

# BoAML Banking & Insurance CEO Conference 2010

## 'Competing in the Age of Austerity'



 BANCO  
POPULAR

London, September 28th 2010

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# Agenda

1. A challenging environment for retail banks
2. Banco Popular: managing through the cycle with a superior business model
3. Competing in the age of austerity: the path to a profitable model
4. Conclusions



# Agenda

**1. A challenging environment for retail banks**

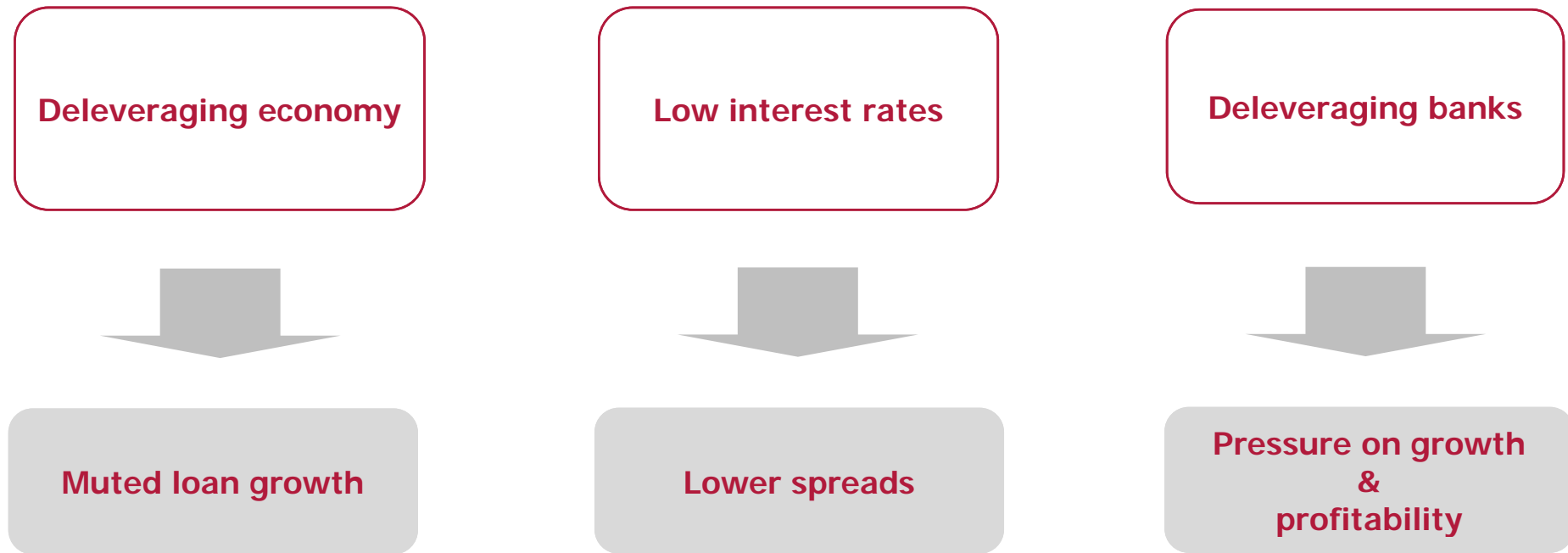
**2. Banco Popular: managing through the cycle with a superior business model**

**3. Competing in the age of austerity: the path to a profitable model**

**4. Conclusions**

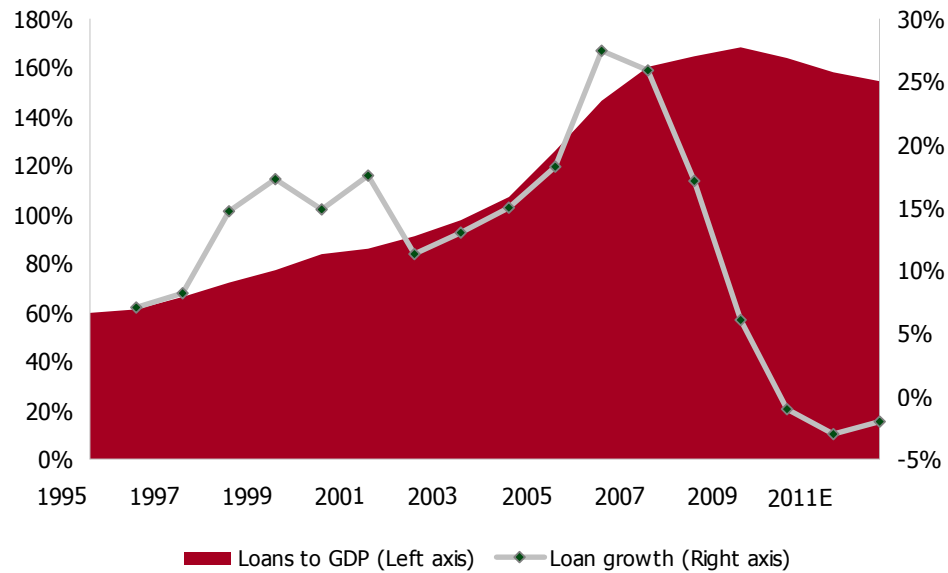


# Competing in the age of austerity: a challenging environment for retail banks



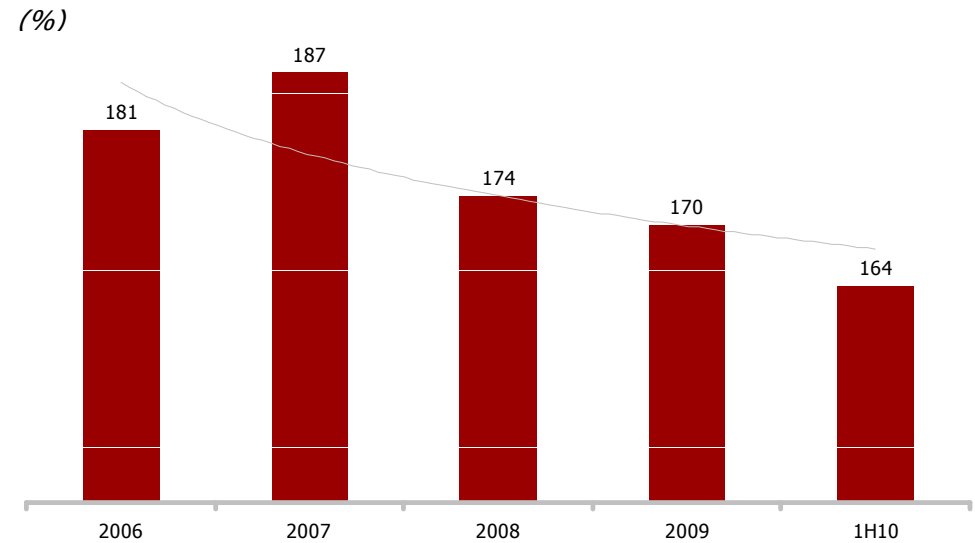
# Competing in the age of austerity: deleveraging economy and Spanish banks

## Muted loan growth: Spanish Private Loans to GDP



Source: BoS, BoAML

## Loan to deposits Spanish banks

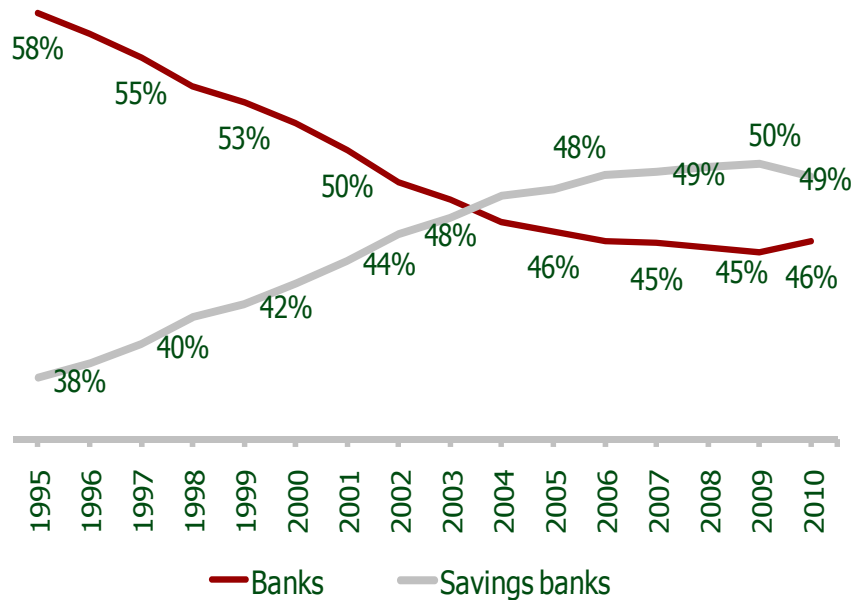


Source: Quarterly reports; Spanish peers: Santander Spain, BBVA Iberia, Banesto, Sabadell & Bankinter

