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Spanish Banks

Same Real Estate Assets, Different Valuations

- Industry Overview

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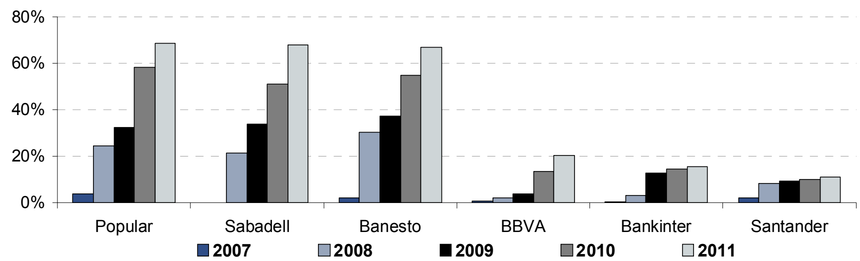
- **Uncertain Real Estate Asset Valuations** — Acquired real estate assets account for 20-80% of the equity value of the Spanish banks. Given this high exposure, valuation is key. The law that regulates the valuation of RE assets in banks leaves the door open to very different valuations. Appraisal updates can take up to five years. Given this situation we could find cases where identical assets have different valuations within the same institution. The impact for the Spanish banks we cover could be significant.

- **New Provisioning Rules Impact** — Earlier this month the Spanish Government announced a new provisioning law targeting real estate exposures. The impact of the provisions is significant and is likely to lead some institutions to report losses in 2012. In our view, Popular is the most affected by the new law on a relative basis (as a % of total assets and a % of pre-provision profit). Popular and Banesto will fall into losses during 2012 after implementing the new provisioning rules, on our estimates.

- **Adjusting Estimates** — We adjust our models to incorporate: (i) the new provisioning law, (ii) the new real estate adjustments explained in this report, and (iii) the LTRO benefit. We cut our estimates for 2012, while increasing our EPS estimates for 2013-14. Popular and BBVA remain among our Least Preferred European Banks.

- **Remain Cautious** — We remain concerned about the Spanish banks sector despite the c13% YTD underperformance to the European banks index. Spanish banks trade at 1.0x PTBV 2012E, a 10% premium to the European banks sector. Santander (TP: €6.4 from €6.2) and BBVA (TP: €6.8) trade at a small premium in terms of PTBV but with a superior ROE, hence our Neutral ratings (2H). We keep our Sell ratings (3H) on Popular (TP: €2.6), Caixabank (TP: €2.6 from €2.7) Bankinter (TP: €3.4) and Sabadell (TP: €2.1). Our Neutral rating (2H) on Banesto (TP: €4.3 from €4.0) is also unchanged. For details on our target price changes, see page 15.

Figure 1. Spanish Banks — Acquired Real Estate Assets as % of Equity, 2007-2011 (%)



Source: Companies, Citi Investment Research and Analysis. Note: Includes foreclosures and asset purchases.

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Same Real Estate Asset, Different Valuations

The Spanish Government recently approved a new provisioning law for Spanish banks. The government estimated an impact at a system level of c€50bn of additional provisions. The key question mark that arises is if that €50bn will be: (i) additional capital or (ii) banks will transfer funds around the balance sheet to cover the deficit. €50bn represents 5% of GDP and below 3% of the Spanish system loans. We won't know if this amount is enough to cover all the real estate losses until the end of the crisis.

The new provisions are focused on developers' related loans and assets owned as of December 2011. The €50bn looks to us like a catch-up exercise. According to various press sources (eg CincoDias) the provisions for future foreclosures will also be increased. 2012 is expected to be a difficult year in terms of NPL entries. Between the new provisions to legacy assets and the increased provisions for new entries in 2012, we believe Spanish banks' profitability will be under significant pressure, particularly the smaller names.

While we see the new law as clearly positive, uncertainty still remains in terms of the valuation of the real estate assets in the balance sheets. Banks own €80bn of land and work in progress, but what is the underlying valuation of these assets? An asset exchange between a developer and a bank is a private agreement; it can be done at a price that differs significantly with the real value of the asset. The Spanish valuation law only applies to mortgage guarantees, technical reserves of insurers and the NAV calculations of mutual and pension funds.

Figure 2. Spanish Financial System — Exposure to the Developer Sector, June 2011 (€Bn)

	Exposure	Coverage
Problematic assets	**175**	
- Land and work in progress	80	31%
- Other problematic assets	87	27%
Non problematic	**148**	**0%**
Total Exposure	**323**	**16%**

Source: Ministry of Economy and Citi Investment Research and Analysis

Private agreements with inflated valuations might look good for banks in the short term given lower provisions, but in the long term they can turn expensive, given the regulatory changes. Additionally, higher prices might drive lower sales. Banks with potential higher valuations on real estate assets might have difficulty disposing of the assets given lower market prices. An inflated valuation over time, in the current cycle, becomes even more inflated. The profitability constraints that we have now compared to 12 months ago don't help either.

In this situation the less affected names should be those banks that have taken a prudential approach since the beginning of the crisis. Bankinter is a clear example of this.

Figure 3. Spanish Banks — Summary of Earnings Estimates and TP changes

Ticker	Current price	Rating		Target Price			EPS 2012E		EPS 2013E	
	As at 26/2/12	Old	New	Old	New	ETR	Old	New	Old	New
BBVA.MC	€6.77	2H	2H	€6.80	€6.80	6.6%	€0.80	€0.55	€0.82	€0.82
BKT.MC	€4.97	3H	3H	€3.40	€3.40	-28.4%	€0.40	€0.33	€0.42	€0.43
BTO.MC	€3.98	2H	2H	€4.00	€4.30	7.9%	€0.04	€-0.25	€0.46	€0.50
CABK.MC	€3.60	3H	3H	€2.70	€2.60	-21.3%	€0.33	€0.29	€0.33	€0.28
POP.MC	€3.05	3H	3H	€2.60	€2.60	-10.8%	€0.04	€-0.30	€0.23	€0.23
SABE.MC	€2.41	3H	3H	€2.10	€2.10	-10.1%	€0.04	€0.04	€0.14	€0.14
SAN.MC	€6.28	2H	2H	€6.20	€6.40	11.4%	€0.80	€0.80	€0.79	€0.86

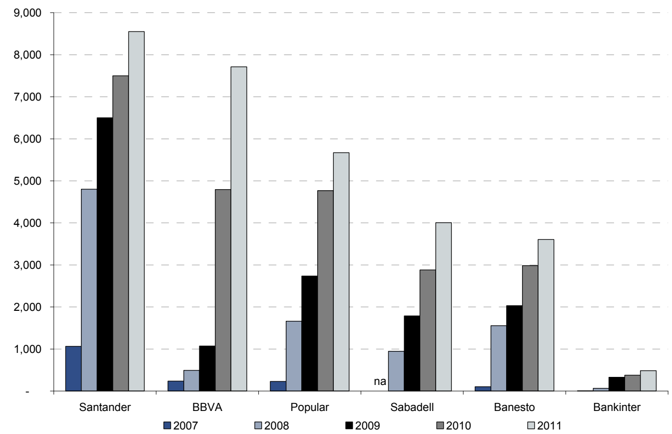
Source: Citi Investment Research and Analysis

Real Estate Valuations Matter

Acquired real estate assets have increased eightfold since 2007

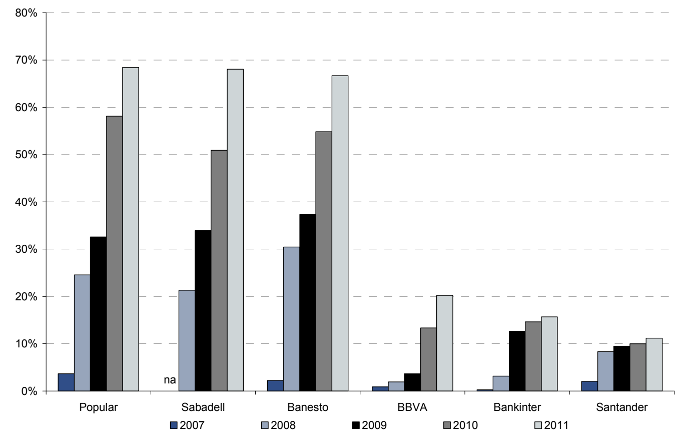
Since 2007 banks have increased significantly the amount of acquired real estate assets[1] in their balance sheets. When developers started to struggle with their financial commitments, banks started taking real estate assets in exchange for the loans. This way they could provide liquidity in exchange for an asset in an apparently healthy real estate market. In the charts below we show how all the banks have increased their real estate holdings significantly between 2007 and 2011. Given the size of the portfolios the valuation of those assets becomes key.

Figure 4. Spanish Banks — Total Acquired Real Estate Assets, 2007-2011 (Euros in Millions)



Source: Company data. Note: We include in acquired assets both foreclosures and asset purchases coming from real estate developers and dwellings

Figure 5. Total Acquired Real Estate Assets as a % of Total Equity, 2007-2011 (%)



Source: Company data and Citi Investment Research and Analysis. Note: We include in acquired assets both foreclosures and asset purchases coming from real estate developers and dwellings

The valuation framework under the existing Spanish law (also called "the ECO law") is mandatory under certain types of transactions. The acquisition of an asset from a bank for private purposes is not included as one of them. Banks can have three types of real estate assets: own usage, renting purposes and available for sale. We will focus in the available for sale assets.

We have checked with the banks we cover and all of them use ECO valuations when real estate assets enter the balance sheet. While the ECO valuations are only valid for 6 months, banks can keep assets in their books without updating prices for up to 5 years. The differences in the value can be significant.

The key error from the current crisis is the lesson learnt from the last real estate crisis

We believe that the high exposure to the real estate sector could be explained by what happened in the previous Spanish real estate crisis. In the early 1990s, Spain suffered a severe financial crisis mostly hitting directly the real estate sector. Most banks disposed of the real estate assets they had with significant losses. The companies investing during that crisis in the real estate sector made significant amounts of money. The largest real estate groups in Spain (ie. Metrovacesa, Vallehermoso, Urbis, etc) were originated by banks in those years.

[1] Note: We include in acquired assets both foreclosures and asset purchases coming from real estate developers and dwellings

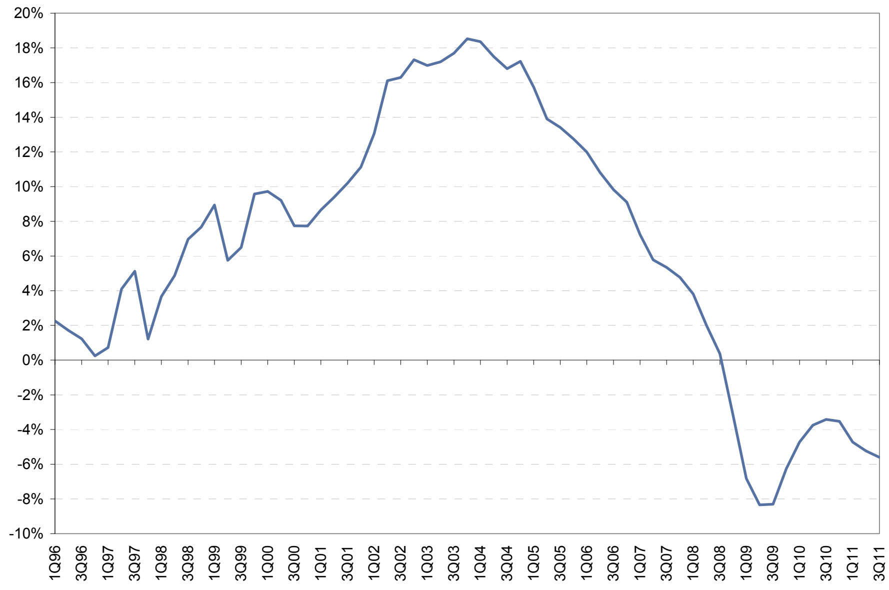
Most of the current banks' management teams were in their early days in the previous crisis. These bankers saw how others accumulated the profits of the recovery. As a result, we believe many executives thought that keeping the assets at high value in their books was not a problem, as the short-term price mismatch would be covered by a recovery in prices during the following years. In the current crisis we think it is very likely that real estate prices will not recover as fast, given the negative long-term economic outlook.

The ECO law, the IVS and the RICS provide a framework for RE valuation purposes

What the ECO law and other international standards provide are frameworks for valuation purposes. They take into account replacement cost, value in time, the usage of the assets and all the basic principles to make the valuation as fair as possible. In Spain the market normally uses the ECO framework while the IVS and RICS are used in some cases when international groups are involved in the transaction.[2]

In general, supply and demand have different pricing interests in the real estate market. In the case of banks' transactions with developers, we could find that the prices agreed are higher than the market might expect. This could happen because it is in the interests of both institutions to keep a high price, in one case to reduce the debt, in the other case to minimise the short-term losses. In this case both parties expect the revaluation of the asset to fill the value gap over time.

Figure 6. House Prices Growth (YoY), 1Q96-3Q11



Source: Ministry of Public Works and Transport

[2] For more details about the valuation regulation and the key international valuations standards please see the section "Appraisal Valuation Regulation".

IVS = International Valuation Standards

RICS = Royal Institution of Chartered Surveyors

Example of the Impacts of Different Valuation

When banks acquire real estate assets a key variable is the transfer price. As explained before, the asset valuation could be subject to different methodologies and also timing differences. In order to explain the potential accounting differences and P&L/balance sheet impact we have assumed two base scenarios: one where the bank has applied a prudential valuation and one with inflated valuation vs current market value.

The two differences between prudential and not prudential accounting are: (i) the timing of the disposal and (ii) the level of provisions taken

There are two main differences: the timing of disposal and the level of provisions:

- A prudent valuation minimizes the gap between demand and supply prices. A smaller price gap increases the chances of selling the assets, **reducing the selling period of the assets and the losses for the bank** given the market trends.
- Given the recently approved regulation**, an inflated valuation implies higher provisions** to be charged to the P&L now, when the P&L account is severely under risk. This difference is adjusted when the asset is sold.

