bank of Spain, Estimates from analysts consensus.

Note: (1) Average RoE include listed Spanish banks: CBK, BKIA, BKT, LBK.

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3. **Significant cost synergies, real estate assets well provisioned with manageable execution risks**

4. **Attractive financials (targeting RoI 13-14% and EPS accretive in year 2), enhancing KPIs for Group, Spain and Portugal**

Relevant cost synergies: Targeting EUR c.500m

Key Cost Synergies Drivers

- **Improving operating efficiency by leveraging Santander Group's capabilities and best practices:**
 - Leverage Santander Group's *economies of scale* (e.g. joint purchasing)
 - Optimization of combined *branch network*
 - One single IT platform / operations optimization
 - HQ optimization
 - Benefit from Santander Group's global units to improve cost efficiencies

Expected efficiency improvements by 2020:

EUR c.500m
before tax

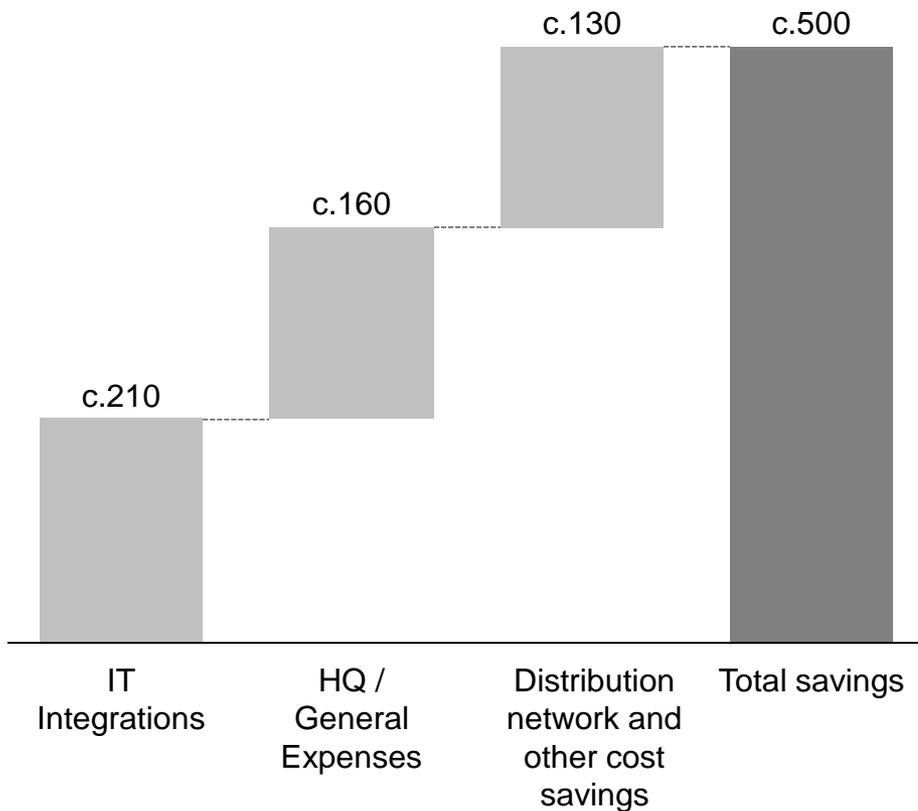
c.33% of Popular or
c.10% of the combined
2017 cost base of
Spain and Portugal

