

Interview with the Chairman, Pedro Guerrero

How would you sum up the year 2014 in macroeconomic terms?

The economic situation in Spain was much better in 2014 than in the previous few years.

However, internationally the panorama was mixed.

The US economy grew by more than 2% for the third year running and returned to pre-crisis levels of employment, becoming the main driver of the world economy.

The situation was very different in the emerging countries which, with some positive exceptions such as India, had a year of serious upheaval as a result of significant internal imbalances, large fiscal deficits, the depreciation of their currencies and above all the drastic fall in commodity prices. Even China was not as vigorous as before.

The euro zone for its part is suffering a marked slowdown, affected by Germany's loss of momentum, the lack of reforms in countries such as Italy and France and the deleveraging process which is still ongoing throughout Europe. For some months now the spectre of deflation has been threatening the economic recovery, and has forced the ECB to adopt a highly expansive monetary policy, which includes the recent

approval of a programme of purchases of public debt for an amount of more than a trillion euros. These exceptional measure should help to reactivate the economy of the zone, stimulating consumption and investment and making European companies' exports more competitive.

Spain, which will be one of the major beneficiaries of this plan, was the positive note struck in the euro zone in 2014. In the past few quarters Spain's GDP has grown faster than that of our European neighbours. The main macroeconomic indicators have shown positive trends: the balance of payments has performed well thanks to the increase in exports and the fall in oil prices; the public deficit has been reduced; consumption and investment, especially in capital equipment, has revived... And, more importantly, the labour market is recovering, as is reflected by the 417,000 new Social Security registrations in 2014.

This context, which should help to reactivate demand for borrowing and to reduce non-performing loans and provisions, should be good for banks' profitability.

On the other hand, their margins will come under pressure from low interest rates and fierce competition.



**How do you see the economy developing in 2015?
Is it too soon to talk of a definitive recovery?**

After five consecutive quarters of growth and six of declining unemployment rate, we can affirm that the Spanish economy has left the recession behind. There are sufficient reasons for looking at the near future with optimism, and I am confident that Spain's GDP will grow in 2015 by more than 2%, in line with the forecasts of the main institutions and analyst firms. Apart from that of the United States, Spain's is the only major economy to have seen its outlook upgraded by the IMF.

We are reaping the fruits of the structural reforms (although much work remains to be done on them), the clean-up of the financial sector and the strenuous efforts made by businesses and families to improve competitiveness and correct the serious imbalances of the past. As if this were not enough, we have also encountered some unexpected allies, in the form of the drastic fall in the price of oil; the ECB's stimulus plan, which has brought financing costs down to unprecedented levels; and the depreciation of the euro, which helps stimulate exports from the euro zone to the rest of the world. Prospects are frankly positive, although there are some uncertainties, as a result of the mountain of public and private sector indebtedness, the high rate of unemployment and the problems being suffered by both the major European and the emerging economies.

What would you say were the most important milestones of 2014 for Bankinter's shareholders?

Firstly, I should like to highlight the outstanding results obtained by Bankinter in the stress tests to which the ECB and the European Banking Authority subjected European Union banks with assets in excess of €30 billion.

This is the first time an analysis of this rigorous and exhaustive nature has been carried out on all European banks as a whole, and it represents the starting point for the projected Banking Union.

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In the most adverse scenario of this exercise, which assumes a 1% contraction in Spain's GDP in 2015 and an unemployment rate of 27.1% in 2016 (i.e. a highly improbable scenario), at the end of the period Bankinter would have a CET 1 capital ratio of 10.99%, double the minimum of 5.5% required by the regulators in order to pass the test. This is the best score obtained by any listed Spanish bank, and places us among the most solvent institutions in Europe.

In the AQR (Asset Quality Review), a prior step to the above-mentioned exercise, Bankinter was one of the few institutions that did not need to make additional provisions from 2014 results.

Our solvency has also been confirmed by the rating agencies. Standard and Poor's increased our rating on two occasions during 2014 (which is something really exceptional), allowing us once again to be classified as 'investment grade'.