The final overall cost is the same, assuming no fiscal effect (Figure 7), even if the timing of booking the losses/provisions is longer in the case of an inflated valuation vs a more prudent valuation. If we were to consider the fiscal effect, a prudential valuation provides an upfront tax benefit when the initial loss is assumed by the institution.

In the table below we outline the acquisition of a real estate asset from a developer/ client, the recognition of losses and provisions as well as the final disposal impact under each accounting treatment.

Figure 7. Example to Show the Different Outcome Depending on Accounting Style

	Inflated Value	Prudential Value
1) The bank acquires a real estate asset for €100, the current market value is actually €70		
Value of the asset	100	100
Realized losses * (A)	0	-30
Net value of the asset	**100**	**70**
2) The bank has not sold the asset. Spain new provisioning rules require higher provisions for the most problematic assets		
Value of the asset	100	70
Provisions** (B)	-80	-56
Net Value	**20**	**14**
3) The asset is sold for a price of €10, after a sharp decrease in market prices		
Original value of the asset	100	100
Total accumulated losses/provisions (A+B)	-80	-86
Net Value (Value of the Assets before disposal)	**20**	**14**
Disposal price	10	10
Loss on sale (C)	-10	-4
Final Total Cost (Losses + Provisions) (A+B+C)	**-90**	**-90**

Source: Citi Investment Research and Analysis. * Note: 0% tax rate assumed. **Assuming 80% provisioning.

Impact on Our Coverage Universe

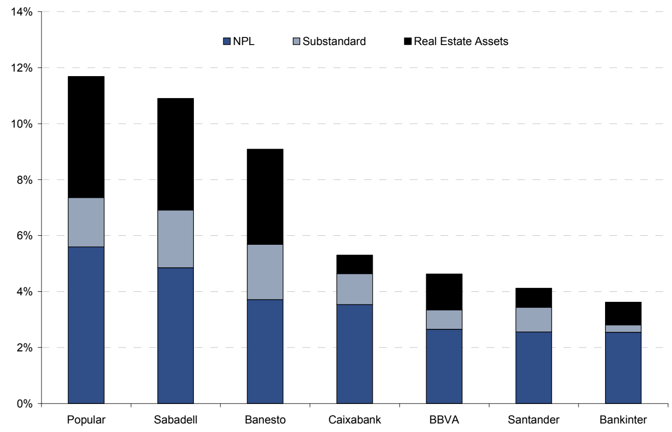
All the banks we cover are using the ECO valuation methodology

The intention of the analysis of this report was to assess if, among the different banks we cover, there were different valuations among similar real estate assets. We were expecting only some banks to use the ECO valuation but found that all the banks we cover use the ECO valuation done by independent appraisal companies, with the valuations updated every 2 to 6 years.

According to the Spanish banks we cover, the assets they have are fairly valued. So we wonder why are they not selling more of them? We think there are five likely reasons: (i) lack of commercial focus, (ii) lack of demand, (iii) carrying value in banks are still too high, (iv) banks expect prices to recover significantly or (v) management wants to amortise the losses over multiple years. According to data from the banks, asset sales really only began in 2011. Prices also fell more during this period, and at the same time the banks' improved their commercial focus.

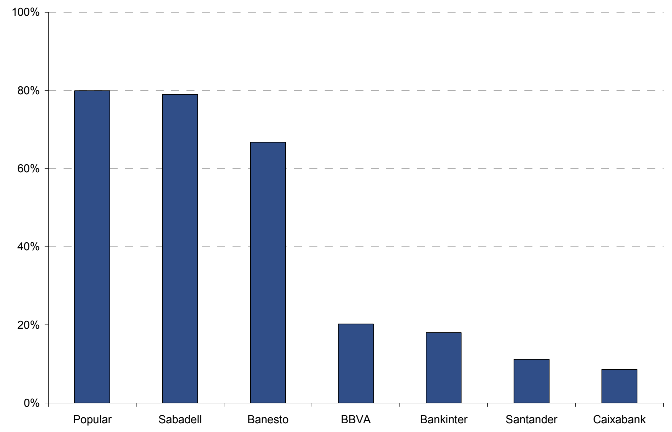
In most cases, real estate assets have been entered into the balance sheet to avoid becoming an NPL. If we want to analyze the real estate assets we need to put it in the context of a non-performing asset including NPLs, substandard loans (watchlist) as well as adding foreclosures. According to Figure 9 below the most exposed names to foreclosures (on a relative basis) are Popular, Sabadell and Banesto.

Figure 8. Spanish Banks — NPA* to Total Assets, 4Q11 (%)



Source: Company data and Citi Investment Research and Analysis. Note: NPA as a sum of NPL, Substandard and acquired real estate assets. Note: We include in acquired assets both foreclosures and asset purchases coming from real estate developers and dwellings

Figure 9. Spanish Banks — Acquired Real Estate Assets as % of Equity, 4Q11 (%)



Source: Company data and Citi Investment Research and Analysis. Note: We include in acquired real estate assets both foreclosures and asset purchases coming from real estate developers and dwellings

Given the lack of information on acquired real estate assets from the banks in our coverage universe we could consider for our analysis four different ways to adjust real estate valuations:

- % of lending exposure to developers.
- Exposure to real estate assets on an absolute and relative basis.
- % of land over total assets.
- Data from comparable banks.

Better disclosure, better assets?

However, we did find some additional information on acquired real estate assets in the 2011 annual reports of Banesto and Bankinter, which other banks do not provide. These two banks provide more data than the standard template provided by the Bank of Spain. This disclosure makes us more comfortable regarding any potential impact on the real estate provisions for these two banks under the new laws.

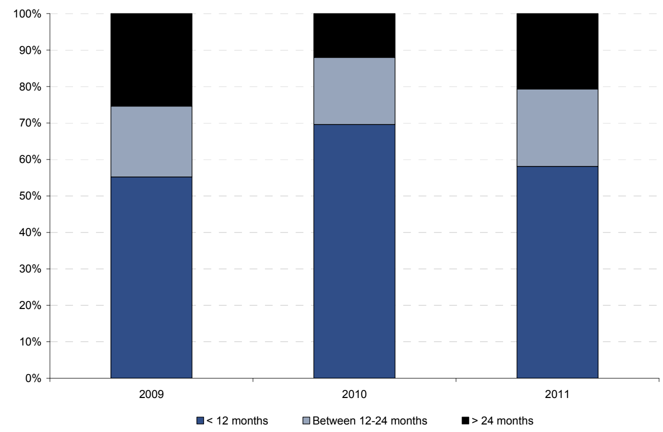
Banesto provides the accounting and appraisal value of the assets in the last two years. Additionally, it provides the vintage of the appraisal. Bankinter provides what percentage of assets comes from corporate and from the retail activities. It also provides the duration of the assets on balance sheet.

What Bankinter data tells us is that the amount of assets that remain in the balance sheet for more than 12 months has gone from c80% to c60% a year ago. This implies that Bankinter is selling more. In the case of Banesto, the information shows how the percentage of appraisals not updated in the last 24 months is around one third of the total.

Banesto argues in its annual report that "practically all the assets" are valued with the ECO valuation methodology

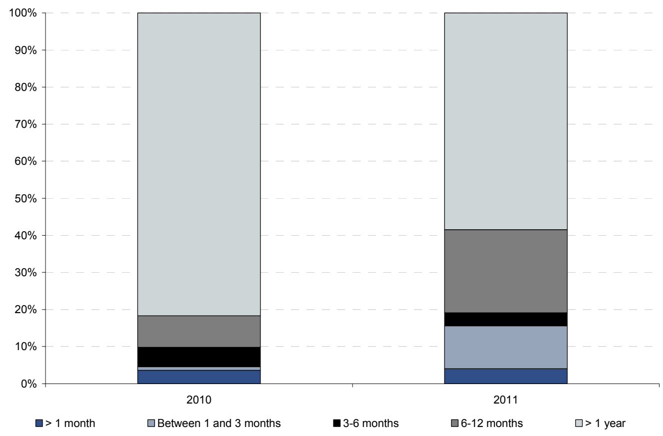
In the Bankinter annual report, the bank highlights how all the acquired real estate assets have been valued through the ECO regulation. In the case of Banesto, it argues that "practically all the assets" have been valued through the ECO valuation, however, this implies that other valuation methodologies have been used.

Figure 10. Banesto — Real Estate Assets per Vintage of Appraisal, 2011 (% of total)



Source: Citi Investment Research and Analysis

Figure 11. Bankinter — Real Estate Assets per Vintage of Consolidation, 2011 (% of total)



Source: Citi Investment Research and Analysis

We have undertaken a stress test to asses the impact of adjustment valuations for different vintages. For our analysis we use Banesto as a proxy for the rest of the banks. The key assumptions of our analysis to estimate the reduction in prices for the different banks are the following:

- Same split by type of asset as per latest data available.
- Same split of assets in terms of vintage of the appraisals as Banesto in 4Q11.
- We apply a haircut to the valuations depending on the type of asset and the number of years the asset is on balance sheet (see Figure 12).

Figure 12. Stress Test — Haircut Assumptions (%)

	< 12 months	Between 12-24 months	> 24 months
Finished buildings	10%	15%	20%
Under construction	15%	25%	35%
Land	15%	30%	45%

Source: Citi Investment Research and Analysis

We know from official statistics that house prices have fallen c17% from peak levels in early 2008[3]. As per Figure 12 our numbers assume a higher impact for riskier assets.

The stress test impact for Santander, BBVA and Bankinter is less significant compared to other banks

The result of our stress test (level of haircut) shows a small impact for Santander, BBVA and Bankinter. For Popular, Sabadell and Banesto it is significantly higher. However, the absolute haircut numbers don't seem that big according to Figure 13.

Figure 13. Spanish Banks — Stress Test on Real Estate Assets (€ mn)

	Acquired RE Assets (Gross)	Haircut (pre tax)	Haircut as % of Value	Haircut as % of BV
Santander	8,552	1,647	19%	2%
Bankinter	484	88	18%	3%
BBVA	7,714	1,630	21%	4%
Banesto	3,607	708	20%	13%
Sabadell	4,006	781	19%	13%
Popular	5,668	1,152	20%	14%

Source: Citi Investment Research and Analysis

Figure 14. Spanish Banks — Real Estate Assets Split (% of total)

	Santander	BBVA	Popular	Bankinter	Banesto
Finished buildings	44%	28%	32%	46%	40%
Under construction	6%	5%	15%	32%	8%
Land	50%	67%	53%	21%	52%
Total	**100%**	**100%**	**100%**	**100%**	**100%**

Source: Citi Investment Research and Analysis

In our base case explained above, the average level of haircut to the portfolios is c20%. If we do a sensitivity analysis assuming a range of haircuts between 10 and 30% of the current gross values, the impact varies significantly as shown in the tables below.

Figure 15. Spanish Banks — Sensitivity Analysis of Haircut to Gross Real Estate Assets (€ mn)

	10%	15%	20%	25%	30%
Santander	855	1,283	1,710	2,138	2,566
BBVA	771	1,157	1,543	1,929	2,314
Popular	567	850	1,134	1,417	1,700
Sabadell	401	601	801	1,002	1,202
Banesto	361	541	721	902	1,082
Bankinter	48	73	97	121	145

Source: Citi Investment Research and Analysis

Figure 16. Sensitivity Analysis of Haircut to Gross Real Estate Assets as a % of Book Value (%)

	10%	15%	20%	25%	30%
Santander	1.1%	1.7%	2.2%	2.8%	3.4%
Bankinter	1.6%	2.4%	3.1%	3.9%	5.4%
BBVA	2.0%	3.0%	4.0%	5.1%	6.1%
Banesto	6.7%	10.0%	13.3%	16.7%	20.0%
Sabadell	6.8%	10.2%	13.6%	17.0%	23.7%
Popular	6.8%	10.3%	13.7%	17.1%	24.0%

Source: Citi Investment Research and Analysis

[3] Ministry of Housing

Appraisal Valuation Regulation

The legal value of an ECO valuation expires after 6 months

In 2003, the Spanish Government approved a legal framework (law ECO/805/2003) on property appraisal regulations and certain rights for specific financial purposes. The ECO regulation represents a framework for the valuation; it provides the value of an asset at a certain moment in time. The legal value of an ECO valuation expires after 6 months. This law defines the most commonly used valuation methods in appraisals and is mandatory in Spain in four different cases:

- When guaranteeing a mortgage or for a loan guarantee.
- Hedging of technical provisions of insurance companies.
- Valuation of the assets of the real estate investment institutions.
- Valuation of the real estate assets of pension funds.

A bank's acquisition of a real estate asset from a developer would be considered a private agreement

The acquisition of a real estate asset from a developer by a bank would be considered a private agreement. There is no legal obligation to comply with the ECO law. The price is the result of negotiation between the two private parties and is the best reasonable proof of the value, according to the law[4].

Having said this, the valuation should be revised every 3 to 5 years if the changes in the value are small, according to the law CBE 4/2004 (Article 34); there are no comments about valuation revisions if there are big changes in the value.

Additionally, there are other valuation methodologies and frameworks that are commonly used in the Spanish real estate market, the key two are:

- **IVS (International Valuation Standards) –** The most widely known framework internationally. Its regulation is published by the International Valuation Standards Council (IVSC), an independent body that sets global standards for valuation. The latest IVSC was published in 2011 (IVS-2011).
- **RICS (Royal Institution of Chartered Surveyors) –** International professional body for qualifications and standards in land, property and construction. Its guidelines are widely used in Europe, especially in the UK.

[4] The best proof of a reasonable valuation for this type of assets would be a private selling agreement between two non-related parties. Law CBE 4/2004 (Article 34, section c 5).