Restructuring Costs EUR 1.3Bn

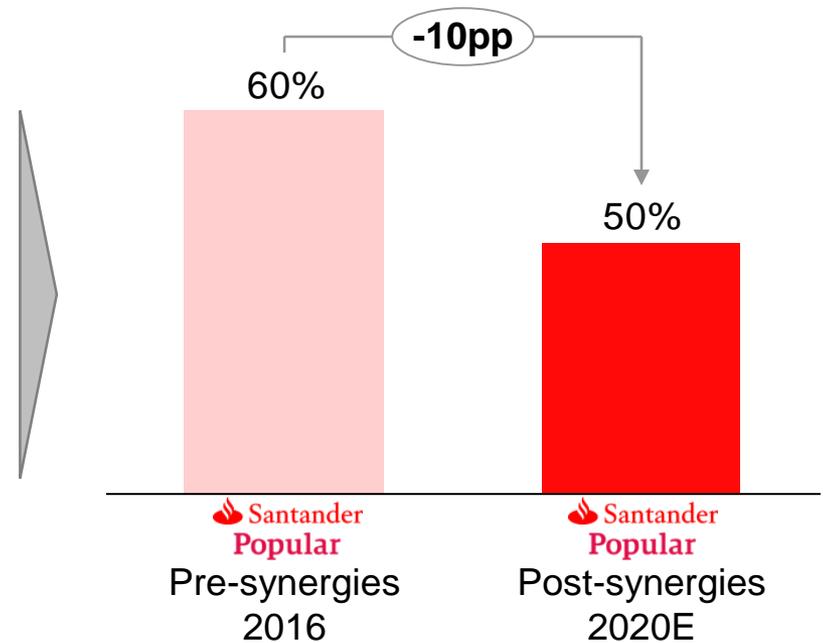
Improving efficiency of combined entity

Annual cost savings

(million euros)



Cost to Income ratio Spain (%)



Manageable execution risks

Potential Business Risks

Total Real Estate assets and loans of c.€34Bn gross (c.20Bn€ net)

Loans ex- Real Estate

Integration risk: revenue attrition

Preserving SME franchise

Mitigants

- **Provisioning above peers average** and roadmap in place to accelerate combined NPA reduction
- **Strong track record** of NPA management by Santander

- **Additional provisions to align with Santander criteria**

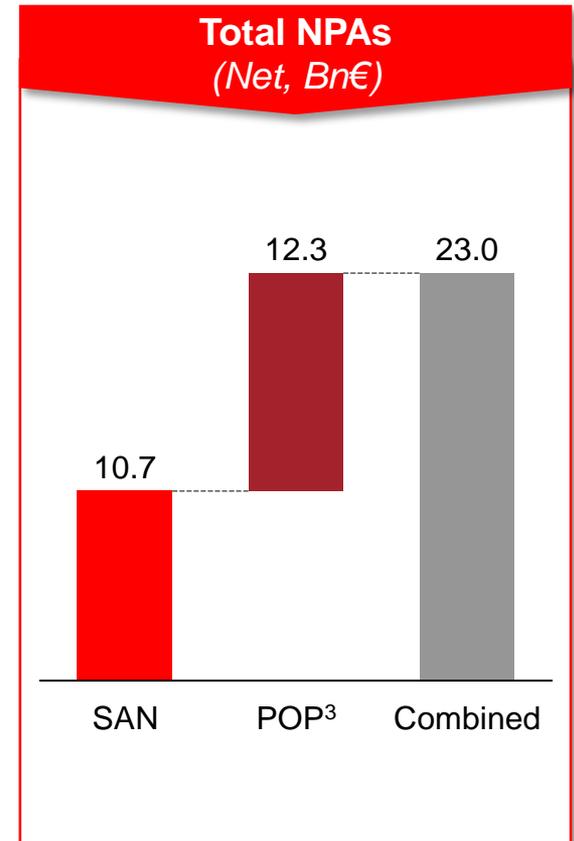
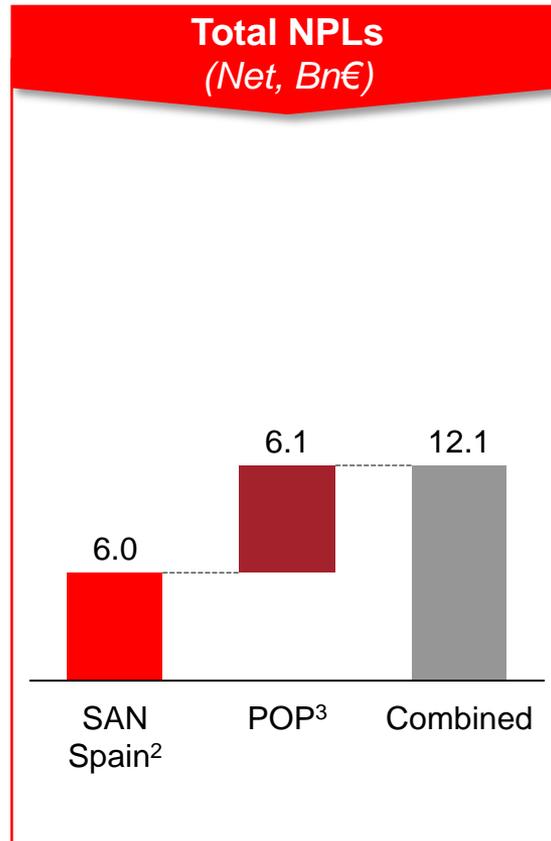
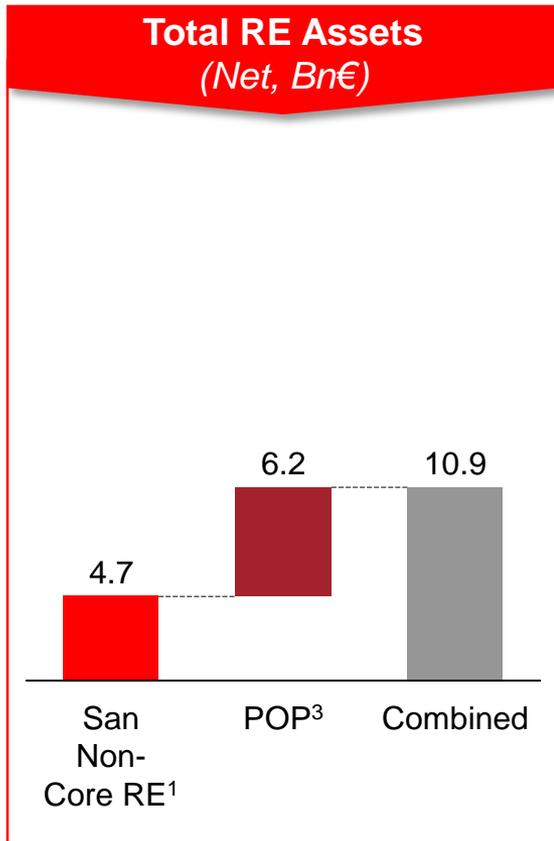
- **Proven integration track record** with limited potential revenue attrition
- **Assuming 9% revenue attrition** vs. consensus
- **Sharing of Best Practices and Know-How**