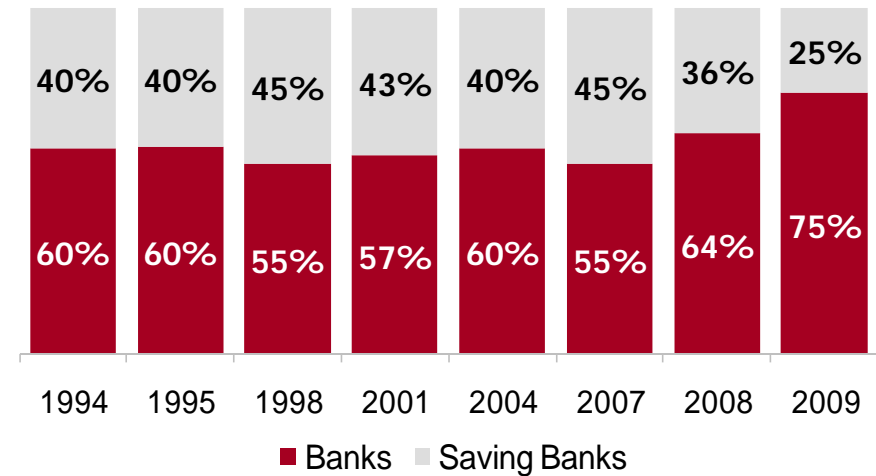


# Competing in the age of austerity: new competitive landscape in Spain

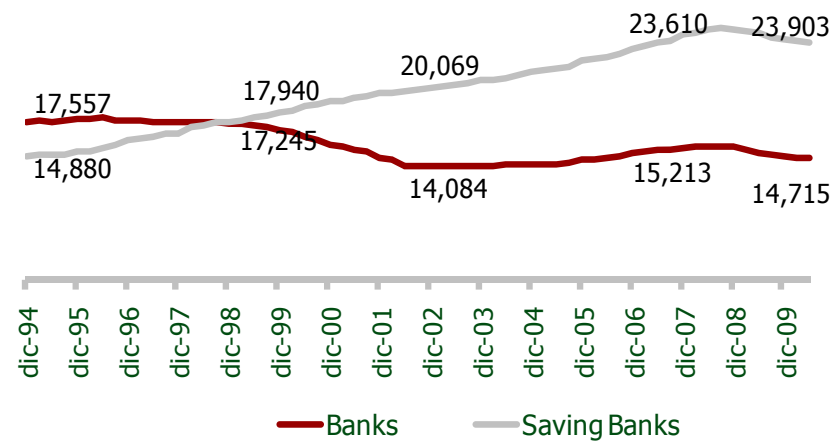
Market structure: loans market share



Market structure: Net Profit market share banks vs. cajas



Market structure: number of branches



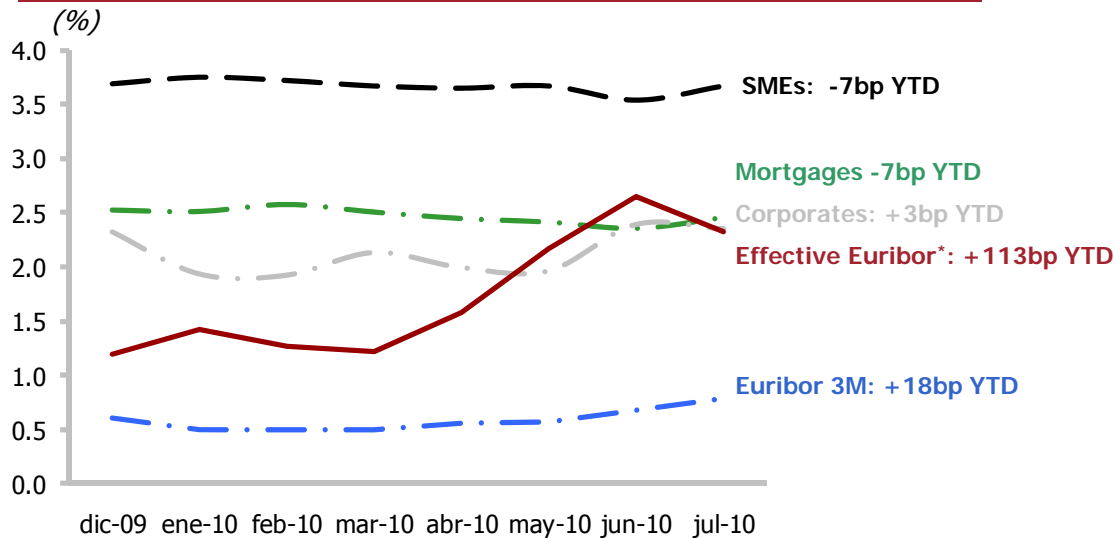
Savings banks would have to reduce branches by 25%, according to the BoS



Source: BoS. Only Spanish operations

# Competing in the age of austerity: managing spreads and margins is the key

Credit institutions front book yield vs. effective rate (\*)



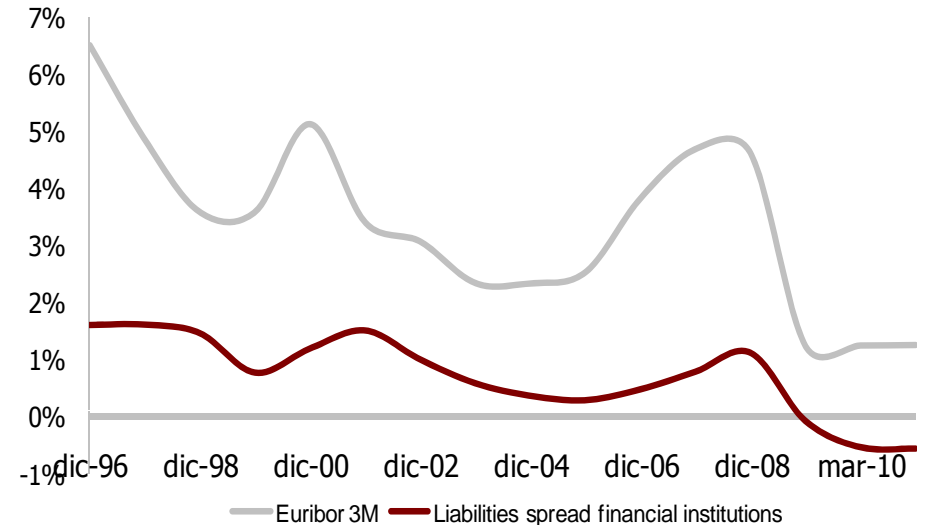
\* Note: Effective Euribor3M= Euribor 3M+ Spanish sovereign spread

Source: BoS; Bloomberg

## Our views

- Front book spreads do not reflect hike in funding cost
- Assets spreads will be at structurally high levels due to risk perception, higher capital consumption and scarcity of capital & liquidity
- Only banks with client focus will be able to increase prices effectively

Liabilities spread credit institutions



Source: BoS

## Our views

- Deposits will be structurally more expensive
- Competition should ease in coming months, but will continue as attraction for new individual clients
- Not all institutions are able to pay equally for deposits
- Interest rates will remain lower for longer



# Competing in the age of austerity: First conclusions – Not all institutions will be capable of competing in this demanding environment

## Challenges

Deleveraging economy

Low interest rates

Deleveraging banks

## Response to these challenges

Gathering deposits/  
gaining mkt. share

Adjusting spreads/  
profitable growth

Reducing RWA/  
raising Equity

## Our views

Not all institutions will be able to pay equally for deposits or to gain market share