Solving the Valuation Difference Problem

We believe valuation differences should be adjusted to improve visibility in the Spanish banking system's balance sheet. While some may argue that the current provisioning law tries to tackle this issue, we disagree as the valuation of the real estate assets remain unchanged.

The recently approved law penalises prudent institutions

The recently approved law penalises those institutions that have been "fair" in the valuation of their assets, in our view, and is probably too aggressive for those institutions with realistic valuations. Meanwhile, we believe institutions with inflated valuations will still have very high valuations of these assets, even after the new provisions.

More standardised and updated valuations needed

However, we believe the new provisioning law with realistic and updated valuations could provide the necessary regulatory change to clean the real estate assets (not loans) for the system. As some institutions might not have realistic valuations more regulatory changes might follow in the medium term. To address this problem we see scope for three further regulatory changes:

- **Eliminate registration valuation as an alternative –** Most banks we have spoken with agreed that the registration valuations are too high and don't reflect the real value of the asset in most cases.
- **Provisions over the acquired RE assets allocated value –** In many cases, an asset is acquired after a negotiation or a legal process as a payment of a loan. This entry justifies the usage of a new appraisal that in some cases is used to increase the value of the assets so there is no accounting loss. Provisioning for the value of the loan or establishing a minimum would avoid inflated valuations.
- **Mandatory and more frequent ECO valuation for all assets –** Currently the ECO appraisal valuation is not mandatory for assets acquired from a private agreement between two parties. Banks should be obliged to do so, we believe, unless the asset was used for the bank's own purposes. We would also recommend minimizing the period for updates in valuations to 12-24 months maximum. The high cost of recurring appraisals should accelerate the disposal of the assets from banks given the high maintenance cost.

The current regulatory environment could create situations where the valuation of an asset on a bank's balance sheet is unclear, as it is possible to get different valuations for the same assets, even within the same institution. Differences in timing of the acquisition and the lack of revaluations explain these problems.

Impact of New Provisioning Rules

On 2 February the Spanish Finance Minister Mr. Luis de Guindos presented the key lines of a new provisioning law to be applied to developers' exposure to banks (see *Spanish Banks New Financial Reform Guidelines, 2 February 2012*). The law was published on 4 February and the banks starting disclosing their plans to tackle the new provisioning gap.

We consider the recent law to be a catch-up exercise and only affects the back book

However, we consider the recently approved law to be a catch-up exercise, as it only affects loans and acquired real estate assets from developers owned as of December 2011. A second law, which will likely be applied from 2012 onwards to provisioning new loans and asset purchases, should be more aggressive than the one currently in place but not as aggressive as the law for legacy assets.

The coverage requirements under the new provisioning law are summarized in the table below from BBVA. While this law tackles a big part of the problem, the underlying valuation of the assets remains uncertain.

Figure 17. Spanish Banks — Real Estate Exposure New Coverage Requirements

	P&L				Capital	
	Land	Under development	Finished housing	Other	Land	Under development
Performing	7%	7%	7%	7%	0%	0%
Problematic assets						
- Doubtful	60%	50%	25%			
- Substandard	60%	24-50%	20%	24%	20%	15%
- Foreclosures	60%	50%	10-50%			

Source: BBVA

The new provisions represent c5% of Spanish GDP and less than 3% of the system loans

The key questions that arise regarding the government's estimate of a system-level impact of c€50bn in additional provisions are: Will it be (i) additional money or (ii) will banks move money around their balance sheets to cover the deficit? €50bn represents 5% of GDP and less than 3% of the Spanish system's loans. It doesn't look a big number but we won't know if this will be enough until the end of the crisis.

What we have seen so far is that the impact for Santander, BBVA, CaixaBank and Bankinter will be severely diluted due to the tax deductibility of the losses and the buffers currently in their books. The current stock of generic provisions, if any, and the excess regulatory capital can be used as buffers to offset the new law, minimizing its impact.

The largest institutions account for c50% of the total new provisions

In Figure 18 we see how the 11 largest institutions in Spain have more than 50% of the system's provisioning needs. This means that the smallest institutions have the other 50%. It is worth noting that one medium-size caja, Kutxabank (from the Basque Country), doesn't have any P&L impact, as it is already well covered.

In the case of banking groups with listed subsidiaries (ie. "la Caixa", Santander group) both entities have reported the estimated impact of the new law, and the impact on the holding group has been embedded in the impact on all its subsidiaries.

Figure 18. Spanish Banks — New Provisioning Rules Impact (€ mn)

	Provisions				
	Specific	Generic	Total P&L Provisions	Capital Buffer	Total Provisions
BFA *	2,547	849	3,396	1,674	5,070
- Bankia *	2,547	849	3,396	870	4,266
"la Caixa"	2,211	955	3,166	1,305	4,471
- CaixaBank	1,481	955	2,436	745	3,181
Santander	900	1,400	2,300	2,000	4,300
- Banesto	1,000	200	1,200	600	1,800
BBVA	2,220	590	2,810	1,200	4,010
Banco Popular	1,860	740	2,600	850	3,450
Banco Sabadell	1,207	400	1,607	798	2,405
NovaCaixaGalicia	1,205	395	1,600	740	2,340
Banco de Valencia *	617	206	823	428	1,251
Banca Civica	921	327	1,248	783	2,031
BMN	256	109	365	674	1,039
CajaEspaña	479	160	638	502	1,140
Ibercaja *	350	117	467	317	784
Unicaja *	na	na	427	264	691
Kutxabank	-	-	-	650	650
Bankinter	90	56	146	47	193
Subtotal	**15,183**	**6,410**	**21,593**	**12,232**	**33,825**
Total System	**25,000**	**10,000**	**35,000**	**15,000**	**50,000**
Subtotal as % of total	***61%***	***64%***	***62%***	***82%***	***68%***

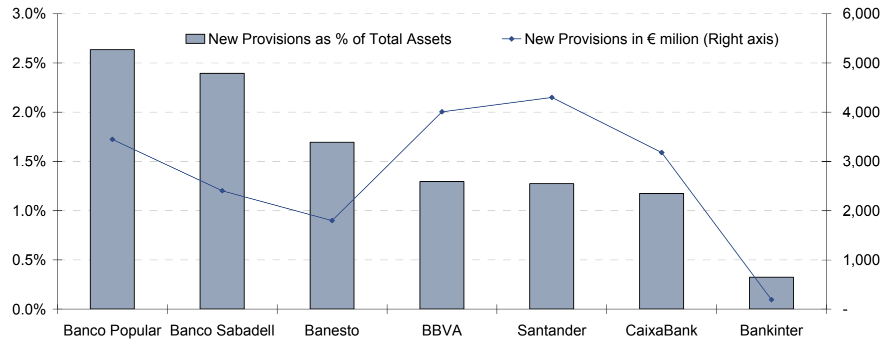
Source: Company data and Citi Investment Research and Analysis. * Note: We assume Bankia, BFA, Banco de Valencia, Caja España and Ibercaja split the P&L provisions 75% specific and 25% generic.

Popular and Sabadell the most affected names on a relative basis

If we focus on our coverage universe we see how the relative impact for Popular and Sabadell is significantly higher than for other banks. The new provisioning needed is more than 2% of the 2011 total assets of Popular and Sabadell.

For BBVA, Santander and Caixabank the amount stands below 1.5% of 2011 total assets. For Bankinter it is less than 0.5%.

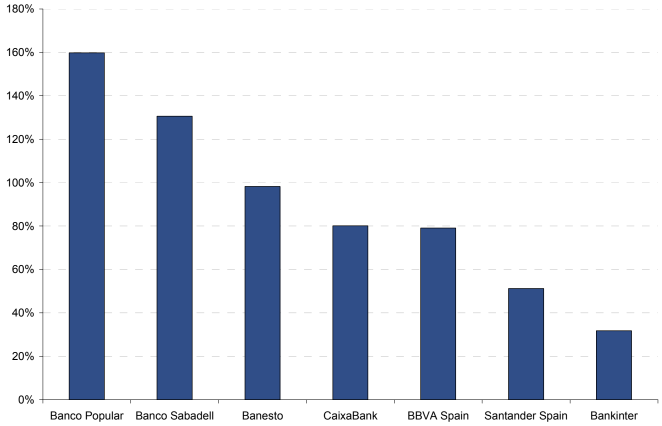
Figure 19. Spanish Banks — Relative New Provisioning Rules Total Impact, 2011



Source: Citi Investment Research and Analysis. * Note: We take only Spanish assets for Santander and BBVA. As a % of group assets it would represent 0.34% for Santander and 0.67% for BBVA.

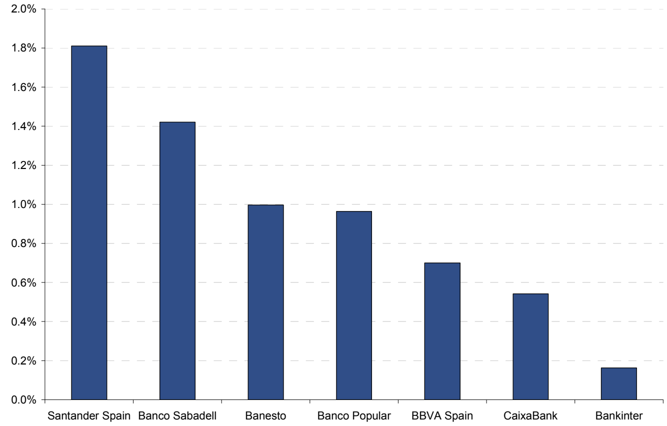
If we split the P&L impact and the capital impact, again, Popular is the most affected name. In the case of the P&L provisions, the impact is more than the 2011 pre-provision profit. The capital buffer impact for Sabadell stands above 140bps, for Popular it is almost 100 bps.

Figure 20. Spanish Banks — New P&L provisions as % of Pre Provision Profit, 2011 (%)



Source: Citi Investment Research and Analysis. * Note: We take only Spanish Pre Provision Profit for Santander and BBVA. As a % of group Pre Provision Profit it would represent 9.4% for Santander and 26.4% for BBVA.

Figure 21. Spanish Banks — New Capital Buffer as % of RWA, 2011 (%)



Source: Company data and Citi Investment Research and Analysis. * Note: We take only Spanish RWA for Santander (SAN Network and Banesto) and BBVA (estimated). As a % of group RWA it would represent 0.35% for Santander and 0.36% for BBVA.

NPL Growth Estimates

NPLs not expected to peak in 2012 or 2013

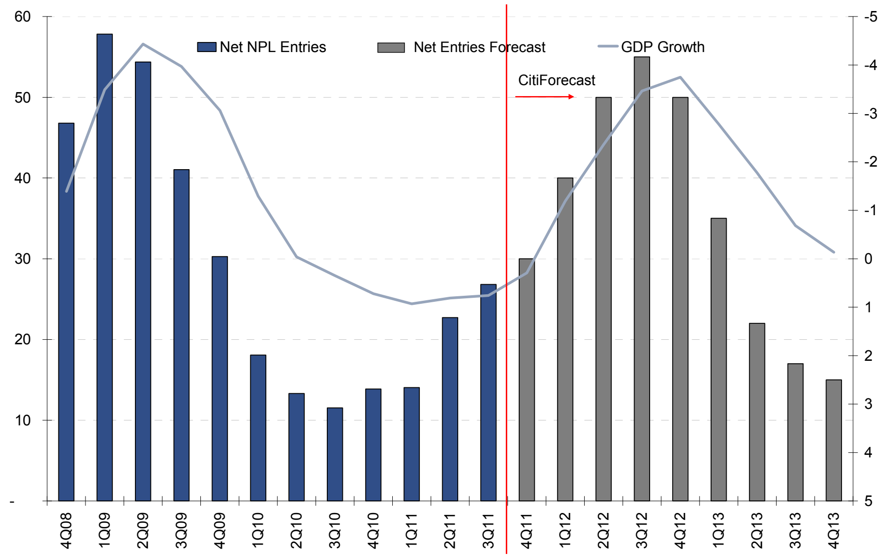
The Bank of Spain held a presentation in Madrid on 4 February explaining the key details of the new provisioning law. One of the most interesting points introduced in the presentation was a chart showing the correlation between the YoY increase in NPLs with GDP growth (inverted). We replicate the chart below but include Citi economists' 2012 and 2013 GDP forecast, including an estimate of NPL growth for the next eight quarters on this basis.

Using Bank of Spain analysis and Citi macro forecasts the NPL stock is expected to grow in 2012 and 2013, which we believe looks very likely. What is also relevant is that under our macro forecasts a second wave of NPLs will be of a similar size to that suffered in late 2008 and early 2009.

NPLs between 2011 and 2013 could double

However, while we think the chart is a good representation of the trend, the actual numbers look high to us, as they imply NPLs would double between the beginning of 2012 and the end of 2013. This looks aggressive if we don't assume a double dip in the Spanish economy. The difference is due to the fact that the chart uses net entries, it doesn't adjust for foreclosure entries, write offs and recoveries.

Figure 22. Spanish System NPLs — System NPLs and Annual GDP Growth, 2007-2013E (€ bn, %)



Source: Bank of Spain and Citi Investment Research and Analysis

Change of Estimates

LTRO benefit to benefit NII, 2012 numbers affected by new real estate provisions

We adjust our models to reflect: (i) the new provisioning law; (ii) the new real estate adjustments explained in this report; and (iii) the LTRO benefit. The impact of the new provisioning law, on our estimates, will see Banesto and Popular record losses in 2012. Caixabank numbers are cut mainly due to reflect Telefonica's dividend cut. For more details about our new forecasts please see Figures 23-38.

Banesto estimates have been adjusted to include the LTRO benefit and a higher level of provisions between 2012 and 2014, including the new law changes. We believe that while the bank will play the carry trade with the LTRO, and will use a significant part of this benefit to provision more during the period, normalizing the bank's cost of risk at a lower level.