Potential risks incorporated in valuation

Transaction assumes an adequate provisioning of RE assets and loans

EUR Bn	Popular Pre-deal (Q1'17)		Popular Post-adjustments			Peers
	Gross value	% Cov.	Provision	% Cov.	Net value	% Cov.
Total RE Assets	17.7	39%	4.7	65%	6.2	52%
<i>Non-performing RE loans</i>	12.1	55%	2.5	75%	3.0	51%
RE assets + RE NPLs	29.8	45%	7.2	69%	9.2	52%
NPLs ex Real Estate	7.0	46%	0.7	56%	3.1	51%
NPA	36.8	45%	7.9	67%	12.3	52%
<i>Performing RE loans</i>	3.8	0%	0	0%	3.8	

Combined NPA exposure



Disposal plan to reduce Popular NPAs to non-material levels in 3 years

1 Santander non-core RE reported as “Real Estate activity in Spain”, including foreclosed assets and rental assets

2 Includes “Real Estate activity in Spain” and NPL in Santander Spain

3 Includes total RE assets and NPLs in Banco Popular perimeter, net of additional adjustments

We are assuming some revenue attrition while not including revenue potential upside

Revenue attrition due to...

- Clients overlap
- Santander Risk appetite
- Higher NPLs after provisions adjustment



Revenues 2019E:

**c.9%
below current
market
consensus**

Positive revenue possibilities (not included)

- Sensitivity to Interest rate changes (c.150m€ @100 bps)
- Revenue synergies (100 – 200m€)

Why are we acquiring Banco Popular?