Increasing importance of a client oriented business model

Basel III implications  
Limited access to capital for some institutions

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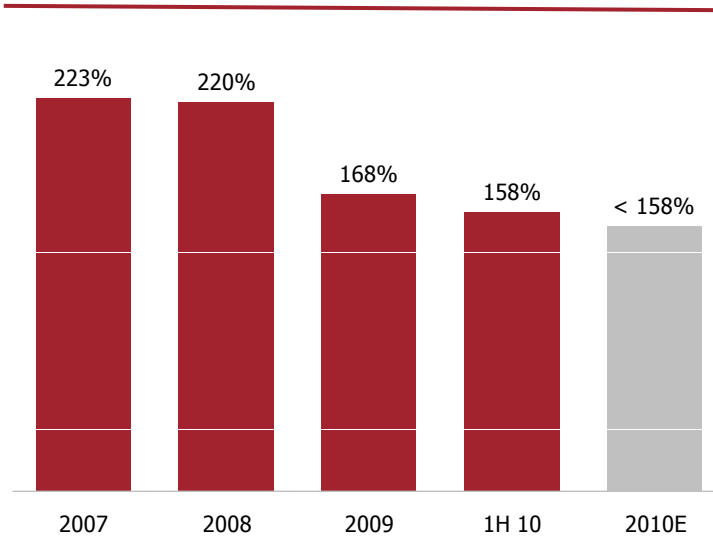
# Popular's strategy: Adaptation to the crisis well ahead of the system

Spanish crisis developments	<p><b>Stage 1</b></p> <p><b>2008-2009</b></p> <ul style="list-style-type: none"> <li>▪ Sharp economic &amp; credit contraction</li> <li>▪ Debt markets frozen</li> <li>▪ High systemic risk</li> <li>▪ Strong decrease interest rates</li> </ul>	<p><b>Stage 2</b></p> <p><b>2010</b></p> <ul style="list-style-type: none"> <li>▪ Economy bottoms, NPLs still rising</li> <li>▪ Debt markets re-open gradually</li> <li>▪ High sovereign risk</li> <li>▪ Low interest rates environment</li> </ul>	<p><b>Stage 3</b></p> <p><b>2011 &amp; onwards</b></p> <ul style="list-style-type: none"> <li>▪ Low GDP growth, NPLs peak</li> <li>▪ Debt markets selectively open for some institutions</li> <li>▪ Low interest rates environment</li> </ul>
Popular	<ul style="list-style-type: none"> <li>▪ Risk management</li> <li>▪ Focus on liquidity</li> <li>▪ Solvency: raising equity</li> <li>▪ Adapt our network structure</li> </ul>	<ul style="list-style-type: none"> <li>▪ Risk management</li> <li>▪ Increase strongly our liquidity</li> <li>▪ Reinforce our already strong solvency</li> <li>▪ Adapt our network structure</li> </ul>	<ul style="list-style-type: none"> <li>▪ Commercial goals: market share gains</li> <li>▪ Increase further our liquidity</li> <li>▪ Focus on profitability</li> </ul>
Savings Banks	<ul style="list-style-type: none"> <li>▪ Risk Management</li> <li>▪ Focus on liquidity</li> <li>▪ Solvency: issuing preferred shares</li> </ul>	<ul style="list-style-type: none"> <li>▪ Risk management</li> <li>▪ Little capacity to reduce commercial gap</li> <li>▪ Solvency: raising public funds</li> <li>▪ M&amp;A: deals announced</li> </ul>	<ul style="list-style-type: none"> <li>▪ Restructuring process</li> <li>▪ Strong reduction branch network</li> <li>▪ Deleverage</li> <li>▪ Solvency: to raise equity, re-pay public aids</li> <li>▪ Corporate governance: change corporate structure, market scrutiny</li> </ul>

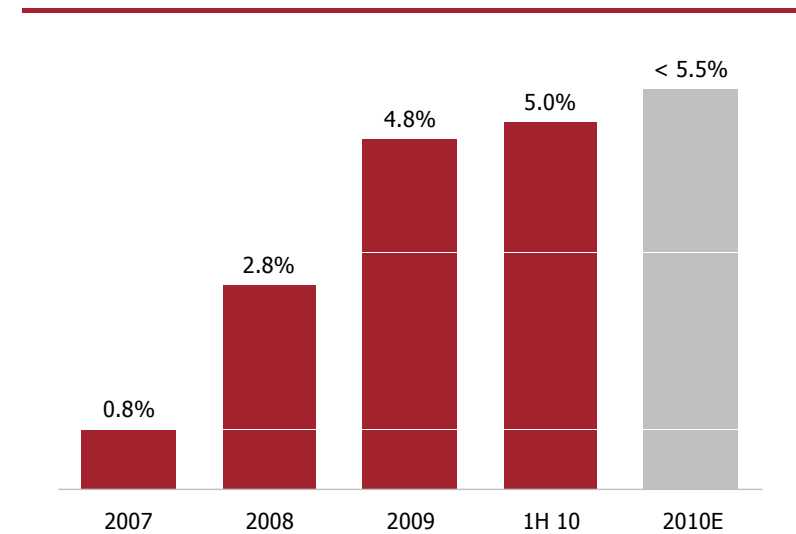


# Popular's strategy: Preserving capital and liquidity while starting to focus on business opportunities as credit deterioration eases