Our target price for Banesto increases to €4.3 from €4 as a result of the increasing long term ROE from 6.6% to 8.2% to reflect lower long-term loan losses and higher NII. In our new estimates, we assume that Banesto will not pay a dividend in 2012. Banesto remains as our only Spanish midcap bank that is not Sell rated.

Figure 23. Banesto – Changes to Our Financial Forecasts, 2012E-14E (Euros in Millions)

	2012E Old	2012E New	% Chge	2013E Old	2013E New	% Chge	2014E Old	2014E New	% Chge
Net Interest Income	1,368	1,513	10.6%	1,340	1,483	10.6%	1,340	1,483	10.6%
Fee Income	616	616	0.0%	622	622	0.0%	628	628	0.0%
Trading Income	119	119	0.0%	119	119	0.0%	119	119	0.0%
Total Income	**2,099**	**2,244**	**6.9%**	**2,077**	**2,220**	**6.9%**	**2,084**	**2,226**	**6.8%**
Total Op. Expenses	(973)	(973)	0.0%	(977)	(977)	0.0%	(982)	(982)	0.0%
Operating Income	**1,125**	**1,271**	**12.9%**	**1,100**	**1,243**	**13.0%**	**1,102**	**1,245**	**12.9%**
Prov. Loan Losses (Net)	(737)	(1,650)	123.9%	(640)	(710)	11.0%	(611)	(674)	10.4%
Available Income to Shareholders	**26**	**(174)**	**-761.2%**	**313**	**346**	**10.7%**	**341**	**379**	**11.1%**
EPS	**0.04**	**(0.25)**	**-761.2%**	**0.46**	**0.50**	**10.7%**	**0.50**	**0.55**	**11.1%**

Source: Citi Investment Research and Analysis

In our view, Popular will benefit from the LTRO to a lesser extent than Banesto, using a smaller amount of the carry trade to provision more in 2012-14. On our numbers, the bank will fall into losses in 2012 given the new provisioning law, despite the liability management exercises that the bank wants to put in place enhancing the trading line.

We assume that Popular will execute all the new provisioning requirements during 2012, despite having the possibility to extend it to 2013 given the benefit of the Banco Pastor acquisition. Despite the changes to our estimates, our target price is unchanged at €2.60. We keep our Sell (3H) rating.

Figure 24. Popular – Changes to Our Financial Forecasts, 2012E-14E (Euros in Millions)

	2012E Old	2012E New	% Chg	2013E Old	2013E New	% Chg	2014E New	2014E New	% Chg
Net Interest Income	2,432	2,557	5.1%	2,359	2,481	5.1%	2,359	2,481	5.1%
Fee Income	787	787	0.0%	807	807	0.0%	834	834	0.0%
Trading Income	279	344	23.1%	282	348	23.4%	287	354	23.7%
Total Income	**3,548**	**3,738**	**5.4%**	**3,498**	**3,686**	**5.4%**	**3,531**	**3,721**	**5.4%**
Total Op. Expenses	-1,684	-1,851	9.9%	-1,633	-1,724	5.5%	-1,620	-1,620	0.0%
Operating Income	**1,864**	**1,887**	**1.2%**	**1,865**	**1,962**	**5.2%**	**1,912**	**2,101**	**9.9%**
Prov. Loan Losses (Net)	-1,546	-3,094	100.2%	-1,209	-1,408	16.4%	-908	-1,107	22.0%
Available Income to Shareholders	**61**	**-488**	**-901.3%**	**457**	**471**	**3.1%**	**860**	**852**	**-0.9%**
EPS	**0.04**	**(0.30)**	**-903.2%**	**0.23**	**0.23**	**3.5%**	**0.39**	**0.37**	**-4.6%**

Source: Citi Investment Research and Analysis

We had already included the LTRO benefit in our Bankinter estimates. In this report, we adjust Bankinter's the loan provisioning requirements given the more negative NPL outlook than initially forecast. However, the decrease in the real estate asset provisioning estimates largely offset the increase in the loan losses assumptions. As a result we increase our EPS estimates by 2-3% in 2013-14.

Figure 25. Bankinter – Changes to Our Financial Forecasts, 2012E-14E (Euros in Millions)

	2012E Old	2012E New	% Chg	2013E Old	2013E New	% Chg	2014E New	2014E New	% Chg
Net Interest Income	614	614	0%	601	601	0%	601	601	0%
Fee Income	201	201	0%	203	203	0%	205	205	0%
Trading Income	98	98	0%	101	101	0%	104	104	0%
Total Income	**1,181**	**1,181**	**0%**	**1,194**	**1,194**	**0%**	**1,221**	**1,221**	**0%**
Total Op. Expenses	-672	-672	0%	-672	-672	0%	-672	-672	0%
Operating Income	**509**	**509**	**0%**	**522**	**522**	**0%**	**549**	**549**	**0%**
Prov. Loan Losses (Net)	-174	-243	40%	-172	-184	7%	-172	-184	7%
Available Income to Shareholders	**194**	**158**	**-19%**	**205**	**210**	**3%**	**224**	**230**	**2%**
EPS	**0.40**	**0.33**	**-19%**	**0.42**	**0.43**	**3%**	**0.43**	**0.44**	**2%**

Source: Citi Investment Research and Analysis

Our estimates for Caixabank are not only affected by the provisioning law. Our estimate changes include: (i) the decrease of the Telefonica dividend, (ii) the LTRO benefit and (iii) the disposal of associates. As a result our estimates are cut by 10-14% in 2012-14.

Our target price for Caixabank is reduced to €2.60 from €2.70 given the cut in the DDM valuation, The change to the TP is only €0.10 as the static ROE and the discount to NAV valuation, the other two valuation methodologies used for the banking group, remain broadly unchanged.

Figure 26. Caixabank – Changes to Our Financial Forecasts, 2012E-14E (Euros in Millions)

	2012E Old	2012E New	% Chg	2013E Old	2013E New	% Chg	2014E Old	2014E New	% Chg
Net Interest Income	3,064	3,276	6.9%	3,029	3,240	6.9%	2,995	3,204	6.9%
Fee Income	1,546	1,546	0.0%	1,531	1,531	0.0%	1,516	1,516	0.0%
Trading Income	627	502	-20.0%	627	502	-20.0%	627	502	-20.0%
Total Income	**5,237**	**5,324**	**1.7%**	**5,187**	**5,272**	**1.6%**	**5,138**	**5,221**	**1.6%**
Total Op. Expenses	(3,136)	(3,136)	0.0%	(3,105)	(3,105)	0.0%	(3,136)	(3,136)	0.0%
Operating Income	**2,101**	**2,188**	**4.1%**	**2,082**	**2,167**	**4.1%**	**2,002**	**2,085**	**4.1%**
Income from Associates (equity method)	1,363	1,055	-22.6%	1,476	1,167	-20.9%	1,544	1,240	-19.7%
Prov. Loan Losses (Net)	(341)	(256)	-24.9%	(1,782)	(1,782)	0.0%	(1,594)	(1,594)	0.0%
Available Income to Shareholders	**1,352**	**1,211**	**-10.5%**	**1,477**	**1,273**	**-13.8%**	**1,613**	**1,412**	**-12.5%**
- EPS	**0.33**	**0.29**	**-10.5%**	**0.33**	**0.28**	**-13.8%**	**0.34**	**0.30**	**-12.5%**

Source: Citi Investment Research and Analysis

Our BBVA numbers are affected by the value uplift coming from the LTRO carry trade and the impact of the new real estate provisions. Our target price is unchanged at €6.80.

Figure 27. BBVA – Changes to Our Financial Forecasts, 2012E-14E (Euros in Millions)

	2012E Old	2012E New	Pct Chg	2013E Old	2013E New	Pct Chg	2014E Old	2014E New	Pct Chg
Net Interest Income	14,172	14,263	0.6%	15,319	15,415	0.6%	16,338	16,438	0.6%
Net Commission Income	4,632	4,632	0.0%	4,946	4,946	0.0%	5,193	5,193	0.0%
Trading Income	1,452	1,452	0.0%	1,547	1,547	0.0%	1,629	1,629	0.0%
Total Revenues	**21,658**	**21,749**	**0.4%**	**23,271**	**23,367**	**0.4%**	**24,695**	**24,795**	**0.4%**
Total Operating Costs	(10,900)	(10,900)	0.0%	(11,679)	(11,679)	0.0%	(12,373)	(12,373)	0.0%
Operating Income	**10,758**	**10,849**	**0.8%**	**11,592**	**11,687**	**0.8%**	**12,321**	**12,422**	**0.8%**
Provision for loan losses	(4,101)	(5,289)	29.0%	(4,257)	(4,357)	2.4%	(4,195)	(4,583)	9.3%
Net Attributable Profit	**4,057**	**2,824**	**-30.4%**	**4,527**	**4,517**	**-0.2%**	**5,078**	**4,867**	**-4.2%**
- Adj. EPS	**0.80**	**0.55**	**-30.4%**	**0.82**	**0.82**	**-0.2%**	**0.89**	**0.85**	**-4.2%**

Source: Citi Investment Research and Analysis

We adjust our Santander estimates to account for the new real estate provisions. Additionally, we revise our group estimates, including the disposal of the Colombian subsidiary (deconsolidated in 2H12) and lower real estate assets provisions in the long term. However, our target price for the bank increases to €6.40 from €6.20, less than the EPS changes in our numbers, due to the €2 billion impact in the book value of the new provisions (see Figure 18).

Figure 28. Santander – Changes to Our Financial Forecasts, 2012E-14E (Euros in Millions)

	2012E Old	2012E New	Chg	2013E Old	2013E New	Chg	2014E Old	2014E New	Chg
Net interest income	33,662	33,899	0.7%	36,765	36,912	0.4%	39,648	39,806	0.4%
Fees	11,389	11,353	-0.3%	12,353	12,275	-0.6%	13,053	12,976	-0.6%
Trading	2,610	2,603	-0.3%	2,752	2,738	-0.5%	2,808	2,794	-0.5%
Operating income	**48,084**	**48,278**	**0.4%**	**52,271**	**52,326**	**0.1%**	**55,901**	**55,968**	**0.1%**
Operating expenses	(21,957)	(21,899)	-0.3%	(23,969)	(23,844)	-0.5%	(25,397)	(25,272)	-0.5%
Gross operating profit	**26,127**	**26,380**	**1.0%**	**28,302**	**28,482**	**0.6%**	**30,504**	**30,696**	**0.6%**
Provisions	(12,219)	(13,524)	10.7%	(13,242)	(13,306)	0.5%	(14,065)	(14,124)	0.4%
Net profit	**7,283**	**7,297**	**0.2%**	**7,881**	**8,526**	**8.2%**	**8,752**	**9,442**	**7.9%**
EPS	**0.80**	**0.80**	**0.2%**	**0.79**	**0.86**	**8.2%**	**0.86**	**0.93**	**7.9%**

Source: Citi Investment Research and Analysis

Figure 29. Banesto — Group Profit and Loss Account, 2009-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Net Interest Income	**1,660**	**-4%**	**1,455**	**-12%**	**1,513**	**4%**	**1,483**	**-2%**	**1,483**	**0%**
Fee Income	617	2%	616	0%	616	0%	622	1%	628	1%
Trading Income	151	-4%	119	-21%	119	0%	119	0%	119	0%
Other	8	-33%	(4)	-154%	-4	0%	-4	0%	-4	0%
Total Income	**2,437**	**-3%**	**2,186**	**-10%**	**2,244**	**3%**	**2,220**	**-1%**	**2,226**	**0%**
Total Op. Expenses	-988	-1%	(964)	-2%	(973)	1%	(977)	0%	(982)	0%
Operating Income	**1,448**	**-4%**	**1,222**	**-16%**	**1,271**	**4%**	**1,243**	**-2%**	**1,245**	**0%**
Income from Associates (equity method)	53	-4%	49	-8%	24	-50%	25	3%	26	3%
Prov. Loan Losses (Net)	(572)	40%	(693)	21%	(1,650)	138%	(710)	-57%	(674)	-5%
Other	(172)	-39%	(448)	160%	110	NM	(70)	-30%	(63)	-10%
Income Before Tax	**757**	**-13%**	**130**	**-83%**	**-245**	**-288%**	**488**	**-299%**	**534**	**9%**
Taxes	(298)	-4%	(5)	-98%	71	-1453%	(141)	-299%	(155)	9%
- Implied Tax Rate	39%		4%		29%		29%		29%	
Net Income	**460**	**-18%**	**125**	**-73%**	**-174**	**-239%**	**346**	**-299%**	**379**	**9%**
Per share data (Euros)										
EPS	**0.67**	**-18%**	**0.18**	**-73%**	**-0.25**	**-239%**	**0.50**	**-299%**	**0.55**	**9%**
Adj. Cash EPS	0.67	-18%	0.18	-73%	-0.25	-239%	0.50	-299%	0.55	9%
Dividend	**0.35**	**-23%**	**0.18**	**-49%**	**0.00**	**-100%**	**0.25**	**na**	**0.28**	**12%**
Payout ratio	52.3%		98.9%		50.0%		50.0%		50.0%	
BVPS	**7.91**	**0%**	**7.86**	**-1%**	**6.87**	**-13%**	**7.12**	**4%**	**7.39**	**4%**
Number of shares (year end)	687.4		687.4		687.4		687.4		687.4	
Operating Ratios										
Net interest margin (CIRA Calculation)	1.39%		1.30%		1.46%		1.49%		1.52%	
Cost / income ratio	**40.6%**		**44.1%**		**43.4%**		**44.0%**		**44.1%**	
Provision charge / customer loans (bps)	76.1		101.2		253.8		111.5		108.0	
Non performing loans ratio	**4.08%**		**4.94%**		**5.90%**		**6.68%**		**6.58%**	
Coverage	54.0%		52.7%		73.4%		76.5%		89.4%	
Return on avg RWAs	0.69%		0.20%		-0.30%		0.62%		0.70%	
ROE	**8.5%**		**2.3%**		**-3.4%**		**7.2%**		**7.6%**	
Balance Summary										
Total assets	117,368	-4%	106,157	-10%	100,791	-5%	98,751	-2%	96,753	-2%
Gross customer loans	**75,169**	**-1%**	**68,465**	**-9%**	**65,004**	**-5%**	**63,688**	**-2%**	**62,399**	**-2%**
Net Customer Loans	75,744	-1%	69,225	-9%	65,764	-5%	64,449	-2%	63,160	-2%
Customer deposits	60,449	6%	51,954	-14%	52,993	2%	54,053	2%	55,134	2%
Loan to deposit ratio	125.3%		133.2%		124.1%		119.2%		114.6%	
Shareholders' equity	**5,439**	**0%**	**5,406**	**-1%**	**4,719**	**-13%**	**4,893**	**4%**	**5,082**	**4%**
Average shareholders' equity	5,435	-1%	5,522	2%	5,063	-8%	4,806	-5%	4,987	4%
Capital Ratios										
Core capital	5,398	3%	5,429	1%	4,742	-13%	4,915	4%	5,105	4%
Tier 1 capital	6,041	2%	6,187	2%	5,501	-11%	5,674	3%	5,863	3%
Risk-weighted assets	64,955	-5%	60,206	-7%	56,514	-6%	54,787	-3%	53,660	-2%
Core capital ratio	**8.31%**		**9.02%**		**8.39%**		**8.97%**		**9.51%**	
Tier 1 ratio	9.30%		10.28%		9.73%		10.36%		10.93%	
Total capital ratio	11.18%		11.54%		11.07%		11.74%		12.34%	