1. **Popular: unique domestic consolidation opportunity in Spain and Portugal**

2. **Strong strategic / business fit at an attractive point in the cycle**

3. **Significant cost synergies, real estate assets well provisioned with manageable execution risks**

4. **Attractive financials (targeting RoI 13-14% and EPS accretive in year 2), enhancing KPIs for Group, Spain and Portugal**

2020E Net profit c.950M€

EUR million

2017E

2018E

2019E

2020E

POPULAR MARKET CONSENSUS

Revenues	2,840	2,920	3,000
Expenses	-1,500	-1,450	-1,460
Margin pre-provision	1,340	1,470	1,540
NET PROFIT	154	450	562

POPULAR WITH SYNERGIES

Revenues		2,662	2,758	
Expenses		-1,384	-1,151	
Margin pre-provision		1,278	1,607	
NET PROFIT		570	825	c.950

2020 assumes:

- No interest rate increase
- 9% Revenues attrition
- Costs synergies c.500m€
- Provisions normalized at 60bps / loans

Profitability improvement targets through economies of scale

■ SAN
■ POP
■ Combined

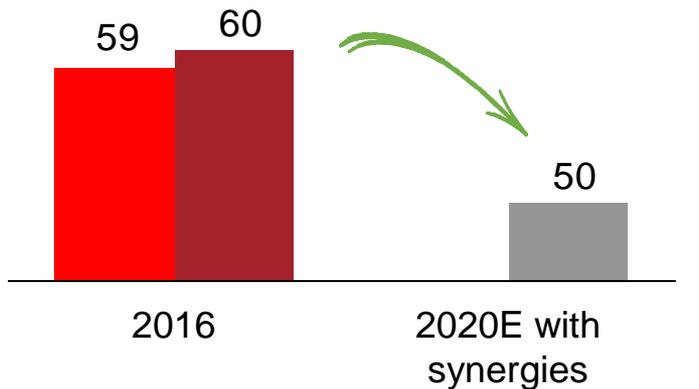


SAN Spain improvement of key ratios

Santander Spain public information perimeter

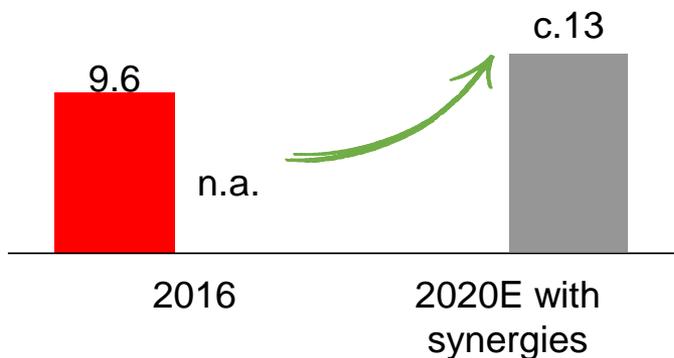
C/I

(%)



RoTE⁽¹⁾

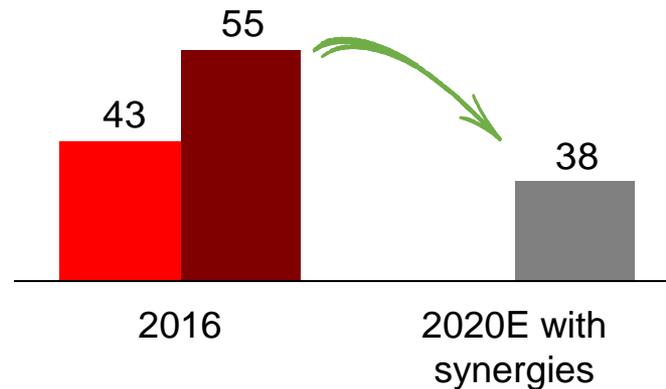
(%)



SAN Totta improvement of key ratios

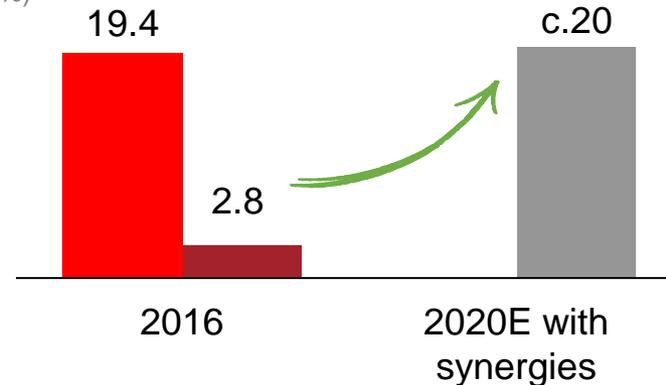
C/I

(%)



RoTE⁽¹⁾

(%)