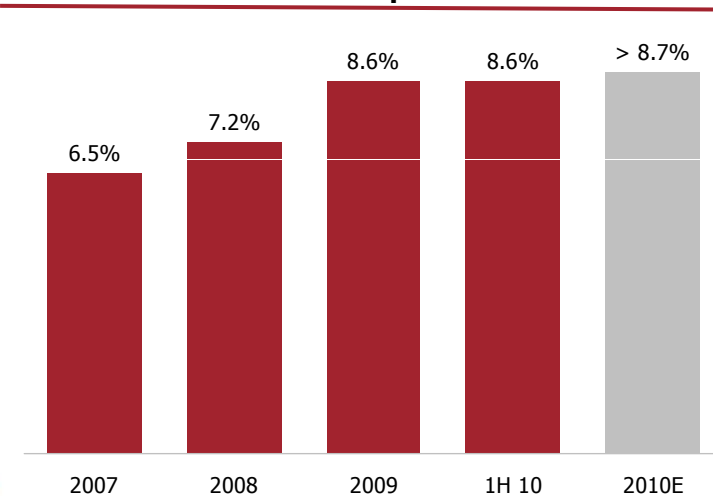
## Loan to Deposits ex repo



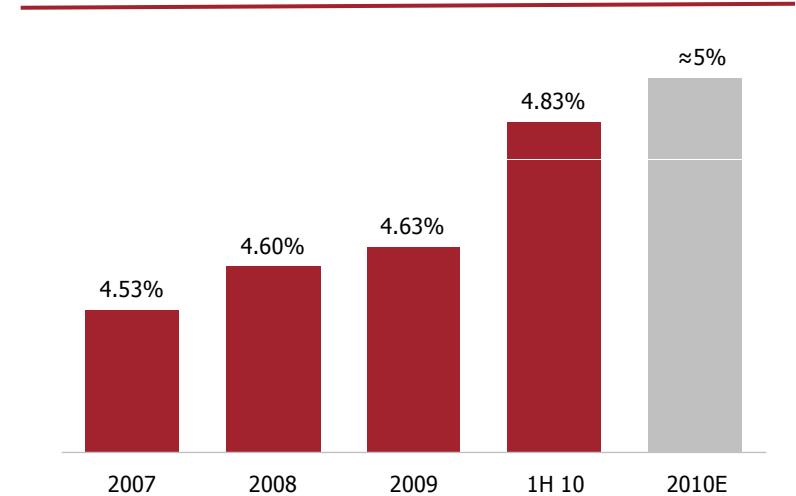
## NPL ratio



## Core capital



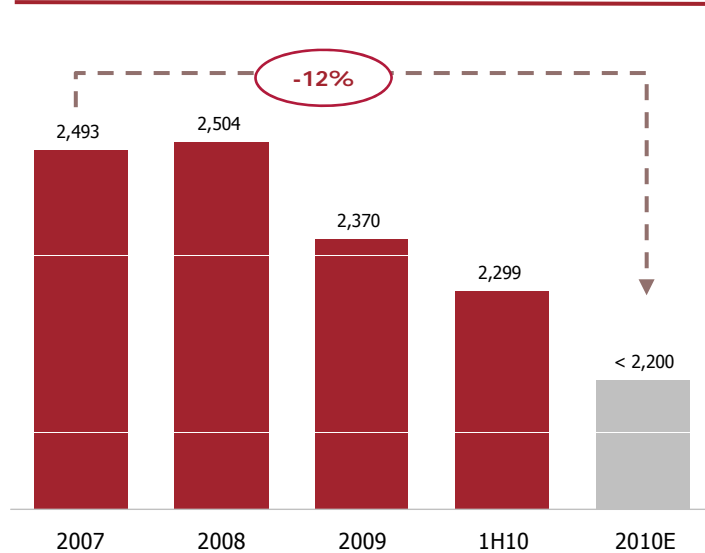
## Business market share <sup>(1)</sup>



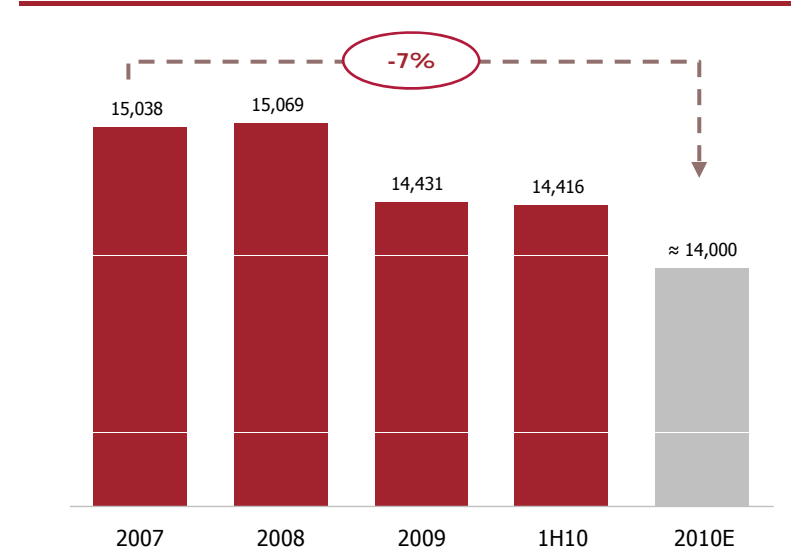
(1) Business market share: overall market share in loans and deposits

# Popular's strategy: optimizing our branch network in the new business environment and capturing synergies from the merger of the subsidiaries

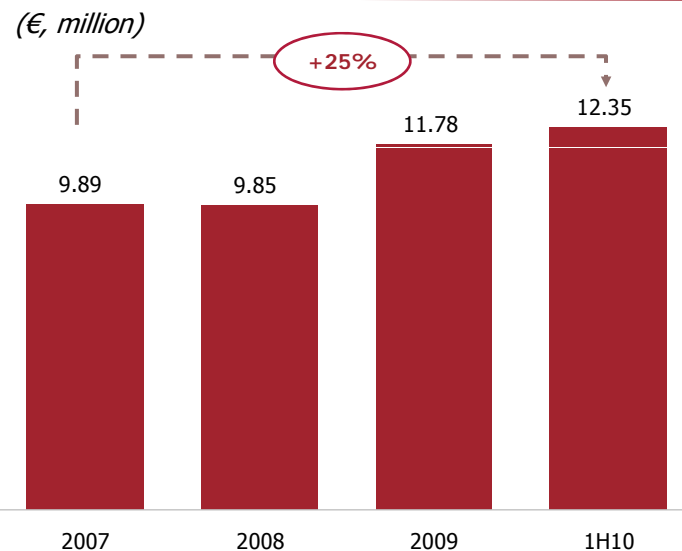
## Branch Network Evolution



## FTEs Evolution



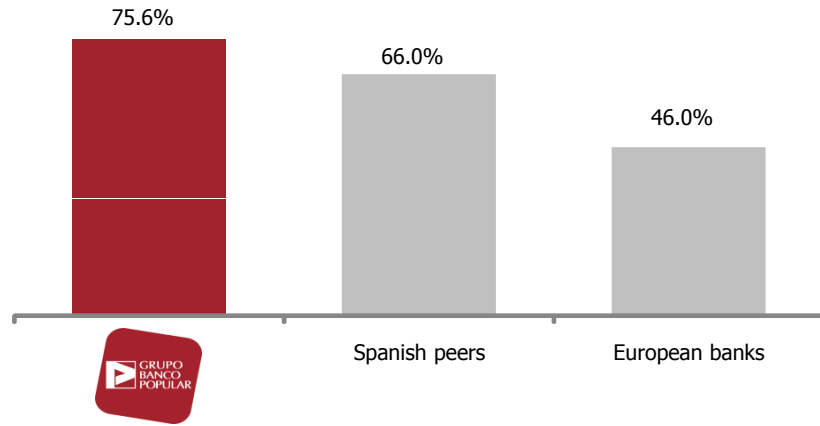
## Business volume per FTE



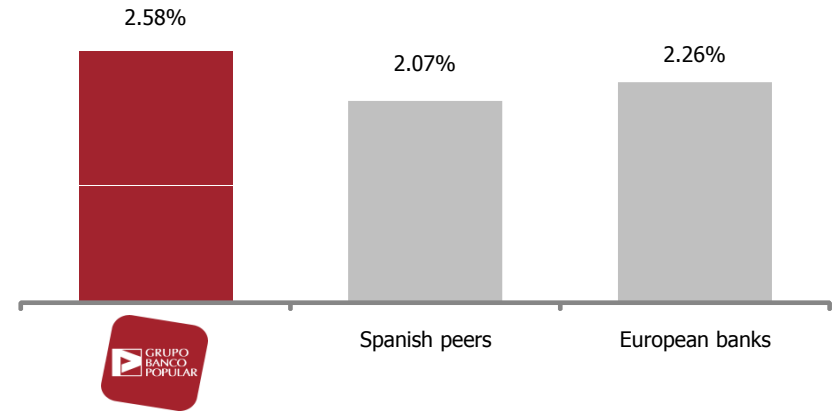
Note: Business volume = loans + deposits + AuM

# Thanks to a robust model, profitable all through the cycle

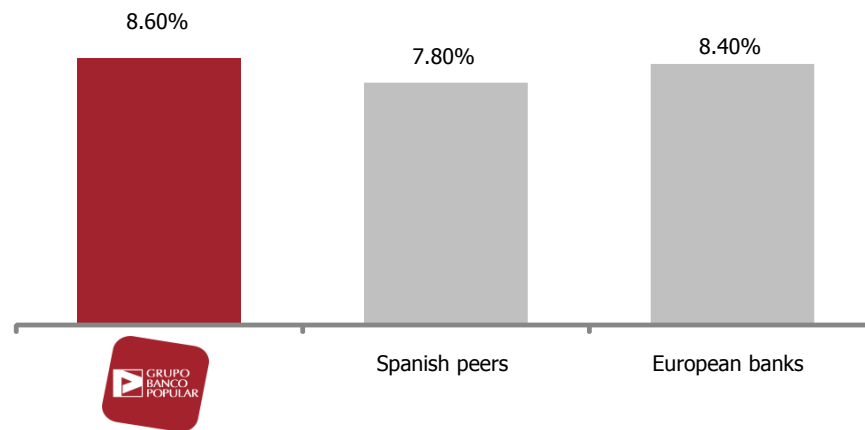
## Retail and commercial: loan to assets



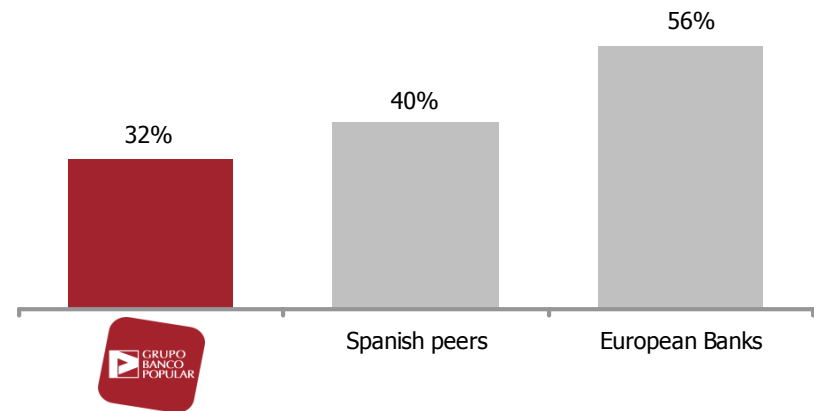
## Pre-provision profit over loans



## Core capital



## Cost to income ratio



Source: Quarterly reports; Spanish peers: Santander Spain, BBVA Iberia, Banesto, Sabadell & Bankinter  
European banks: Credit Suisse Banks Valuation, July 2010 & KBW Valuation July 2010



