

## **Speech of Mr. José Antonio Álvarez, Chief Executive Officer of Banco Santander, at the Annual General Shareholders' Meeting, April 7, 2017**

Mr. President of the government of Cantabria.

Mayor of Santander and authorities here today.

Shareholders of Banco Santander, ladies and gentlemen.

Good morning and thank you for attending Santander's AGM.

The Chairman has commented on the economic environment, the main lines of our business model, strategy and evolution, as well as the extent to which we have met our goals.

I will divide my speech as follows:

- 1) First, I will give you greater details of the Group's performance in 2016.
- 2) I will then share with you my views on the main initiatives and the results of the units in 2016, as well as the management priorities for 2017.
- 3) Lastly, I will dedicate a few minutes to the outlook for this year.

### **1. THE SANTANDER GROUP'S EVOLUTION IN IN 2016**

Our strategy and business model in 2016 continued to generate value for our customers and shareholders. Our geographic diversification and leadership in cost/income efficiency gives us a clear competitive advantage. This has enabled us to counter a difficult macroeconomic environment, particularly for banks, bouts of volatility and the higher tax pressure in some countries.

In this context, we produced solid financial results. We are generating sustainable and predictable returns, meeting our financial and commercial objectives.

As the chairman has already mentioned, we ended 2016 with an **attributable profit** of €6,204 million, 4% more than in 2015 and 15% higher on a currency-neutral basis. The exchange-rate impact was again negative last year.

Our profit puts us among the top part of the 17 global banks that are our peers. Moreover, if we focus just on European banks, our fourth quarter profit was the highest.

This profit includes some non-recurring results for a net negative amount of €417 million compared to €600 million negative in 2015. These figures are the net between positive capital gains and negative results of restructuring costs and other provisions.

The **underlying profit before the non-recurring results and taxes** (the tax rate rose to 30%), **was 12% higher at €11,288 million on a currency-neutral basis.**

These good results were due to an improved performance in most units and to the positive evolution of the main income statement lines:

- **Gross income increased 3% to €43,853 million** on a currency-neutral basis.

Among our European peers, no other bank generated so much gross income in 2016.

**This revenue, moreover, is of great quality, as it was driven by customer business.** Our net interest income and fee income accounted for 94% of total revenues. This structure **enables us to grow consistently and recurrently despite** the pressures on the banking sector in the last few years.

I would like to highlight the **good performance of fee income**, one of our main goals for the year. **It rose 8%** on a currency-neutral basis, double the growth in 2015. This increase was due to more business, greater customer loyalty and the range of higher value-added products.

- **Operating costs, which were €21,088 million, also performed well.** In real terms and on a like-for-like basis, they were 2% lower. This was the third year running that costs were flat or lower as a result of our discipline.

Measures were also taken to rationalise and streamline structures, adapting the cost base to each country's business reality.

In consequence, we were able to keep on investing in the commercial transformation (commercial tools, digitalisation, new branch models, etc.) in order to enhance customer satisfaction, **while remaining one of the world's most efficient banks.**

- **All of this was achieved with a 2% reduction in loan-loss provisions** (on a currency-neutral basis), underscoring the improved credit quality and strengthening the risk culture throughout the Group. On the one hand, all Banco Santander's professionals are responsible for the risk we generate and, on the other, there is a series of principles that are known and are being integrated into our daily work.

I will now turn to the **balance sheet**:

- **Balanced growth between lending and funding.**
- **Loans** rose in **seven of the Group's 10 core units** and to individuals as well as to companies. Our effort in marketing products and services was recognised by the magazine *Euromoney* with the award of **Best bank in the world for SMEs**.
- **Funds** increased in the **10 core units** (current accounts and mutual funds).
- We have comfortable **liquidity ratios that exceed the required levels**.
- In risk quality, the **NPL ratio** improved every quarter in the last 12 quarters and fell **below 4% for the first time in five years** (since March 2012).
- The **cost of credit** dropped to 1.18%, **meeting the goal** set for the coming years.
- In **solvency** terms, the Chairman has already commented on our ratios. I will just reinforce some ideas:
  - Our fully-loaded CET1 ratio increased in every quarter of 2016, after paying **cash dividends of €2,469 million**. Furthermore, the rise was one of quality as we achieved it organically. Unlike other banks, we did not need to sell businesses, restrict growth or cut the dividend.
  - Our levels of capital comfortably exceed the European Central Bank's requirements.
  - Supervisors recognise the advantages of our model and, as a result, allow us to have a capital buffer lower than that of other global systemically important banks.

Moreover, we have combined the generation of capital with **high profitability**. In underlying terms, our return on tangible equity (RoTE) is 11%, comparing well with that of our peers.