(1) Calculated with equity as 11% RWAs

Summary of total provisioning and capital needs

EUR Bn

Real Estate Assets	4.7	Increasing coverage to 65% from current 39%
Real Estate Loans	2.5	Increasing NPLs coverage to 75%
Non Real Estate Loans	0.7	
Total Provision Deficit	7.9	
Net capital deficit	0.8	2.2 current Capital Deficit <ul style="list-style-type: none"> ▪ - 0,6 lower RWA after additional provision ▪ - 0.8 post-deal lower capital deductions
Other adjustments	0.4	
Prov. & Capital deficit	9.1	
Bailed in capital	- 2.0	
Net Prov. & Capital deficit	7.1	

Investment required of €7Bn with a targeted ROI of 13-14%

Provision and Capital Deficit	7.1
Restructuring Costs	1.3
Asset sales	-0.5
Pre Provision Profit 9M	-0.9

Net Investment (EUR Bn) ~7.0

Net Profit 2020 (EUR M) ~950

ROI 13-14%

**CET1 FL neutral impact
EPS accretive from year 2**

Attractive financial impact, enhancing key KPIs for the Group

	2018	2019	2020
Targeted EPS accretion (%)	Slightly negative	c.2%	c.3%
Targeted TNAV/S accretion (%)	c.3%		
CET1 Fully Loaded (%)	Neutral / Slightly positive	<i>Improved organic capital generation</i>	

ROI of 13-14% above Cost of Equity in 2019

EPS accretive from 2019 onwards

Banco Popular acquisition

Creating shareholder value through in-market consolidation

1

Overview
strategic and
financial
rationale

2

Popular
acquisition:
in-depth
review

3

Rights offering

4

Concluding
remarks

Rights Issue for the acquisition of Banco Popular

Size, terms and conditions

- **Rights issue of €7,000Mn**
- Rights offering with **preferential subscription rights for existing shareholders**
- **Underwritten** transaction

Expected timing¹



Banco Popular acquisition

Creating shareholder value through in-market consolidation

1

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Key conclusions

1.

Unique domestic consolidation opportunity to accelerate Santander Spain and Portugal's earnings growth

2.

Strong strategic/business fit at an attractive point in the banking cycle

3.

Significant cost synergies while execution risks manageable and potential revenues upside not being considered

4.

Shareholder value creation: targeting 13-14% RoI, Group's EPS and TNAV/S accretion, growing cash DPS

Creating shareholder value

Allowing us to continue delivering on our commitments

	Q1 2017	2018 targets
Loyal customers	15.5m	18.6m
Digital customers	22.1m	30m
Fee income ¹	12.1%	c.10% CAGR 15-18
Cost of risk	1.17%	1.2% AVG. 15-18
Cost to income	46.1%	45 - 47%
EPS (€)	0.122 (1 st quarter)	Double digit growth
DPS (€)	0.22 ²	Increase
FL CET1	10.66%	>11%

(1) % change (constant euros) (2) Dividends charged to 2017 profit to be submitted to the AGM approval

Thank you

Our purpose is to help people and businesses prosper.

Our culture is based on the belief that everything we do should be

Simple | Personal | Fair



Real Estate Assets - Breakdown

EUR Bn March 2017	POPULAR					SAN RE activities			COMBINED		
	Gross <u>value</u>	% <u>Cover.</u>	Addit. <u>Cover.</u>	Net <u>value</u>	% Final <u>Cover.</u>	Gross <u>value</u>	Net <u>value</u>	% <u>Cover.</u>	Gross <u>value</u>	Net <u>value</u>	% Final <u>Cover.</u>
Finished	6.5	29%	1.5	3.1	52%	2.2	1.1	50%	8.7	4.2	52%
Under const.	0.3	34%	0.1	0.1	60%	0.8	0.4	46%	1.1	0.6	50%
Land	7.9	50%	2.7	1.2	85%	5.1	2.0	61%	13.0	3.2	76%
Others	1.2	27%	0.4	0.6	55%				1.2	0.6	55%
Subtotal	15.9	39%	4.7	5.0	69%	8.1	3.5	57%	24.0	8.5	65%
Rented	1.8	33%	0.0	1.2	33%	1.6	1.2	25%	3.4	2.4	29%
TOTAL	17.7	39%	4.7	6.2	65%	9.7	4.7	52%	27.4	10.9	60%