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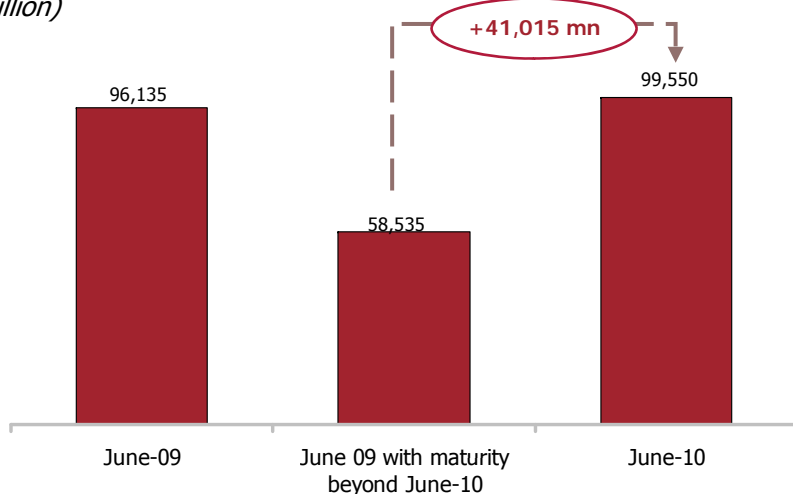
# Competing in the age of austerity: the path to a profitable model



# Managing spreads & margins: capacity and ability to manage spreads on the asset side

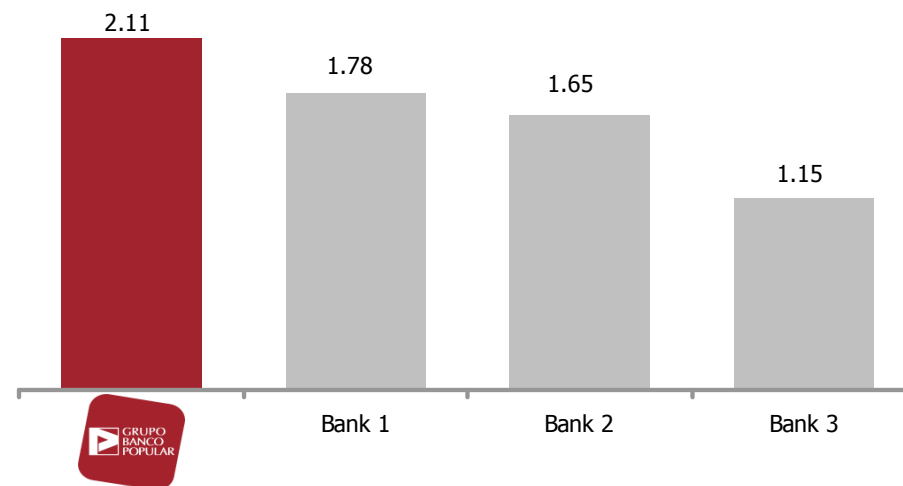
## Capacity: Low duration of lending book

(€, million)



## Ability: NIM vs. peers

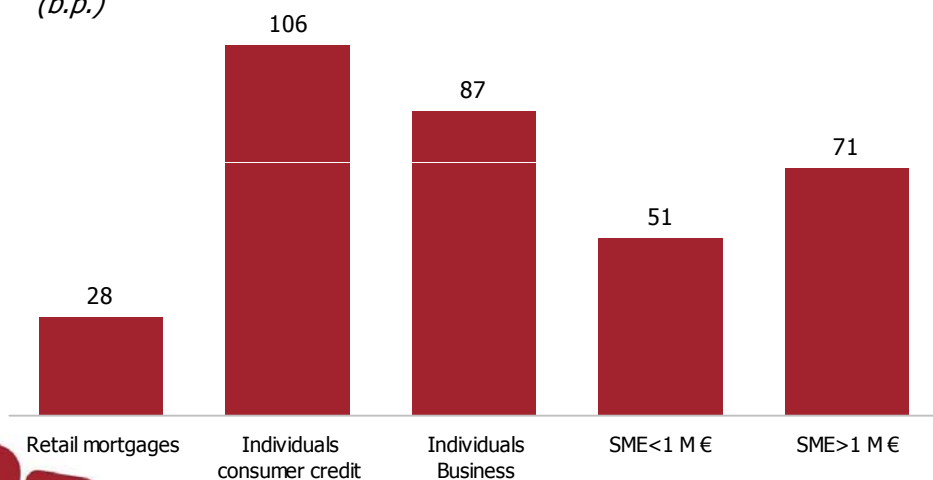
(%)



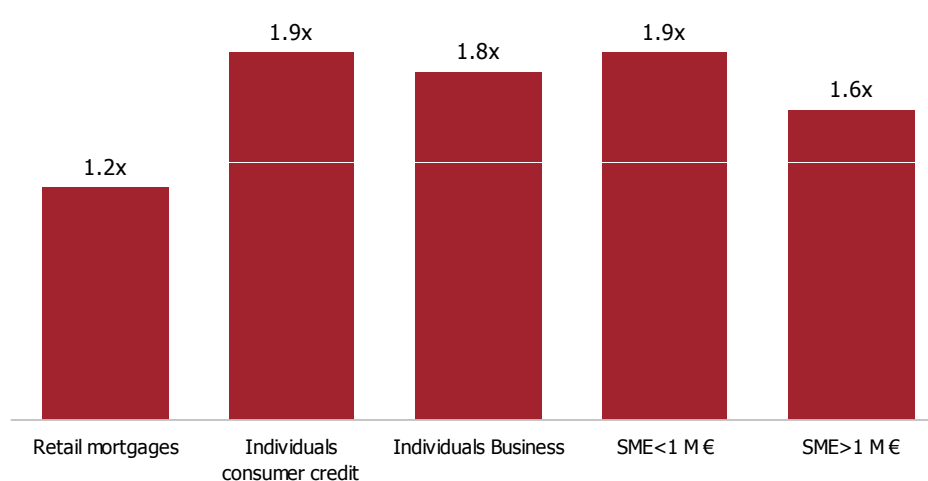
Note: Comparable banks Banco Sabadell, Banesto and Bankinter

## Ability: Front book spreads vs. banks as of May-10

(b.p.)



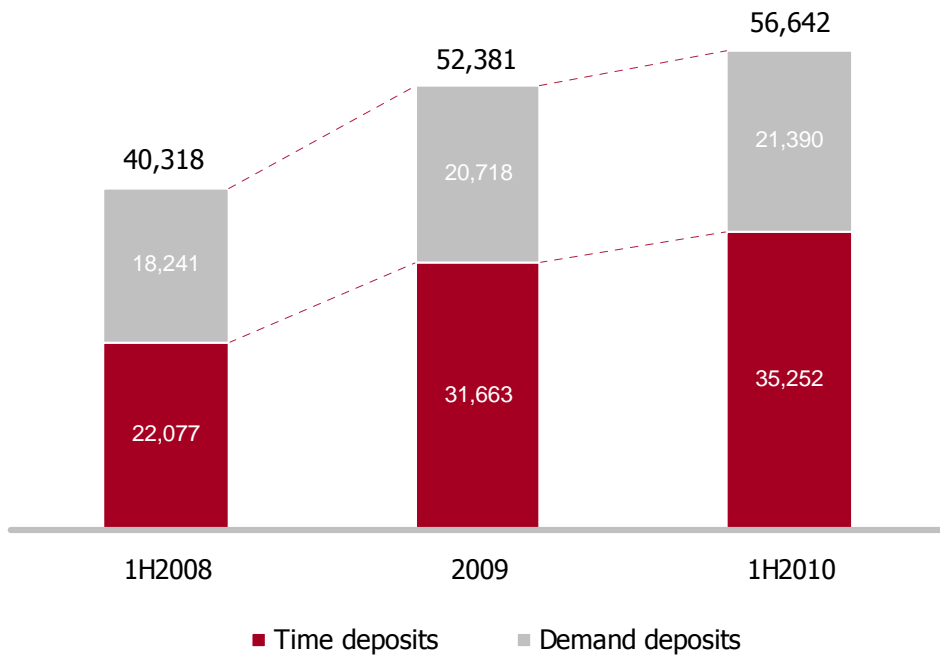
## Ability: Front Book spreads by segment May 10 vs Dec.07