Source: Company reports, Citi Investment Research and Analysis

Figure 30. Popular — Group Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Net Interest Income	**2,452**	**-13%**	**2,087**	**-15%**	**2,557**	**23%**	**2,481**	**-3%**	**2,481**	**0%**
Fee Income	747	-2%	686	-8%	787	15%	807	3%	834	3%
Trading Income	199	-51%	129	-35%	344	166%	348	1%	354	2%
Insurance and Other	66	4%	49	-26%	49	0%	50	2%	51	3%
Total Income	**3,464**	**-15%**	**2,951**	**-15%**	**3,738**	**27%**	**3,686**	**-1%**	**3,721**	**1%**
Total Op. Expenses	-1,313	2%	-1,369	4%	-1,851	35%	-1,724	-7%	-1,620	-6%
Operating Income	**2,150**	**-22%**	**1,581**	**-26%**	**1,887**	**19%**	**1,962**	**4%**	**2,101**	**7%**
Income from Associates (equity method)	-1	NM	46	NM	51	10%	51	0%	51	0%
Prov. Loan Losses (Net)	-1,864	-13%	-1,690	-9%	-3,094	83%	-1,408	-54%	-1,107	-21%
Other	548	20%	507	-7%	507	0%	-24	-105%	-12	-50%
Income Before Tax	**833**	**-22%**	**444**	**-47%**	**-650**	**-246%**	**581**	**-189%**	**1,032**	**78%**
Taxes	-228	-22%	40	-117%	156	291%	-108	-169%	-177	65%
- Implied Tax Rate	27%		-9%		24%		19%		17%	
Net Income	**605**	**-22%**	**484**	**-20%**	**-494**	**-202%**	**473**	**-196%**	**855**	**81%**
Minority Interest	-14	1%	-4	-70%	6	-230%	-2	-136%	-4	75%
Discontinued Operations	0		0		0		0		0	
Available Income to Shareholders	**591**	**-23%**	**480**	**-19%**	**-488**	**-202%**	**471**	**-196%**	**852**	**81%**
Per share data (Euros)										
EPS	**0.44**	**-28%**	**0.35**	**-21%**	**-0.30**	**-188%**	**0.23**	**-177%**	**0.37**	**57%**
Adj. Cash EPS	0.44	-28%	0.35	-21%	-0.30	-188%	0.23	-177%	0.37	57%
Dividend	**0.31**	**0%**	**0.19**	**-38%**	**0.12**	**-37%**	**0.12**	**0%**	**0.18**	**50%**
Payout ratio	71%		55%		na		50%		50%	
BVPS	**5.11**	**-12%**	**5.06**	**-1%**	**3.23**	**-36%**	**3.60**	**11%**	**3.90**	**8%**
Number of shares (year end)	1,375	3%	1,400	2%	1,805	29%	2,206	22%	2,418	10%
Operating Ratios										
Net interest margin (CIRA Calculation)	1.89%		1.60%		1.78%		1.61%		1.66%	
Cost / income ratio	**38%**		**46%**		**50%**		**47%**		**44%**	
Provision charge / customer loans (bps)	190		171		266		125		101	
Non performing loans Ratio	**5.3%**		**6.0%**		**7.7%**		**8.3%**		**7.7%**	
Coverage	40%		35%		61%		60%		66%	
Return on avg Assets	0.5%		0.4%		-0.3%		0.3%		0.6%	
Return on avg RWAs	0.6%		0.5%		-0.5%		0.5%		0.9%	
ROE	**8.0%**		**6.8%**		**-7.6%**		**6.8%**		**9.8%**	
Balance Sheet Summary										
Total assets	130,140	1%	130,926	1%	155,981	19%	151,302	-3%	146,763	-3%
Gross customer loans	**98,213**	**1%**	**98,873**	**1%**	**116,420**	**18%**	**112,927**	**-3%**	**109,539**	**-3%**
Net customer loans	96,032	1%	96,771	1%	113,642	17%	110,066	-3%	106,593	-3%
Customer deposits	66,708	14%	59,085	-11%	76,022	29%	77,542	2%	79,093	2%
Loan to deposit ratio	144.0%		163.8%		281.9%		267.6%		254.0%	
Shareholders' equity	**7,027**	**-9%**	**7,091**	**1%**	**5,837**	**-18%**	**7,948**	**36%**	**9,429**	**19%**
Average shareholders' equity	7,387	2%	7,059	-4%	6,464	-8%	6,892	7%	8,689	26%
Capital Ratios										
Core capital	8,839	11%	8,853	0%	9,181	4%	9,395	2%	9,733	4%
Tier 1 capital	9,070	7%	8,853	-2%	9,181	4%	9,395	2%	9,733	4%
Total capital	9,520	7%	8,980	-6%	9,382	4%	9,597	2%	9,934	4%
Risk-weighted assets	93,747	1%	88,181	-6%	100,412	14%	97,400	-3%	94,478	-3%
Core capital ratio	**9.4%**		**10.0%**		**9.1%**		**9.6%**		**10.3%**	
Tier 1 ratio	9.7%		10.0%		9.1%		9.6%		10.3%	
Total capital ratio	10.2%		10.2%		9.3%		9.9%		10.5%	

Source: Company reports, Citi Investment Research and Analysis

Figure 31. Bankinter — Group Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Net Interest Income	550	-31%	543	-1%	614	13%	601	-2%	601	0%
Fee Income	196	-3%	199	2%	201	1%	203	1%	205	1%
Trading Income	120	36%	98	-19%	98	0%	101	3%	104	3%
Insurance and Other	225	55%	250	11%	269	8%	289	8%	311	8%
Total Income	**1,091**	**-11%**	**1,090**	**0%**	**1,181**	**8%**	**1,194**	**1%**	**1,221**	**2%**
Total Op. Expenses	-656	4%	-645	-2%	-672	4%	-672	0%	-672	0%
Operating Income	**436**	**-27%**	**445**	**2%**	**509**	**15%**	**522**	**3%**	**549**	**5%**
Income from Associates (equity method)	11	-32%	15	34%	15	0%	15	0%	15	0%
Prov. Loan Losses (Net)	-217	-2%	-158	-27%	-243	54%	-184	-24%	-184	0%
Other	-25	NM	-61	NM	-61	0%	-61	0%	-61	0%
Income Before Tax	**205**	**-41%**	**240**	**17%**	**220**	**-8%**	**292**	**33%**	**319**	**9%**
Taxes	-54	-40%	-59	8%	-62	4%	-82	33%	-89	9%
- Implied Tax Rate	27%		25%		28%		28%		28%	
Net Income	**151**	**-41%**	**181**	**20%**	**158**	**-13%**	**210**	**33%**	**230**	**9%**
Per share data (Euros)										
EPS	**0.32**	**-44%**	**0.38**	**20%**	**0.33**	**-14%**	**0.43**	**31%**	**0.44**	**1%**
Adj. Cash EPS	0.32	-44%	0.38	20%	0.33	-14%	0.43	31%	0.44	1%
Dividend	**0.16**	**-48%**	**0.19**	**21%**	**0.16**	**-14%**	**0.22**	**31%**	**0.22**	**1%**
Payout ratio	49%		50%		50%		50%		50%	
BVPS	**5.45**	**0%**	**5.63**	**3%**	**5.73**	**2%**	**5.98**	**4%**	**6.10**	**2%**
Number of shares (year end)	473		477		483		489		564	
Operating Ratios										
Net interest margin (CIRA Calculation)	1.01%		0.96%		1.06%		1.08%		1.11%	
Cost / income ratio	**60%**		**59%**		**57%**		**56%**		**55%**	
Provision charge / customer loans (bps)	51		36		59		46		47	
Non Performing Loan ratio	**2.8%**		**3.2%**		**3.9%**		**4.3%**		**4.3%**	
Coverage	67%		52%		48%		43%		42%	
Return on avg RWAs	0.48%		0.61%		0.56%		0.77%		0.85%	
ROE	**5.8%**		**6.9%**		**5.8%**		**7.4%**		**7.2%**	
Balance Sheet Items										
Total assets	54,025	-1%	59,491	10%	56,600	-5%	54,952	-3%	53,354	-3%
Gross customer loans	**44,162**	**4%**	**44,647**	**1%**	**42,478**	**-5%**	**41,241**	**-3%**	**40,041**	**-3%**
Net Customer Loans	41,868	5%	42,658	2%	40,445	-5%	39,225	-3%	38,082	-3%
Customer deposits	23,009	4%	24,244	5%	24,729	2%	25,224	2%	25,728	2%
Loan to deposit ratio	182.0%		176.0%		163.6%		155.5%		148.0%	
Shareholders' equity	**2,580**	**0%**	**2,685**	**4%**	**2,767**	**3%**	**2,922**	**6%**	**3,439**	**18%**
Average shareholders' equity	2,581	16%	2,632	2%	2,726	4%	2,845	4%	3,181	12%
Capital Ratios										
Core capital	2,094	6%	2,660	27%	2,692	1%	2,797	4%	2,912	4%
Tier 1 capital	2,301	0%	2,668	16%	2,700	1%	2,805	4%	2,920	4%
Risk-weighted assets	30,974	-1%	28,912	-7%	27,756	-4%	27,200	-2%	26,656	-2%
Core Capital Ratio	**6.8%**		**9.2%**		**9.7%**		**10.3%**		**10.9%**	
Tier 1 ratio	7.4%		9.2%		9.7%		10.3%		11.0%	
Total capital ratio	9.9%		11.5%		9.7%		10.3%		11.0%	

Source: Company reports, Citi Investment Research and Analysis

Figure 32. Caixabank — Group Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Net Interest Income	**3,418**	**3,170**	**-7%**	**3,276**	**3%**	**3,240**	**-1%**	**3,204**	**-1%**
Fee Income	1,406	1,562	11%	1,546	-1%	1,531	-1%	1,516	-1%
Trading Income & Other	826	627	-24%	502	-20%	502	0%	502	0%
Total Income	**5,650**	**5,359**	**-5%**	**5,324**	**-1%**	**5,272**	**-1%**	**5,221**	**-1%**
Total Op. Expenses	-3,366	-3,232	-4%	-3,136	-3%	-3,105	-1%	-3,136	1%
Operating Income	**2,284**	**2,127**	**-7%**	**2,188**	**3%**	**2,167**	**-1%**	**2,085**	**-4%**
Income from Investments & Dividends	729	913	25%	1,055	16%	1,167	11%	1,240	6%
Prov. Loan Losses (Net)	-1,456	-2,422	66%	-256	-89%	-1,782	596%	-1,594	-11%
Other	-146	541	NM	-1,500	NM	0	0%	0	0%
Income Before Tax	**1,411**	**1,159**	**-18%**	**1,487**	**28%**	**1,552**	**4%**	**1,731**	**11%**
Taxes	-199	-106	-47%	-276	161%	-279	1%	-319	14%
- Implied Tax Rate	14.1%	9.1%		18.6%		18.0%		18.4%	
Net Income	**1,212**	**1,053**	**-13%**	**1,211**	**15%**	**1,273**	**5%**	**1,412**	**11%**
Per share data (Euros)									
EPS	**0.36**	**0.29**	**-19%**	**0.29**	**1%**	**0.28**	**-5%**	**0.30**	**7%**
Dividend	**0.31**	**0.23**	**-26%**	**0.23**	**0%**	**0.23**	**0%**	**0.23**	**0%**
Payout ratio	86.3%	79.0%		78.3%		82.3%		77.0%	
BVPS	**5.82**	**5.01**	**-14%**	**4.62**	**-8%**	**4.64**	**0%**	**4.71**	**1%**
Number of shares (year end)	3,363	3,840		4,371		4,707		4,707	
Operating Ratios									
Net interest margin (CIRA Calculation)	1.28%	1.17%		1.22%		1.24%		1.27%	
Cost / income ratio	**59.6%**	**60.3%**		**58.9%**		**58.9%**		**60.1%**	
Provision charge / customer loans (bps)	77	130		14		101		93	
Non Performing Loan ratio	**3.59%**	**4.91%**		**6.22%**		**6.79%**		**6.45%**	
Coverage	71.0%	60.1%		56.7%		59.7%		70.6%	
Return on avg RWAs	0.79%	0.73%		0.90%		0.99%		1.10%	
ROE	**6.2%**	**5.4%**		**6.1%**		**6.1%**		**6.4%**	
Balance Sheet Items									
Total assets	273,067	270,425	-1%	265,017	-2%	257,066	-3%	249,354	-3%
Gross customer loans	**189,389**	**186,049**	**-2%**	**182,328**	**-2%**	**176,858**	**-3%**	**171,552**	**-3%**
Net Customer Loans	184,438	180,412	-2%	176,188	-2%	170,321	-3%	164,664	-3%
Customer deposits	136,448	131,047	-4%	128,426	-2%	127,142	-1%	128,413	1%
Loan to deposit ratio	135.2%	137.7%		137.2%		134.0%		128.2%	
Shareholders' equity	**19,561**	**19,251**	**-2%**	**20,193**	**5%**	**21,843**	**8%**	**22,167**	**1%**
Average shareholders' equity	19,561	19,406	-1%	19,722	2%	21,018	7%	22,005	5%
Capital Ratios									
Core capital	13,417	17,178	28%	17,348	1%	17,525	1%	17,849	2%
Tier 1 capital	13,417	17,178	28%	17,348	1%	17,525	1%	17,849	2%
Risk-weighted assets	150,419	137,355	-9%	130,487	-5%	127,878	-2%	127,878	0%
Core Capital Ratio	**8.92%**	**12.51%**		**13.29%**		**13.70%**		**13.96%**	
Tier 1 ratio	8.92%	12.51%		13.29%		13.70%		13.96%	
Total capital ratio	8.92%	12.80%		16.19%		16.66%		16.91%	