**In short, in 2016:**

- Both profit and dividends increased.
- We grew in volumes on a currency-neutral basis.
- The balance sheet structure remained balanced.
- And we significantly improved our solvency and credit quality.

All of this was achieved while progressing in our commercial transformation, fostering customer relations and improving their experience of the bank.

## **2. EVOLUTION BY BUSINESS AREAS**

I will now briefly look at the evolution of the main units in 2016 and the priorities for 2017.

The strategy for the **units in MATURE MARKETS** was to increase the number of loyal customers, gain market share, control costs and improve credit quality.

At **SANTANDER ESPAÑA** we continued to focus on building a deeper and lasting relationship with its customers. The **1|2|3 strategy** is already yielding good results:

- We increased the number of customers and loyalty, with more than 500,000 new customers from other banks and more than 100,000 new loyal companies.
- We bolstered commercial activity. The 1|2|3 customers already account for more than half of new loans.
- We enhanced the customer experience. We moved from fifth place in customer satisfaction rankings to the Top 3.
- We improved risk quality. Not only did we attract more profitable customers, but also more solvent ones. This is reflected in the improvement in our NPL ratio and in our cost of credit ratios, which have evolved favourably and are well below the sector's average.
- In order to back up this strategy, we created the new model of larger branches known as Smart Red, which enables better advice and service to be provided, as well as integration with digital channels.
- As a result of these initiatives, we are gaining market share in new consumer credit, capturing payrolls and transactional products as continuing to lead the wholesale and private banking segments.
- **Regarding results.** Against a backdrop of tough competition and very low interest rates, Santander Spain **posted an attributable profit of €1,022 million, 5% more** than in 2015. An improved risk profile, lower provisions, the efficiency plan and a rise in fee income underpinned the higher profit.
- We will continue to concentrate **in 2017** on increasing our market share organically and profitably. We also want to keep on enhancing the customer experience: we will continue the digital transformation and the change in our branches. Lastly, we want to be the reference bank for SMEs and companies, reinforcing our commercial positioning while maintaining leadership in wholesale banking and large companies.

Of note in the **UNITED KINGDOM** in an environment of greater uncertainty in the second half of the year was our solid business evolution, with 1|2|3 customers

reaching 5.1 million and growth in loans to companies. We remained focused on operational excellence, with a continuous improvement in our mobile phone channels and online banking. The number of digital clients rose 25%.

- I would like to stress that the agenda of regulatory changes is very demanding for the UK banking sector. As I announced at the last AGM, and in accordance with local requirements, we have begun the process of ring-fencing part of our wholesale activity, which has to be completed in 2019.
- **Attributable profit was 4% lower** (on a currency neutral basis) **at €1,681 million**, hit by the new corporation tax surcharge on banks. **Profit before taxes**, which better reflects the business performance, **increased 8%** thanks to larger volumes, the good management of spreads, control of costs and lower provisions.
- Our priority **for 2017** is to progress in installing the new structure that I have commented on. In addition, the retail bank will focus on customer loyalty as the main driver of growth, we will give priority to operational and digital excellence in order to offer the best customer experience, and we will concentrate on obtaining an increasing profitability. In short, we will continue our commitment to British companies and customers.

**SANTANDER CONSUMER FINANCE** offers a unique value proposal and holds a clear leadership position in Europe. In 2016, we continued to gain market share, underpinned by a solid business model.

- We also successfully completed the agreement with Banque PSA Finance (BPF), which enabled us to boost business in 11 countries and strengthen our diversification.
- **Attributable profit increased 18% to €1,093 million**. Profit was higher for the seventh year running (in 2009 earnings were less than €500 million), which underscores the strength of our business model throughout the economic cycle.
- Our goal **in 2017** is to maintain the level of profitability and keep on gaining market share. We are also focusing on pro-actively managing agreements with car manufacturers and on accelerating the digitalisation of business.

In the **UNITED STATES**, we integrated into one holding (Santander Holding) all our operations in the country and we made significant progress in complying with regulatory requirements. In addition, we continued to work on the transformation programme to improve risk management and technological and operational capacities.

- All these changes and measures are aimed at building in the medium term a more profitable business, but they are impacting results temporarily and largely explain the **reduction in attributable profit to €395 million**.
- We have two priorities **in 2017**: improve the risk control and management systems in order to advance in the regulatory agenda and strengthen the franchise, aiming for greater customer loyalty and an enhanced customer experience.
- All of this should enable significant growth in the coming years, moving the country's profitability close to the Group's standards.

Our bank in **PORTUGAL** is the most solid and profitable in the country.