# Managing spreads & margins: balancing growth into cheap and time deposits to offset current tough competitive environment and low interest rates

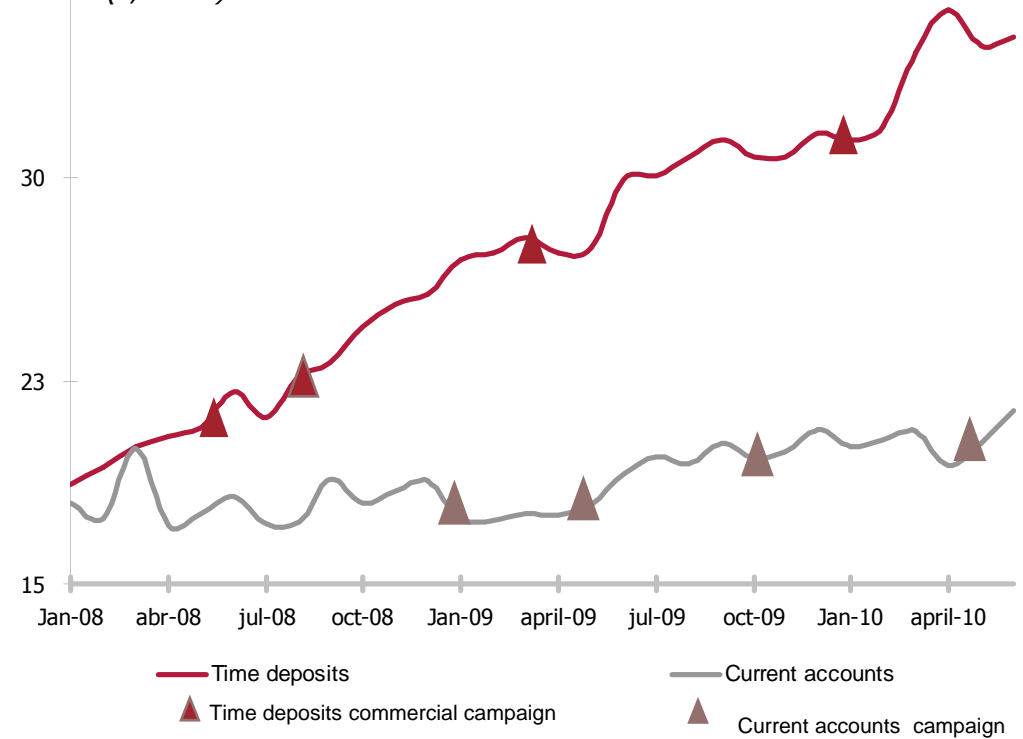
## Balanced deposit growth

(€, million)

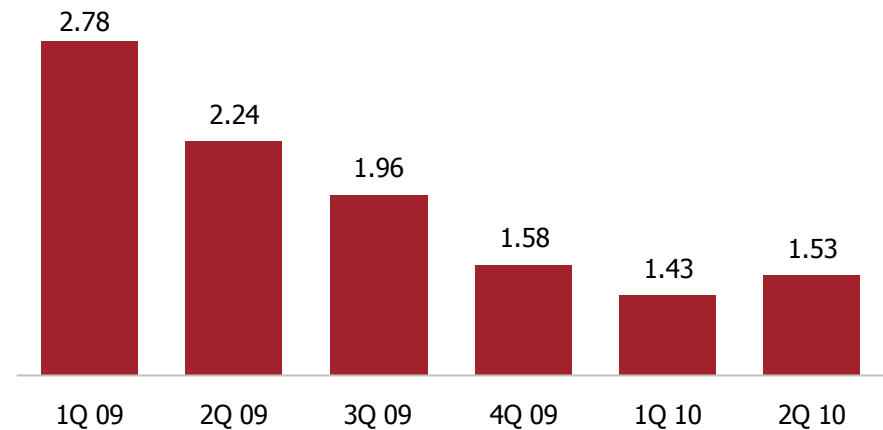


## Retail funds monthly evolution 2007-1H 10

(€, billion)

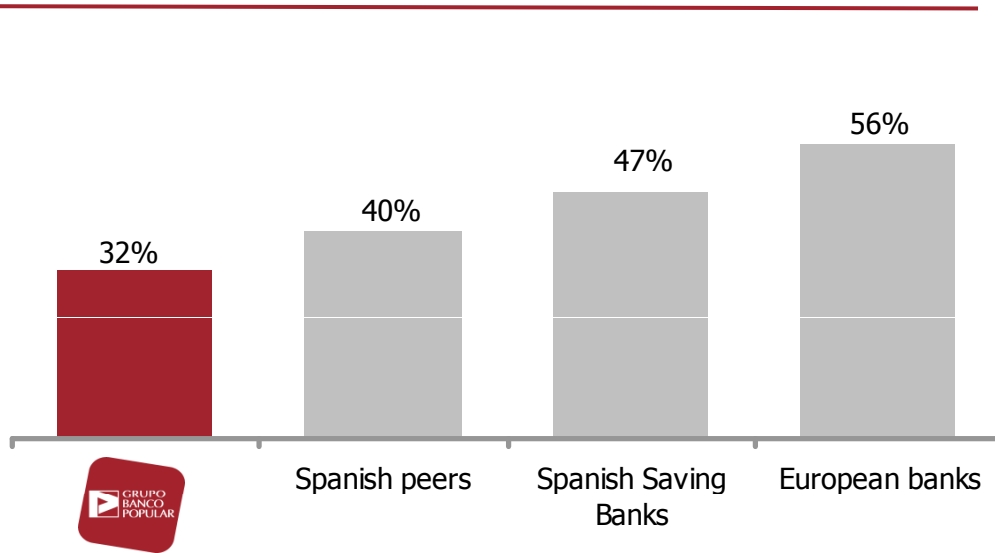


## Customer deposits cost evolution

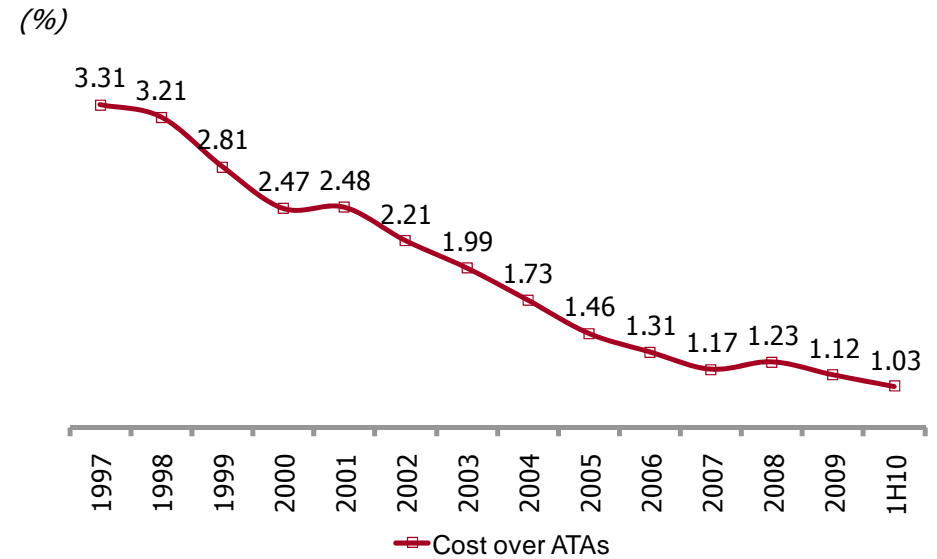


# Cost control: embedded in our culture

## Cost to income ratio 1H10



## Banco Popular's costs as % of ATAs

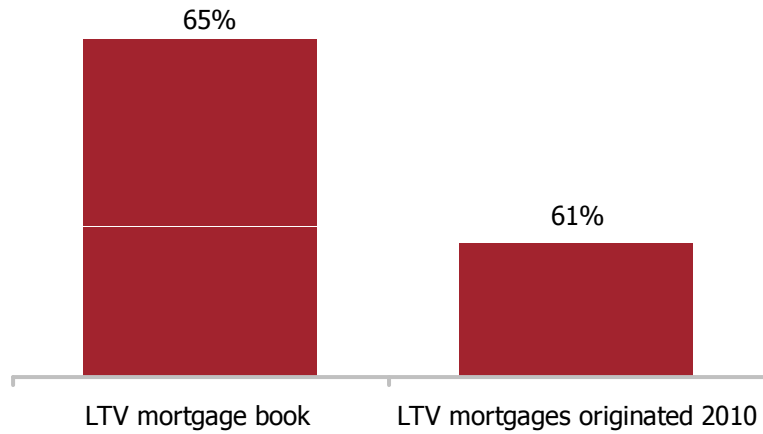


Source: BoS, Quarterly reports; Spanish peers: Santander Spain, BBVA Iberia, Banesto, Sabadell & Bankinter  
European banks: Credit Suisse