Source: Company reports, Citi Investment Research and Analysis

Figure 33. Caixabank — Divisional Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	2,011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Banking & insurance									
Net Interest Income	**3,623**	**3,540**	**-2%**	**3,646**	**3%**	**3,610**	**-1%**	**3,574**	**-1%**
Fee Income	1,406	1,562	11%	1,546	-1%	1,531	-1%	1,516	-1%
Trading Income & Other	826	627	-24%	502	-20%	502	0%	502	0%
Total Income	**5,855**	**5,729**	**-2%**	**5,694**	**-1%**	**5,642**	**-1%**	**5,591**	**-1%**
Total Op. Expenses	-3,349	-3,219	-4%	-3,122	-3%	-3,091	-1%	-3,122	1%
Operating Income	**2,506**	**2,510**	**0%**	**2,572**	**2%**	**2,551**	**-1%**	**2,469**	**-3%**
Income from Investments & Dividends	31	53	71%	55	3%	56	3%	58	3%
Other Operating Items	0	0	NM	0	0%	0	0%	0	0%
Prov. Loan Losses (Net)	-1,456	-2,422	66%	-256	-89%	-1,782	596%	-1,594	-11%
Income Before Tax	**841**	**941**	**12%**	**870**	**-8%**	**825**	**-5%**	**933**	**13%**
Taxes	-258	-212	-18%	-244	15%	-231	-5%	-261	13%
- Implied Tax Rate	0	0	0%	0	0%	0	0%	0	0%
Net Income	**583**	**729**	**25%**	**627**	**-14%**	**594**	**-5%**	**672**	**13%**
Minority Interest	0	0	0%	0	3%	0	3%	0	3%
Available Income to Shareholders	**583**	**729**	**25%**	**627**	**-14%**	**594**	**-5%**	**672**	**13%**
Own funds	13,706	14,113	3%	14,426	2%	14,723	2%	15,059	2%
ROE	4%	5%		4%		4%		5%	
Investments									
Net Interest Income	**-205**	**-370**	**80%**	**-370**	**0%**	**-370**	**0%**	**-370**	**0%**
Fee Income	0	0	0%	0	0%	0	0%	0	0%
Trading Income	0	0	0%	0	0%	0	0%	0	0%
Other	0	0	0%	0	0%	0	0%	0	0%
Total Income	**-205**	**-370**	**80%**	**-370**	**0%**	**-370**	**0%**	**-370**	**0%**
Total Op. Expenses	-17	-13	-24%	-13	3%	-14	3%	-14	3%
Operating Income	**-222**	**-383**	**73%**	**-383**	**0%**	**-384**	**0%**	**-384**	**0%**
Income from Investments & Dividends	698	860	23%	1,000	16%	1,111	11%	1,182	6%
Other Operating Items	0	0	NM	0	0%	0	0%	0	0%
Other	94	-259	NM	0	NM	0	NM	0	NM
Income Before Tax	**570**	**218**	**-62%**	**617**	**183%**	**727**	**18%**	**798**	**10%**
Taxes	59	106	80%	-33	-131%	-48	47%	-58	20%
- Implied Tax Rate	0	0	0%	0	0%	0	0%	0	0%
Net Income	**629**	**324**	**-48%**	**584**	**80%**	**679**	**16%**	**740**	**9%**
Minority Interest	0	0	0%	0	3%	0	3%	0	3%
Available Income to Shareholders	**629**	**324**	**-48%**	**584**	**80%**	**679**	**16%**	**740**	**9%**
Own funds	5,535	6,049	9%	6,341	5%	6,681	5%	7,051	6%
ROE	12%	6%		9%		10%		11%	

Source: Company reports, Citi Investment Research and Analysis

Figure 34. BBVA — Group Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Net Interest Income	**13,320**	**-4%**	**13,203**	**-1%**	**14,263**	**8%**	**15,415**	**8%**	**16,438**	**7%**
Dividends	553	25%	23	-96%	25	10%	28	10%	30	10%
Fee Income	4,537	2%	4,580	1%	4,632	1%	4,946	7%	5,193	5%
Insurance & Other Income	1,159	43%	1,366	18%	1,402	3%	1,459	4%	1,535	5%
Trading Income	1,894	23%	1,480	-22%	1,452	-2%	1,547	7%	1,629	5%
Total Income	**20,910**	**1%**	**20,629**	**-1%**	**21,749**	**5%**	**23,367**	**7%**	**24,795**	**6%**
Total Operating Expenses	(8,967)	7%	(10,003)	12%	(10,900)	9%	(11,679)	7%	(12,373)	6%
Operating Profit	**11,942**	**-3%**	**10,627**	**-11%**	**10,849**	**2%**	**11,687**	**8%**	**12,422**	**6%**
Prov. Loan loss (net)	(4,718)	-14%	(4,231)	-10%	(5,289)	25%	(4,357)	-18%	(4,583)	5%
Equity Method	0	NM	0	NM	0	NM	0	NA	0	NA
Net income from non-fin activities	0	NM	0	NM	25	NM	25	NM	25	NM
Other income / losses	(803)	0%	(2,629)	228%	(1,762)	-33%	(1,065)	-40%	(1,068)	0%
Pre-tax Profit	**6,422**	**12%**	**3,766**	**-41%**	**3,824**	**2%**	**6,290**	**65%**	**6,796**	**8%**
Income Tax	(1,427)	25%	(425)	-70%	(455)	7%	(1,165)	156%	(1,264)	8%
Minorities	(388)	1%	(483)	24%	(545)	13%	(609)	12%	(666)	9%
Net Profit	**4,607**	**9%**	**2,859**	**-38%**	**2,824**	**-1%**	**4,517**	**60%**	**4,867**	**8%**
Per share data										
EPS	**1.10**	**2%**	**0.61**	**-45%**	**0.55**	**-9%**	**0.82**	**48%**	**0.85**	**4%**
Adj. EPS	1.10	2%	0.61	-45%	0.55	-9%	0.82	48%	0.85	4%
Dividend	0.42	0%	0.42	0%	0.42	0%	0.43	2%	0.45	5%
Payout ratio	38%	0	69%	0	76%	0	52%	0	53%	0
BVPS	**8.00**	**6%**	**7.78**	**-3%**	**7.86**	**1%**	**8.20**	**4%**	**8.60**	**5%**
Tangible BVPS	6.22	10%	6.01	-3%	6.23	4%	6.67	7%	7.08	6%
Number of shares (year end)	4,491	15%	4,903	9%	5,294	8%	5,695	8%	5,695	0%
Number of shares (avg)	4,196	8%	4,697	12%	5,099	9%	5,494	8%	5,695	4%
Operating ratios										
Net Interest margin (NII/ ATA)	2.45%		2.30%		2.30%		2.37%		2.45%	
Cost / income ratio	**43%**		**48%**		**50%**		**50%**		**50%**	
Provision charge / gross customer loans	135		117		142		113		116	
NPL ratio	**4.50%**		**4.39%**		**4.39%**		**4.21%**		**4.04%**	
Coverage	62%		61%		67%		75%		83%	
Return on Avg Assets	0.85%		0.50%		0.46%		0.69%		0.73%	
ROE	**14.1%**		**7.7%**		**7.1%**		**10.2%**		**10.2%**	
Balance Sheet Summary										
Total assets	552,738	3%	597,688	8%	642,194	7%	660,639	3%	679,216	3%
Net Customer Loans	**338,857**	**5%**	**351,900**	**4%**	**361,946**	**3%**	**372,560**	**3%**	**383,783**	**3%**
Customer deposits	275,789	9%	282,173	2%	269,285	-5%	283,371	5%	298,097	5%
Loan to deposit ratio	123%		125%		134%		131%		129%	
Shareholders Equity	**35,920**	**23%**	**38,166**	**6%**	**41,634**	**9%**	**46,684**	**12%**	**48,988**	**5%**
Average Shareholders' Equity	32,610	19%	37,043	14%	39,900	8%	44,159	11%	47,836	8%
Capital Position										
Core capital	30,098	30%	34,161	13%	35,914	5%	39,250	9%	41,553	6%
Tier 1 capital	33,023	21%	34,161	3%	35,914	5%	39,250	9%	41,553	6%
Total capital	42,924	9%	42,770	0%	44,523	4%	47,859	7%	50,162	5%
Risk-weighted assets	313,327	5%	330,771	6%	341,178	3%	361,649	6%	383,348	6%
Core capital ratio	**9.61%**		**10.33%**		**10.53%**		**10.85%**		**10.84%**	
Tier 1 ratio	10.54%		10.33%		10.53%		10.85%		10.84%	
Total capital ratio	13.70%		12.93%		13.05%		13.23%		13.09%	
Tangible Equity/ Assets	5.05%		4.93%		5.13%		5.75%		5.93%	

Source: Company reports, Citi Investment Research and Analysis

Figure 35. BBVA — Divisional Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Spain										
Net Interest Income	**4,878**	**-12%**	**4,399**	**-10%**	**4,232**	**-4%**	**4,147**	**-2%**	**4,147**	**0%**
Fee Income	1,672	-5%	1,468	-12%	1,291	-12%	1,291	0%	1,291	0%
Insurance	504	5%	471	-6%	462	-2%	462	0%	462	0%
Trading Income	2	-9%	19	nm	20	5%	21	5%	22	5%
Total Revenues	**7,055**	**-10%**	**6,357**	**-10%**	**6,005**	**-6%**	**5,921**	**-1%**	**5,922**	**0%**
Total Operating Expenses	(2,815)	-1%	(2,801)	0%	(2,883)	3%	(2,884)	0%	(2,885)	0%
Operating Profit	**4,240**	**-16%**	**3,556**	**-16%**	**3,122**	**-12%**	**3,037**	**-3%**	**3,037**	**0%**
Prov. Loan losses (Net)	(1,316)	-28%	(1,711)	30%	(2,840)	66%	(1,602)	-44%	(1,554)	-3%
Net Profit	**2,255**	**-19%**	**1,363**	**-40%**	**250**	**-82%**	**1,068**	**328%**	**1,103**	**3%**
Loans and credits	213,281	7%	209,622	-2%	203,334	-3%	197,234	-3%	191,317	-3%
Deposits	127,219	39%	114,783	-10%	117,078	2%	119,420	2%	121,808	2%
Eurasia										
Net Interest Income	345	-11%	801	132%	1,061	33%	1,146	8%	1,238	8%
Fee Income	236	6%	391	66%	444	14%	480	8%	518	8%
Trading Income	132	NM	105	-21%	89	-15%	94	6%	102	8%
Total Revenues	**1,080**	**13%**	**1,952**	**81%**	**2,315**	**19%**	**2,513**	**9%**	**2,730**	**9%**
Total Operating Expenses	(295)	6%	(645)	119%	(836)	30%	(886)	6%	(957)	8%
Operating Profit	**785**	**16%**	**1,307**	**67%**	**1,479**	**13%**	**1,626**	**10%**	**1,772**	**9%**
Loan loss provisions (net)	(89)	NM	(149)	66%	(175)	18%	(189)	8%	(204)	8%
Net Profit	**588**	**24%**	**1,027**	**75%**	**1,118**	**9%**	**1,232**	**10%**	**1,343**	**9%**
Loans and credits	23,813	-22%	33,905	42%	36,278	7%	39,180	8%	42,315	8%
Deposits	20,884	-40%	21,786	4%	22,875	5%	24,705	8%	26,681	8%
Mexico										
Net Interest Income	3,688	12%	3,796	3%	4,149	9%	4,821	16%	5,301	10%
Fee Income	1,233	14%	1,184	-4%	1,258	6%	1,392	11%	1,461	5%
Insurance and Other	179	55%	230	28%	249	8%	264	6%	286	8%
Trading Income	395	7%	298	-25%	299	1%	328	10%	345	5%
Total Revenues	**5,496**	**13%**	**5,544**	**1%**	**5,992**	**8%**	**6,842**	**14%**	**7,429**	**9%**
Total Operating Expenses	(1,899)	22%	(2,029)	7%	(2,221)	9%	(2,571)	16%	(2,825)	10%
Operating Profit	**3,597**	**8%**	**3,515**	**-2%**	**3,772**	**7%**	**4,271**	**13%**	**4,604**	**8%**
Loan loss provisions (net)	(1,229)	-19%	(1,167)	-5%	(1,115)	-4%	(1,322)	19%	(1,480)	12%
Net Profit	**1,711**	**26%**	**1,735**	**1%**	**1,977**	**14%**	**2,196**	**11%**	**2,326**	**6%**
Loans and credits	34,743	27%	34,681	0%	47,279	36%	55,051	16%	61,657	12%
Deposits	37,013	28%	36,131	-2%	13,681	-62%	15,929	16%	17,841	12%
USA										
Net Interest Income	1,794	7%	1,663	-7%	1,685	1%	1,752	4%	1,822	4%
Fee Income	651	7%	662	2%	643	-3%	669	4%	696	4%
Trading Income	156	0%	146	-7%	150	3%	156	4%	162	4%
Total Revenues	**2,551**	**6%**	**2,383**	**-7%**	**2,383**	**0%**	**2,479**	**4%**	**2,578**	**4%**
Total Operating Expenses	(1,517)	11%	(1,560)	3%	(1,659)	6%	(1,722)	4%	(1,787)	4%
Operating Profit	**1,034**	**-1%**	**823**	**-20%**	**724**	**-12%**	**757**	**5%**	**791**	**4%**
Loan loss provisions (net)	(703)	-50%	(363)	-48%	(250)	-31%	(255)	2%	(265)	4%
Net Profit	**239**	**-125%**	**(713)**	**-398%**	**337**	**-147%**	**356**	**6%**	**373**	**5%**
Loans and credits	38,408	-4%	38,927	1%	34,548	-11%	35,239	2%	36,649	4%
Deposits	42,343	-32%	37,777	-11%	38,649	2%	40,581	5%	42,610	5%
South America										
Net Interest Income	2,495	-3%	3,164	27%	3,696	17%	4,136	12%	4,547	10%
Fee Income	957	5%	1,077	13%	1,208	12%	1,337	11%	1,460	9%
Trading Income	514	27%	477	-7%	457	-4%	511	12%	561	10%
Total Revenues	**3,797**	**4%**	**4,457**	**17%**	**5,049**	**13%**	**5,627**	**11%**	**6,172**	**10%**
Total Operating Expenses	(1,668)	6%	(2,042)	22%	(2,327)	14%	(2,591)	11%	(2,841)	10%
Operating Profit	**2,129**	**3%**	**2,415**	**13%**	**2,723**	**13%**	**3,036**	**12%**	**3,331**	**10%**
Loan loss provisions (net)	(419)	-3%	(449)	7%	(516)	15%	(578)	12%	(648)	12%
Net Profit	**889**	**14%**	**1,005**	**13%**	**1,137**	**13%**	**1,267**	**12%**	**1,385**	**9%**
Loans and credits	30,408	20%	38,831	28%	44,573	15%	49,921	12%	55,912	12%
Deposits	33,496	14%	42,468	27%	47,773	12%	53,506	12%	59,927	12%
Corporate Center										
Total Revenues	932	1%	(27)	-103%	41	-253%	21	-48%	0	-98%
Net Profit	(1,072)	97%	(1,557)	45%	(1,993)	28%	(1,602)	-20%	(1,663)	4%