- The two priorities in 2016 were: on the one hand, the structural improvement of the commercial model, which was reflected in a 21% rise in digital customers and 32% in loyal ones. On the other hand, the technological and operational integration of Banif's business, which was successfully completed in October, within the schedule.
- Very good year in results. **Profit was 33% higher at €399 million**, due to higher gross income and lower provisions.
- **In 2017**, we want to continue to gain profitable market share and optimise the cost of funding. We are also determined to improve efficiency and the cost of credit and adjust the capital structure to the new regulatory demands.

Business volumes in **DEVELOPING MARKETS** grew at a faster pace than in mature ones, interest rates were higher and also profitability. In this environment, Santander has local critical mass, strong commercial models and active risk management, all of which produced very good results in all units.

Beginning with **BRAZIL**, and in an environment of recession, profit was excellent, due to the franchise improvements made in the last few years, good business dynamics and progress in digitalisation. The number of digital clients increased 45% to more than six million.

- We continued in 2016 to be the clear leader in wholesale banking and we continued to make significant improvements in retail banking and in developing high growth businesses where we are gaining market share. Of note was the payroll loan, acquiring business, via Getnet, and auto finance, where we strengthened our leadership position.

- All these measures were reflected in the financial variables: we boosted deposits, grew in mutual funds more than the market, improved the credit trend in the second half of the year and significantly increased profits.
- **Attributable profit was 15% higher at €1,786 million**, due to the good performance of commercial revenues, particularly fee income; improved efficiency, with costs once again increasing at below the average inflation rate, and a cost of credit lower than envisaged at the start of the year.
- We are particularly pleased that in 2016 we formed for the first time part of the group of best companies to work for in the country.
- As regards the strategic priorities **for 2017**, we are focusing on revenue growth and on increasing our market share in acquiring business, consumer credit and SMEs. We remain immersed in the digital transformation and are paying particular attention to risk management and recoveries.

The strategy in **MEXICO** was very centred on customer retention, the commercial transformation and innovation. We were very busy in launching products and commercial agreements such as the Santander Plus programme (similar to the 1|2|3 account in Spain), which has already attracted more than 1.1 million customers. We also launched the Santander-Aeroméxico card, of which more than 430,000 were issued.

- In consequence, we increased lending and deposits, the number of loyal customers rose 16% and digital ones increased 46% to 1.3 million.
- **Attributable profit rose 18%** (on a currency neutral basis) **to €629 million**, driven by gross income, mainly net interest income.
- **In 2017** we are improving our commercial tools, the CRM and digital platforms. We are strengthening the Santander Plus offer in order to deepen customer loyalty. We are also focusing on increasing the number of payroll accounts, consolidating mortgage business and recovering leadership in SMEs.
- In order to attain these objectives and continue to improve the franchise and operating systems, we announced a three-year MXN 15 billion **investment plan**.

At **SANTANDER CHILE** the priority was to maintain market leadership and improve the quality of service. We started from a position of disadvantage compared to our competitors but managed to close the gap in the last few years. In 2016, we topped the customer satisfaction ranking. We gained market share and continue to be the leaders in lending and second in deposits.

- **Attributable profit increased 16%** (currency neutral) **to €513 million**, with the main P&L lines performing well.
- Our focus **in 2017** is on consolidating the commercial transformation via the new branch model. We are continuing to improve the quality of customer attention and their experience. We are also strengthening business with large and medium-sized companies and paying particular attention to increasing fee income.

In **ARGENTINA**, after the change in the institutional framework, we want to exploit the country's high growth potential and a financial system which is very transactional. This is why we decided to bolster our position in the country by acquiring Citi's retail business.

- **Attributable profit was 52%** (currency neutral) **higher at €359 million**, thanks to the good performance of net interest income and fee income.
- **In 2017**, our priorities are to integrate the business acquired, continue the transformation plan toward a digital bank and grow in loans to companies and individuals and in customer funds.

In **POLAND**, we continue to be the reference bank in innovation and digital channels. We increased the number of loyal customers, particularly companies, and our credit growth is well above that of the sector as a whole.

- **Attributable profit was 6% lower at €272 million**, due to the new tax on assets. **Excluding this impact, profit rose 14%** thanks to the good performance of net interest income and a very significant improvement in credit quality.
- The strategic objectives **for 2017** are: maintain the high standards in quality of service; increase the number of loyal clients and progress in end- to-end digital transformation in order to be leaders in digital channels. We also want to gain market share in volumes and maintain leadership in profitability in a tougher regulatory environment.

Lastly, the units in **URUGUAY** and **PERU** **increased** their profits **32% and 21%, respectively** (on a currency neutral basis). In Uruguay's case, this was due to significant growth in gross income and in Peru's to lower provisions.