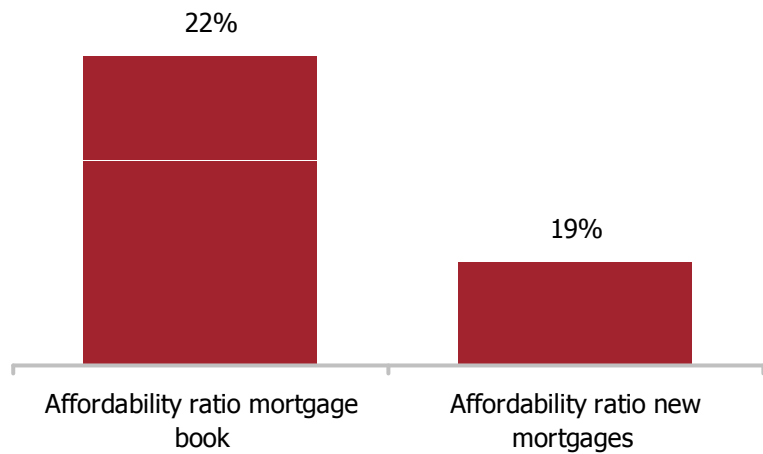


# Risk management: Very conservative new loan underwriting

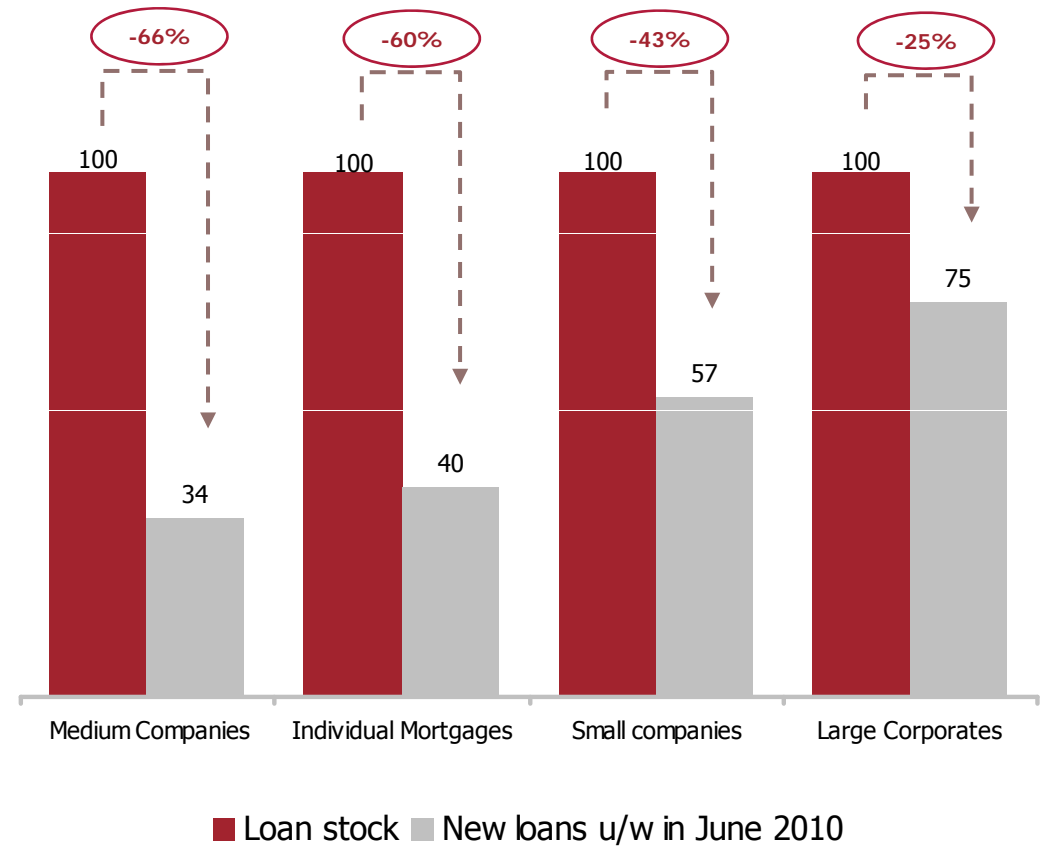
## Loan to Value residential mortgages



## Affordability ratio residential mortgages

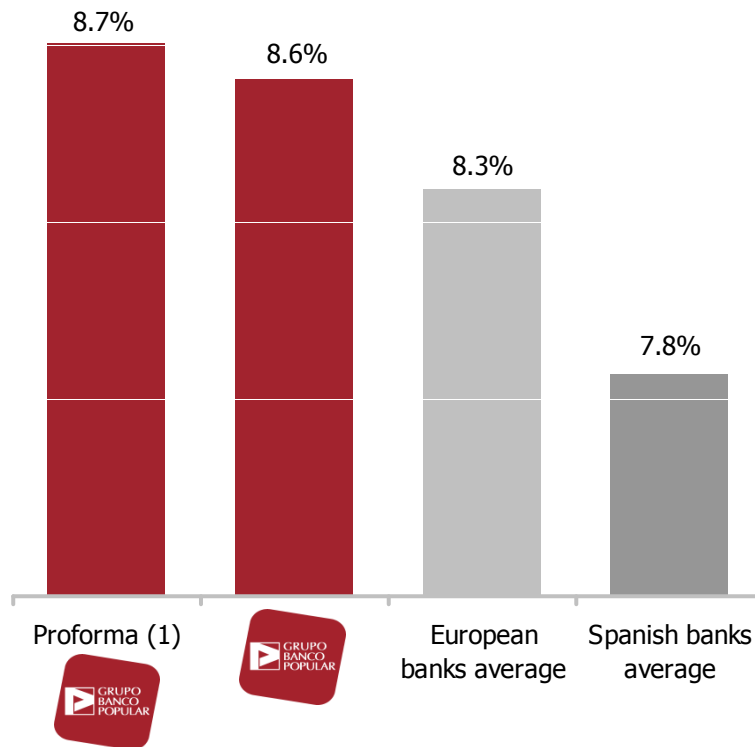


## Expected Loss new production vs. stock- (Index 100)



# Capital management: a solid core capital above our Spanish and European peers but also of higher quality with an expected negligible impact from new Basel III proposals

## Core capital vs. banking sector



## Very limited Impact from new Basel III proposals (\*)

- Few minorities (EUR33m or 4bp core capital )
- DTAs < 10% Core capital
- Financial Institutions stakes < 10% Common Equity
- DTAs + Financial Inst. stakes < 15% Common Equity
- AFS reserves- Expected limited impact
- Nil Market risk (0.48% of total RWA)
- Least Leveraged bank in Western Europe (14x TA/TE)