Source: Company reports, Citi Investment Research and Analysis

Figure 36. BBVA — Divisional Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Bancomer										
Net Interest Income	3,623	11%	3,715	3%	4,063	9%	4,729	16%	5,202	10%
Fee Income	1,158	13%	1,104	-5%	1,174	6%	1,305	11%	1,370	5%
Trading Income	283	6%	234	-17%	233	-1%	259	11%	272	5%
Total Revenues	**4,920**	**12%**	**4,945**	**1%**	**5,361**	**8%**	**6,177**	**15%**	**6,728**	**9%**
Total Operating Expenses	(1,758)	24%	(1,880)	7%	(2,056)	9%	(2,392)	16%	(2,632)	10%
Operating Profit	**3,162**	**6%**	**3,066**	**-3%**	**3,305**	**8%**	**3,784**	**14%**	**4,096**	**8%**
Loan loss provisions (net)	(1,229)	-19%	(1,167)	-5%	(1,115)	-4%	(1,322)	19%	(1,480)	12%
Pre-tax Profit	1,850	28%	1,842	0%	2,190	19%	2,463	12%	2,616	6%
Net Profit	**1,399**	**25%**	**1,419**	**1%**	**1,643**	**16%**	**1,847**	**12%**	**1,962**	**6%**
Loans and credits	34,626	27%	39,203	13%	47,279	21%	55,051	16%	61,657	12%
Deposits	37,033	16%	11,344	-69%	13,681	21%	15,929	16%	17,841	12%
RWAs	40,260	18%	45,582	13%	53,990	18%	61,742	14%	67,916	10%
Cost/ income ratio (CIRA cal.)	**36%**		**38%**		**38%**		**39%**		**39%**	
Bancomer (Mexican Pesos)										
Net Interest Income	60,715	-1%	64,280	6%	70,708	10%	77,779	10%	85,556	10%
Fee Income	19,406	0%	19,098	-2%	20,435	7%	21,457	5%	22,529	5%
Trading Income	4,732	-6%	4,054	-14%	4,054	0%	4,256	5%	4,469	5%
Total Revenues	**82,446**	**-1%**	**85,533**	**4%**	**93,298**	**9%**	**101,593**	**9%**	**110,657**	**9%**
Total Operating Expenses	(29,474)	10%	(32,521)	10%	(35,773)	10%	(39,351)	10%	(43,286)	10%
Operating Profit	**52,972**	**-6%**	**53,012**	**0%**	**57,525**	**9%**	**62,243**	**8%**	**67,371**	**8%**
Loan loss provisions (net)	(20,626)	-28%	(20,196)	-2%	(19,408)	-4%	(21,737)	12%	(24,345)	12%
Pre-tax Profit	30,892	13%	31,847	3%	38,117	20%	40,506	6%	43,026	6%
Net Profit	**23,359**	**11%**	**24,514**	**5%**	**28,588**	**17%**	**30,379**	**6%**	**32,269**	**6%**
Loans and credits	571,886	12%	707,668	24%	792,589	12%	887,699	12%	994,223	12%
Deposits	611,624	2%	204,768	-67%	229,340	12%	256,861	12%	287,684	12%
RWAs	664,930	5%	822,805	24%	905,085	10%	995,593	10%	1,095,153	10%
Cost/ income ratio (CIRA cal.)	**36%**		**38%**		**38%**		**39%**		**39%**	
USA (Euros in Millions)										
Net Interest Income	1,794	7%	1,663	-7%	1,685	1%	1,752	4%	1,822	4%
Fee Income	651	7%	662	2%	643	-3%	669	4%	696	4%
Trading Income	156	0%	146	-7%	150	3%	156	4%	162	4%
Total Revenues	**2,551**	**6%**	**2,383**	**-7%**	**2,383**	**0%**	**2,479**	**4%**	**2,578**	**4%**
Total Operating Expenses	(1,517)	11%	(1,560)	3%	(1,659)	6%	(1,722)	4%	(1,787)	4%
Operating Profit	**1,034**	**-1%**	**823**	**-20%**	**724**	**-12%**	**757**	**5%**	**791**	**4%**
Loan loss provisions (net)	(703)	-50%	(363)	-48%	(250)	-31%	(255)	2%	(265)	4%
Pre-tax Profit	309	NM	(1,049)	NM	474	NM	502	6%	526	5%
Net Profit	**239**	**NM**	**(713)**	**NM**	**337**	**NM**	**356**	**6%**	**373**	**5%**
Loans and credits	38,408	-4%	38,927	1%	34,548	8%	35,239	8%	36,649	8%
Deposits	42,343	-32%	37,777	-11%	38,649	2%	40,581	5%	42,610	5%
RWAs	27,321	0%	29,139	7%	29,227	0%	29,811	2%	31,004	4%
Cost/ income ratio (CIRA cal.)	**59%**		**65%**		**70%**		**69%**		**69%**	
USA (US$ in Millions)										
Net Interest Income	2,390	4%	2,189	-8%	2,156	-2%	2,243	4%	2,332	4%
Fee Income	867	4%	871	0%	823	-6%	856	4%	891	4%
Trading Income	207	0%	192	-7%	192	0%	200	4%	208	4%
Total Revenues	**3,398**	**3%**	**3,136**	**-8%**	**3,051**	**-3%**	**3,173**	**4%**	**3,300**	**4%**
Total Operating Expenses	(2,022)	9%	(2,053)	2%	(2,123)	3%	(2,204)	4%	(2,287)	4%
Operating Profit	**1,376**	**-4%**	**1,084**	**-21%**	**927**	**-14%**	**969**	**5%**	**1,012**	**4%**
Loan loss provisions (net)	(938)	-53%	(478)	-49%	(320)	-33%	(326)	2%	(339)	4%
Pre-tax Profit	408	-120%	(1,381)	-438%	607	-144%	643	6%	673	5%
Net Profit	**317**	**-123%**	**(938)**	**-396%**	**431**	**-146%**	**456**	**6%**	**478**	**5%**
Loans and credits	51,405	-12%	50,368	-2%	50,368	0%	51,375	2%	53,430	4%
Deposits	56,671	-38%	48,879	-14%	49,857	2%	52,350	5%	54,967	5%
RWAs	36,566	-9%	37,703	3%	37,703	0%	38,457	2%	39,995	4%
Cost/ income ratio (CIRA cal.)	**60%**		**65%**		**70%**		**69%**		**69%**	

Source: Company reports, Citi Investment Research and Analysis

Figure 37. SAN — Group Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Net interest income	**29,224**	**11%**	**30,821**	**5%**	**33,899**	**10%**	**36,912**	**9%**	**39,806**	**8%**
Fee Income	9,734	7%	10,471	8%	11,353	8%	12,275	8%	12,976	6%
Insurance and Other	487	3%	464	-5%	423	-9%	401	-5%	392	-2%
Trading	2,606	-24%	2,500	-4%	2,603	4%	2,738	5%	2,794	2%
Total income	**42,051**	**7%**	**44,257**	**5%**	**48,278**	**9%**	**52,326**	**8%**	**55,968**	**7%**
Operating expenses	(18,196)	11%	(19,889)	9%	(21,899)	10%	(23,844)	9%	(25,272)	6%
Gross operating profit	**23,855**	**4%**	**24,367**	**2%**	**26,380**	**8%**	**28,482**	**8%**	**30,696**	**8%**
Prov. Loan Losses (Net)	(10,258)	8%	(10,562)	3%	(13,524)	28%	(13,306)	-2%	(14,124)	6%
Equity method earnings	(2)	NM	5	-424%	20	279%	20	0%	20	0%
Other	(1,543)	-10%	(2,772)	80%	(1,255)	-55%	(1,497)	19%	(1,439)	-4%
Pre-tax profit	**12,052**	**2%**	**11,038**	**-8%**	**11,622**	**5%**	**13,700**	**18%**	**15,154**	**11%**
Tax	(2,923)	25%	(3,157)	8%	(3,320)	5%	(3,919)	18%	(4,326)	10%
Goodwill	0	NM	0	0%	0	0%	0	0%	0	0%
Other extraordinary income	(27)	NM	(1,694)		0		0		0	
Total Minorities	(921)	79%	(836)	-9%	(1,005)	20%	(1,255)	25%	(1,386)	10%
Net profit	**8,181**	**-9%**	**5,351**	**-35%**	**7,297**	**36%**	**8,526**	**17%**	**9,442**	**11%**
Per share data										
EPS	**0.99**	**-10%**	**0.62**	**-37%**	**0.80**	**29%**	**0.86**	**7%**	**0.93**	**9%**
Adj. Cash EPS	0.99	-9%	0.82	-18%	0.80	-2%	0.86	7%	0.93	9%
Dividend	**0.60**	**0%**	**0.60**	**0%**	**0.60**	**0%**	**0.60**	**0%**	**0.60**	**0%**
Payout ratio	61%	11%	97%	59%	75%	-22%	70%	-7%	65%	-8%
BVPS	**9.01**	**8%**	**8.58**	**-5%**	**7.94**	**-7%**	**8.21**	**3%**	**8.54**	**4%**
Tangible BVPS	**6.05**	**9%**	**5.76**	**-5%**	**5.37**	**-7%**	**5.74**	**7%**	**6.07**	**6%**
Number of shares (year end)	8,329	1%	8,909	7%	9,777	10%	10,154	4%	10,154	0%
Number of shares (avg)	8,279	2%	8,619	4%	9,126	6%	9,965	9%	10,154	2%
Operating Ratios										
Net Interest margin (NII/ ATA)	2.51%		2.50%		2.63%		2.69%		2.73%	
Cost / income ratio	**43.3%**		**44.9%**		**45.4%**		**45.6%**		**45.2%**	
Provision charge / gross customer loans	142		140		169		153		153	
Non Performing Loan Ratio	**3.8%**		**4.2%**		**4.4%**		**3.9%**		**3.5%**	
Coverage	72.7%		61.4%		62.3%		75.1%		89.6%	
Return on Avg Assets	0.70%		0.43%		0.57%		0.62%		0.65%	
Return on Avg RWAs	1.40%		0.91%		1.26%		1.38%		1.44%	
ROE	**11.4%**		**7.1%**		**9.5%**		**10.6%**		**11.1%**	
Balance Sheet Items										
Total assets	1,217,501	10%	1,251,525	3%	1,322,016	6%	1,424,782	8%	1,490,151	5%
Net Customer Loans	**724,154**	**6%**	**750,100**	**4%**	**812,303**	**8%**	**880,758**	**8%**	**916,058**	**4%**
Customer deposits	581,385	19%	588,977	1%	628,546	7%	700,358	11%	738,151	5%
Loan to deposit ratio	125%		127%		129%		126%		124%	
Shareholders Equity	**75,018**	**9%**	**76,414**	**2%**	**77,633**	**2%**	**83,385**	**7%**	**86,735**	**4%**
Average Shareholders' equity	71,842	14%	75,716	5%	77,023	2%	80,509	5%	85,060	6%
Capital Ratios										
Core capital	53,205	10%	56,694	7%	57,553	2%	63,571	10%	67,173	6%
Tier 1 capital	60,617	7%	62,294	3%	62,873	1%	68,625	9%	71,975	5%
Risk-weighted assets	604,885	8%	565,958	-6%	594,362	5%	638,063	7%	672,911	5%
Core capital ratio	**8.80%**		**10.02%**		**9.68%**		**9.96%**		**9.98%**	
Tier 1 ratio	10.02%		11.01%		10.58%		10.76%		10.70%	
Total capital ratio	13.11%		13.56%		13.01%		13.02%		12.85%	
Tangible Equity/ Assets	4.14%		4.10%		3.97%		4.09%		4.14%	