I will end this overview of the business areas with some comments on **GLOBAL CORPORATE BANKING**, whose results are included in the profit figures I have given for each of the countries.

The main activity of this business is:



- a) To provide service to our more global clients, who benefit from our international presence and connectivity between regions.
- b) Offer products and solutions to the segment of companies and SMEs in retail banking.

We are leaders in countries such Spain and Brazil, as well as number one in some products for the whole of Latin America.

**Profit was 30% higher in 2016** (on a currency neutral basis), underpinned by the strength and diversification of revenues. The latter represent 13% of the Group's total: 86% of revenues come from customers.

**Looking ahead**, we will continue to develop this business in the UK and US, while strengthening our presence in countries where we already are leaders.

We will also continue to bolster connectivity with retail banking clients and progress toward a model that is lighter and more efficient in capital.

I would like to point out that these results would not have been possible without the **CORPORATE CENTRE'S** contribution. We continued to work in 2016 on creating a more agile centre and one that contributes more value to the Group.

We are optimising and digitalising processes and have restructured functions and posts in order to improve productivity and efficiency, while our policies, models and control frameworks enable the Group to have solid governance.

### **3. ENVIRONMENT, OBJECTIVES AND CONCLUSION**

Ladies and gentlemen, shareholders,

After detailing the Group's performance and that of the main units, I will now end with a **look at the future**.

2016 has been a year of sensible changes in the economic and political arena and 2017 still offers some uncertainties in these areas.

There are some **positive aspects**, however, that invite optimism about the near future.

- Financial markets are increasingly resilient, quickly recovering from bouts of volatility.
- The outlook for 2017 points to some strengthening of global growth, which could reach 3.4%.
- This growth will be supported by both mature as well as developing economies, which will improve, as a whole, their growth for the first time in

five years.

- Developing economies as a whole have accelerated their growth. Countries such as Brazil and Argentina have adopted economic policies that should enable them to leave behind recession in the coming quarters.
- Mature economies were already showing recovery in the second half, particularly the UK where the impact of the referendum to leave the EU has so far been limited. Meanwhile the Spanish economy is again growing at more than 3%.
- Expectations of interest rate hikes, very positive for our commercial and retail banking business, are increasingly greater in those countries where we operate.

We are thus seeing the **positive trends of the Group in 2016 being maintained in the first months of this year.**

- We are continuing to increase our loyal and digital clients which, coupled with a good evolution of the markets, is reflected in revenue growth.
- Operating costs continue to be under control and credit quality is improving further, underpinned by the macroeconomic recovery and risk management.
- And we are still generating capital organically.

These trends allow us to be optimistic about achieving the goals we announced to investors last September, and which the Chairman has shown.

In order to attain them, **we have set the following financial priorities for 2017:**

- Accelerate **revenue growth**, particularly in **developing markets**, where we see high one-digit or double-digit growth in all units and where interest rates enable good spreads to be obtained.
- In **mature markets**, where revenues are under pressure, we must **increase our market share**, mainly in companies, and continue to grow in fee income, mainly in cards, insurance and funds. The recent agreement to acquire 50% of Santander Asset Management should be seen in this context.
- Continue to keep **costs under control**, keeping their total increase below the average inflation of the countries where we operate.
- Keep on **improving the cost of credit**, with the Group's provisions falling as the cycle improves in some core markets such as Brazil and Spain.
- Grow **risk-weighted assets (RWAs)** below the increase in the Group's loans and

profit in order to improve our return on risk-weighted assets (RoRWA) ratio.

- All these measures should **move our profitability** toward the RoTE goal of 11% in 2018, while strengthening our capital ratio.

Ladies and gentlemen, shareholders

Although our share price has increased significantly in the earlier months of 2017, **I believe that our share price today still does not reflect the strength of our balance sheet and the potential in the long term of our Group results:**

I am confident that the diversification and quality of our businesses, their growth capacity and profitability potential will be reflected in a higher share price.

**Lastly, I would like to thank all the Group's professionals** for their efforts in transforming and improving our bank. The achievements in 2016 and attaining the goals in 2017 would not be possible without the contribution of each and every one of them.

As well as having the best professionals, we have also drawn up succession plans in key posts in order to guarantee business continuity in the future.

We will continue to work every day to help people and businesses prosper, and to turn Santander into the best retail and commercial bank by earning the lasting loyalty of our customers, communities and, in particular, all our shareholders.

**I firmly believe that, with the efforts of all of us, the engagement of our employees and the confidence of our customers and all of you, we can attain all our goals.**