Naturally these events are reflected in the market and in Bankinter's financing capacity.

On 27 January 2015 we issued €1 billion of mortgage covered bonds, at long term (ten years), at an IRR of 1.1%, 34 basis points below the interest rate on Spanish government bonds at the same term at that date. The issue was heavily over-subscribed.

The second thing I would like to highlight, though just as important, is our profit and loss account.

Results for 2014 are the best in the history of Bankinter. Admittedly net profit for 2007 was higher in absolute amount, but in that year we had a huge exceptional item as a result of the sale of 50% of our life insurance company.

The most important thing about the results for 2014 is their quality. The CEO will comment on the results in more detail, but I should like to

stress that there are no exceptional items of any kind, that net gains on financial transactions are very moderate and sustainable, that by far the greater part of results is obtained from customer business, and that our ALCO portfolio averaged less than €5 billion during the year, i.e. somewhat more than our equity, which is in line with the technical recommendation for hedging the interest rate risk. It is a portfolio of very similar size to the one we had in the years before the crisis.

The quality of the results and the vigorous growth in customer activity and in all lines of revenue, as well as the more favourable Spanish economic environment, which suggests a lower cost of non-performing loans in 2015, makes it very likely that in this year Bankinter's results will once again increase significantly.

Another sign of the Bank's good progress is the fact that this year we have increased our workforce by 97 people in net terms, which is an increase of 2.37%.

The third milestone to highlight is our performance on the stock exchange during 2014. As a consequence of all the above, it was very positive. Our stock rose by more than 30%. After being the best bank share of the 49 included in the Eurostoxx 600 index in 2013, this past year we were second in Europe and once again the best Spanish credit institution in the IBEX 35.

Evidently the market is recognising the Bank's good performance.

Lastly, I should like to talk about the dividend. In the first quarter, Banco de España, Spain's central bank, exempted us from the limit of 25% of net profit which it had imposed generally on Spanish banks, and allowed us to reach 33.6%, in view of our solvency and business strength.

This is the percentage we have applied to payments (in cash, as is our practice) of the successive interim dividends made in 2014.

The limits established by Banco de España for distribution of dividends cease to be in force as a result of the approval by the Governing Council of the European Central Bank of its recommendation ECB/2015/2 on the distribution of dividends

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by credit institutions. Bankinter meets all the applicable capital requirements contained in this recommendation, and is classified as a category 1 institution.

Consequently the Board of Directors will propose to the General Meeting of Shareholders the distribution of 50% of the profit for the year in the form of a cash dividend, since it considers that this is a prudent policy which contributes to capital conservation and allows the Bank to maintain an appropriate level of solvency even in adverse economic scenarios, as was demonstrated in the recent stress tests. The complementary dividend proposed amounts to €69 million, meaning that the pay-out for 2014 will be 50%.

This marks Bankinter's fiftieth year in business. What are the main differences between banks' business now and that of fifty years ago?

Fifty years ago the Spanish banking system was radically different.

The sector was highly fragmented, with many banks (more than 200), most of which were very small and of very varied kinds (commercial, industrial, regional and local banks, savings banks, credit cooperatives, rural savings banks, state-owned banks, and so on). What is more, there was very little competition, since prices were regulated, the technological and financial levels were very low and contact with the outside world was almost non-existent.

Now, fifty years on, after many trials and tribulations, including the process of consolidation of the 80s and 90s and above all the recent terrible financial crisis, the panorama is completely different.

Very few banks remain, hardly a score of significant players, all of them very big, and two of them with a strong international presence. The market is very advanced technologically, operationally and financially as regards commercial banking, and competition is fierce.

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Only a few banks survived in this market -no more than twenty players are still competitive. There are all large companies, and two of them have a strong international presence. Currently, retail banking is a highly developed sector in terms of technologies, operations and financing, with implies fierce competition.

Now that the banking bail-out has been completed, the surviving institutions are solid and well capitalised, although in general they are still engaged in far-reaching restructuring processes, which is not the case of Bankinter.