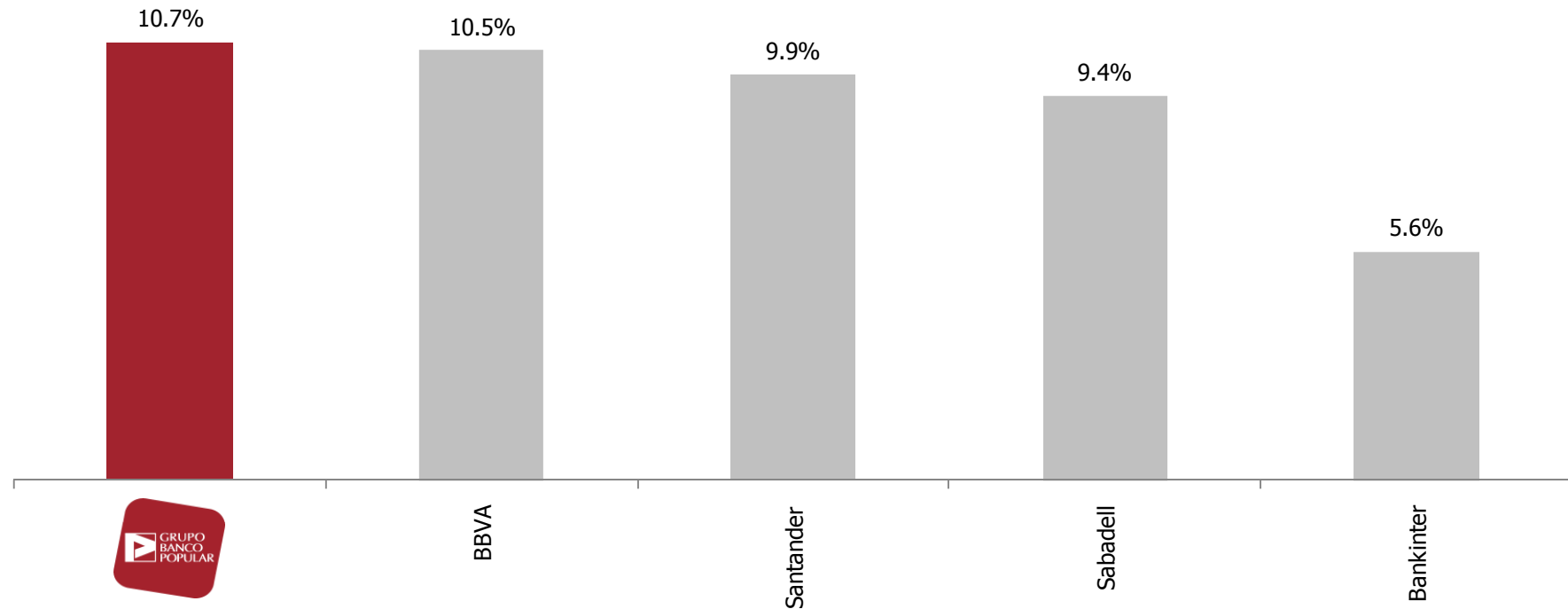
**Negligible impact on capital**



(1) 16 bp. From transaction with Crédit Mutuel  
 Source: European banks: Credit Suisse, July 2010. Includes banks that have received States' equity injections. Spanish banks: Quarterly reports 2Q 2010  
 \* Note: preliminary impact

# Capital management: building a model with buffers well above peers to protect capital through the cycles

Spanish listed banks' loss absorption capacity under the Stress Test's assumptions  
(% on exposure considered in the stressed adverse scenario + sovereign shock)

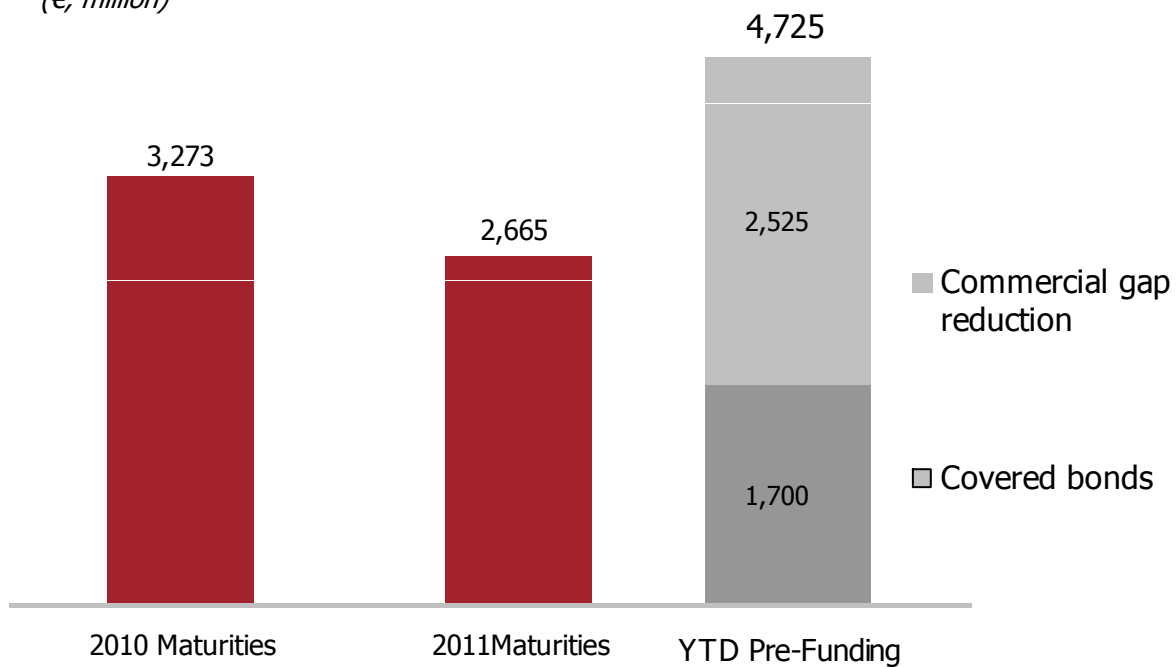


Source: CEBS, Bank of Spain, Banco Popular estimates

# All combined with a conservative liquidity management: we have already pre-funded all 2010 maturities and part of 2011 and we keep a strong second line of liquidity

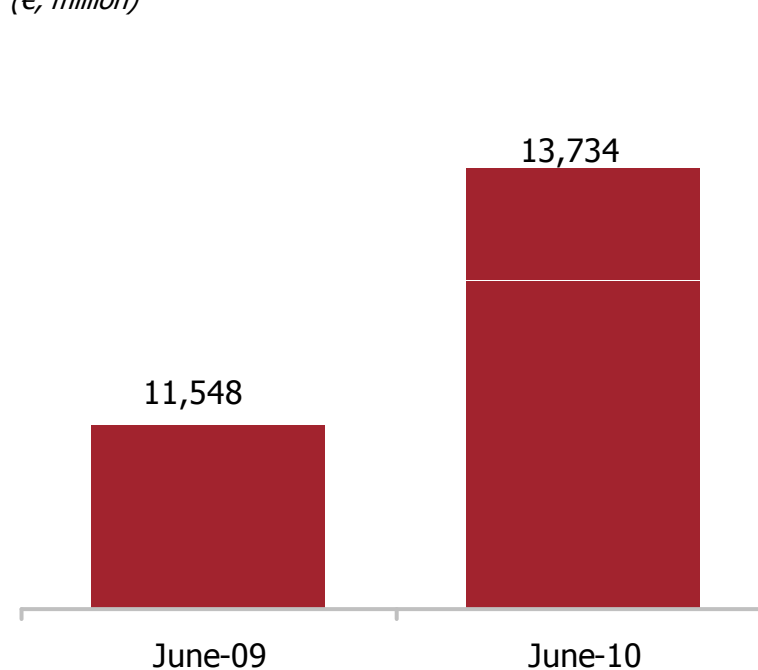
M&L Term maturities & funding evolution

(€, million)



Line of liquidity available at ECB (unutilized and after haircuts)

(€, million)



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## Conclusions

- **Still cautious with the economic & financial markets situation: preserving capital & reinforcing liquidity.**
- **Our business model has demonstrated its superiority in a very challenging environment: very low interest rates, severe economic and credit deterioration, closed debt markets and de-leveraging economy.**
- **And we have adapted it to the new environment over the last 2 years well ahead of peers and of the system: strong commercial gap reduction (€15 bn), increasing core capital by 34% and optimizing our branch network (-13% branches).**
- **Thus, a superior business model and our quicker adaptation to the new environment will allow us to improve profitability, focus on profitable growth and exploit future market opportunities while c.50% of the market embarks upon consolidation.**



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