Technology has brought big changes to the way banks operate. Telephone, internet and mobile banking, etc. have become very important, and in the case of Bankinter they have enabled us to gain an advantage, since as is well known we have always been at the forefront as far as innovation is concerned.

Moreover, in these times much more far-reaching changes are afoot, and we have to confront them. The rise of social media, the sophistication and ubiquity of mobile devices, the boom in big data, as well as the arrival of new players through the involvement of technological companies in the payments system and the phenomena known as crowdfunding or direct lending, are revolutionising the banking business.

And yet the basic principles of our business remain unchanged. Trust continues to be the raw material with which we work, and it is this principle in mind that we are committed to our duty of carrying out banking activities scrupulously, rigorously, ethically and responsibly, managing resources efficiently so as to be able to encourage lending, which is our ultimate objective. But always doing it in a responsible and prudent manner, never forgetting that we are merely the managers of the resources that our customers and shareholders entrust us with.

What is your assessment of the Bank's activity in the field of sustainability in 2014?

Very positive. Our investors, employees, customers and suppliers, and members of the non-profit and voluntary sector see Bankinter as a bank with integrity and values.

Our commitment to the various stakeholder groups finds expression in two ways.

One is an advanced and demanding policy of corporate governance involving compliance with all the recommendations of the Code of Best Practices.

The other is our Sustainability Plan, which is called “Noughts and Crosses” and is intended to align the business with the management of the three business dimensions: economic, social and environmental.

Under this plan, which has just completed its third year, we have carried out numerous initiatives aimed at making Bankinter a bank whose business model incorporates the social and environmental aspects associated with its activity. This is demonstrated by our inclusion once more in the Carbon Disclosure Project and in the FTSE4Good sustainability index, which recognises us as one of the international companies with the best conduct in environmental, social and governance matters.

Although all these actions are fully reported in the information on sustainability that has been made available to all shareholders, I should like to highlight some of them.

For example the 'Involved and Caring' programme, which after three editions is consolidating itself as a reference in the non-profit and voluntary sector; and the 'Adaptative' project, which started last summer and through which the Bank has equipped the National Hospital for Paraplegics in Toledo the most advanced technological systems in the field of distance training and adaptation to the new technologies for persons with spinal cord injuries. I would also mention that in 2014 we subscribed to the National Financial Literacy Plan of the AEB (Spanish Banking Association), developing an innovative teaching methodology for providing financial training to primary school pupils by means of a video game. More than 900 pupils from four schools in Madrid attended this course, which will be extended this year to ten more schools.

And what projects of the Bankinter Foundation for Innovation would you highlight from this past year?

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the Círculo de Empresarios (a leading business association) is seeking to help one hundred Spanish companies with annual turnover of between €25 million and €250 million to become major corporations, i.e. with an annual turnover of around €1 billion. At the end of November we presented the shortlist with the names of the first 15 companies chosen.

Cre100do.es was born out of the imperative need for the Spanish economy to have large companies.

If the best of our medium-sized companies were to become large companies, in accordance with the criteria referred to, the aggregate productivity

of the Spanish economy would grow by between 10% and 15% and nearly half a million direct jobs would be created for this reason alone.

But in order for there to be large companies, it is a sine qua non to also have an ecosystem that drives the emergence of a new generation of entrepreneurs. This is the objective of the Entrepreneurs programme. In the first year and a half of the programme's existence, the Foundation has analysed more than 850 different entrepreneurial projects and the Bank has invested in ten of them, becoming a "go-to" early-stage investor.

These initiatives, together with the rest of the Foundation's programmes (FTF (Future Trends Forum) and Akademia), enjoy enormous prestige, which transcends our borders. This is shown by the fact that the prestigious University of Pennsylvania, which has analysed nearly 7,000 think tanks from around the world has once again designated the Foundation as the best think tank in Spain and one of the world's 30 leading think tanks (ranked 26th, to be precise) in the field of science and technology.

For all these reasons we continue to have in the Foundation an emblem of the Bank's DNA: Innovation.