Source: Company reports, Citi Investment Research and Analysis

Figure 38. SAN — Divisional Profit and Loss Account, 2010-14E (Euros in Millions)

	2010	% Chg	2011	% Chg	2012E	% Chg	2013E	% Chg	2014E	% Chg
Continental Europe										
Net interest income	9,872	-14%	10,666	8%	11,073	4%	11,329	2%	11,609	2%
Operating income	**14,793**	**-9%**	**15,347**	**4%**	**15,855**	**3%**	**16,287**	**3%**	**16,752**	**3%**
Operating expenses	(5,917)	0%	(6,612)	12%	(6,910)	4%	(7,088)	3%	(7,250)	2%
Gross operating profit	**8,875**	**-14%**	**8,735**	**-2%**	**8,946**	**2%**	**9,199**	**3%**	**9,502**	**3%**
Provisions	(4,019)	29%	(4,192)	4%	(6,011)	43%	(4,868)	-19%	(4,858)	0%
Pre-tax profit	**4,684**	**-34%**	**4,039**	**-14%**	**2,810**	**-30%**	**4,037**	**44%**	**4,365**	**8%**
Tax	(1,220)	-35%	(1,049)	-14%	(789)	-25%	(1,135)	44%	(1,221)	8%
Minorities	(96)	3%	(117)	22%	(145)	24%	(264)	82%	(284)	8%
Net profit	**3,355**	**-33%**	**2,849**	**-15%**	**1,876**	**-34%**	**2,638**	**41%**	**2,859**	**8%**
Loans and credits	**323,660**	**1%**	**315,081**	**-3%**	**309,203**	**-2%**	**308,537**	**0%**	**309,090**	**0%**
Deposits	247,715	25%	247,582	0%	252,152	2%	261,820	4%	271,351	4%
Cost/ income ratio	**40%**		**43%**		**44%**		**44%**		**43%**	
NIM (Citi estimate)	**1.96%**		**2.13%**		**2.22%**		**2.29%**		**2.34%**	
UK										
Net interest income	4,766	21%	4,176	-12%	3,666	-12%	3,724	2%	3,836	3%
Operating income	**6,285**	**15%**	**5,678**	**-10%**	**5,276**	**-7%**	**5,605**	**6%**	**5,773**	**3%**
Operating expenses	(2,549)	14%	(2,554)	0%	(2,776)	9%	(3,238)	17%	(3,303)	2%
Gross operating profit	**3,735**	**16%**	**3,123**	**-16%**	**2,500**	**-20%**	**2,366**	**-5%**	**2,470**	**4%**
Provisions	(930)	6%	(585)	-37%	(652)	11%	(673)	3%	(673)	0%
Pre-tax profit	**2,700**	**14%**	**1,788**	**-34%**	**1,713**	**-4%**	**1,466**	**-14%**	**1,565**	**7%**
Tax	(734)	15%	(643)	-12%	(428)	-33%	(367)	-14%	(391)	7%
Net profit	**1,965**	**14%**	**1,145**	**-42%**	**1,285**	**12%**	**1,100**	**-14%**	**1,174**	**7%**
Loans and credits	**234,778**	**3%**	**252,154**	**7%**	**268,915**	**7%**	**311,843**	**16%**	**321,199**	**3%**
Deposits	185,276	11%	194,318	5%	205,241	6%	245,565	20%	252,932	3%
Cost/ income ratio	**41%**		**45%**		**53%**		**58%**		**57%**	
NIM (Citi estimate)	**1.40%**		**1.18%**		**1.00%**		**0.93%**		**0.89%**	
USA										
Net interest income	1,736	50%	1,678	-3%	1,788	7%	1,860	4%	1,934	4%
Operating income	**2,106**	**44%**	**2,188**	**4%**	**2,338**	**7%**	**2,430**	**4%**	**2,526**	**4%**
Operating expenses	(937)	6%	(976)	4%	(1,067)	9%	(1,110)	4%	(1,154)	4%
Gross operating profit	**1,169**	**101%**	**1,212**	**4%**	**1,271**	**5%**	**1,320**	**4%**	**1,371**	**4%**
Provisions	(510)	-11%	(374)	-27%	(407)	9%	(387)	-5%	(367)	-5%
Pre-tax profit	**567**	**NM**	**776**	**37%**	**799**	**3%**	**869**	**9%**	**939**	**8%**
Tax	(143)	NM	(250)	-33%	(240)	-4%	(261)	9%	(282)	8%
Net profit	**424**	**NM**	**526**	**24%**	**559**	**6%**	**608**	**9%**	**658**	**8%**
Loans and credits	36,724	6%	40,194	9%	41,369	3%	43,438	5%	45,610	5%
Deposits	32,007	4%	36,884	15%	37,962	3%	39,860	5%	41,853	5%
Cost/ income ratio	**44%**		**45%**		**46%**		**46%**		**46%**	
NIM (Citi estimate)	**3.45%**		**3.07%**		**3.05%**		**3.06%**		**3.03%**	
Latin America										
Net interest income	14,678	23%	16,473	12%	19,436	18%	22,165	14%	24,702	11%
Operating income	**20,676**	**17%**	**22,442**	**9%**	**26,099**	**16%**	**29,398**	**13%**	**32,421**	**10%**
Operating expenses	(7,971)	21%	(8,909)	12%	(10,244)	15%	(11,434)	12%	(12,522)	10%
Gross operating profit	**12,705**	**15%**	**13,533**	**7%**	**15,855**	**17%**	**17,965**	**13%**	**19,898**	**11%**
Provisions	(4,687)	-6%	(5,447)	16%	(6,493)	19%	(7,419)	14%	(8,269)	11%
Pre-tax profit	**7,271**	**34%**	**7,057**	**-3%**	**8,261**	**17%**	**9,455**	**14%**	**10,577**	**12%**
Tax	(1,693)	35%	(1,654)	-2%	(2,192)	32%	(2,514)	15%	(2,816)	12%
Minorities	(850)	99%	(738)	-13%	(879)	19%	(1,010)	15%	(1,121)	11%
Net profit	**4,728**	**23%**	**4,664**	**-1%**	**5,190**	**11%**	**5,931**	**14%**	**6,640**	**12%**
Loans and credits	127,268	30%	139,867	10%	171,077	22%	195,200	14%	218,420	12%
Deposits	137,848	27%	134,078	-3%	157,074	17%	176,997	13%	195,899	11%
Cost/ income ratio	**39%**		**40%**		**39%**		**39%**		**39%**	
NIM (Citi estimate)	**6.03%**		**6.01%**		**6.40%**		**6.20%**		**6.08%**	
Corporate Centre										
Operating income	**(1,808)**	**28%**	**(1,398)**	**-23%**	**(1,290)**	**-8%**	**(1,394)**	**8%**	**(1,503)**	**8%**
Operating expenses	(822)	2%	(838)	2%	(902)	8%	(974)	8%	(1,042)	7%
Net profit	**(2,291)**	**41%**	**(3,833)**	**67%**	**(1,613)**	**-58%**	**(1,750)**	**9%**	**(1,888)**	**8%**

Source: Company reports, Citi Investment Research and Analysis

Bankinter SA

Company description

Bankinter S.A. provides retail and corporate banking services and financial services throughout Spain. The Bank offers mortgage loans, pension funds, life insurance, lease financing, credit cards, mutual funds, online stock brokerage, private banking and Internet banking services.

Investment strategy

We have a Sell/High Risk (3H) rating on Bankinter. Our rating reflects the risks associated with the higher cost of bank funding. A significant increase in funding costs could: (i) accelerate the loan contraction; (ii) hasten asset depreciation; (iii) significantly increase margin pressure, given the rapid movement in rates; (iv) limit liquidity in the debt markets; (v) induce deterioration in the credit environment; and (vi) limit M&A potential given the poor earnings visibility of these banks and the expensive cost of equity and debt paper.

Valuation

Our target price for Bankinter is €3.40. We use the midpoint of our dividend discount model for 2012-14E (with a COE of 13% and an average ROE of 7.2%) combined with a tangible book-based bear case valuation as reference points of our valuation. We use a lower cost of equity (11%) for the terminal value calculation. We believe that this valuation correctly reflects the risks to earnings from: (i) the current deleverage process of the economy; (ii) a rapid deterioration in asset quality; and (iii) margin pressures from the liability side. Note that our valuation of BKT does not include an M&A premium because we see this as unlikely in the current environment.

Risks

We rate Bankinter as High Risk based on our assessment of industry and company-specific risk factors. Our risk rating principally reflects the uncertainties surrounding the current sovereign debt crisis in Europe. With regards to Bankinter, we would highlight the following specific risks that could cause the shares to exceed our target price:

(i) M&A. An offer from a domestic or international bank at a premium to its current market price could result in a sharp re-rating in its shares; (ii) Revival of liquidity. If liquidity were to return to the market at levels similar to 2Q07, BKT's earnings forecasts would have to be revised upwards and this would support its shares.

Banco Popular Espanol

Company description

Banco Popular Espanol SA attracts deposits and offers commercial banking services. The bank offers consumer loans, mortgage loans, asset management and factoring services, mutual funds, pension plans, life insurance, venture capital and real estate loans.

Investment strategy

We have a Sell/High Risk (3H) rating on Banco Popular. Our POP rating reflects the risks remaining in the Spanish local banks from the asset quality and the funding sides, despite the superior earnings generation capability of POP. A sharp deterioration of the asset quality could significantly increase loan loss provisions, eroding the profits and capital ratios of the company. A significant increase in funding costs could: (1) rapidly slow lending growth; (2) hasten asset depreciation; (3) significantly increase margin pressure, given the rapid movement in rates and the flattening of the yield curve; (4) limit liquidity in the debt markets; (5) induce deterioration in the credit environment; and (6) limit M&A potential given the poor earnings visibility of these banks and the expensive cost of equity and debt paper.

Valuation

We use a two-stage dividend discount model (DDM) to value Popular, including the present value of 2012-14E dividends and a terminal value assuming zero growth at the average RoE of 2013-2014E (8.3%) and the final year ROE (9.8%). We assume a 13.5% cost of equity for the group for the DDM and 11% for the terminal value. We cross-check this valuation using: 1) justified price to book valuation; 2) comparable P/E valuation relative to the banks sector; and 3) comparable P/E valuation relative to Popular's historical trading range and growth prospects. From these methods, we derive a target price of €2.60.

Risks

We rate Banco Popular as High Risk based on our assessment of industry and company-specific risk factors. Our risk rating principally reflects the uncertainties surrounding the current sovereign debt crisis in Europe. With regards to Banco Popular, we would highlight the following specific upside risks, which could cause the share price to exceed our target price: (i) M&A. An offer from a domestic or international bank at a premium to its current market price could result in a sharp re-rating in its shares. (ii) Revival of liquidity. If liquidity were to return to the market at levels similar to 2Q07, POP's earnings forecasts would have to be revised upwards and this would support its shares. Conversely, negative developments relating to these risk factors could cause the share to remain below our target price.

Banesto

Company description

Banco Espanol de Credito, SA (Banesto) attracts deposits and offers commercial, retail and private banking services. The company offers loans, lease financing, factoring, treasury, insurance and personal banking services, manages mutual funds, offers asset management services and sponsors credit cards.

Investment strategy

We rate Banesto Neutral/High Risk (2H). Our rating reflects the risks associated with the higher cost of bank funding. A significant increase in funding costs could: (1) accelerate the loan contraction; (2) hasten asset depreciation; (3) significantly increase margin pressure, given the rapid movement in rates and the flattening of the yield curve; (4) limit liquidity in the debt markets; (5) induce deterioration in the credit environment; and (6) limit M&A potential given the poor earnings visibility and the expensive cost of equity and debt paper.

Valuation

Our target price for Banesto is €4.30. We use a dividend discount model, which includes our four-year forecasts, terminal ROE of 8.2%, and a COE of 12.5%. We use a lower terminal cost of equity (11%) for the residual valuation. Using both a growth and a no growth variation of the model, we set our target price at €4.30. We believe that this valuation correctly reflects the risks to earnings from: (i) the current deleverage process of the economy; (ii) a longer-than-expected deterioration in asset quality; and (iii) margin pressures from the liability side.

Risks

We rate Banesto as High Risk because of the uncertainties surrounding the current sovereign debt crisis in Europe. With regards to BTO, we would highlight the following specific risks:

- Macroeconomic weakness. A weak recovery in real GDP growth and employment levels in Spain would put pressure on bank lending growth and in the asset quality indicators.
- Revival of liquidity. If liquidity were to return to the market at levels similar to 2007, BTO's earnings forecasts would have to be revised upwards and this would support its shares.
- Faster-than-expected economic recovery could result in the shares exceeding our target price.

If the impact on the company from any of these factors proves to be more negative than we anticipate, the stock will likely have difficulty achieving our price targets. Conversely, if any of these factors proves to have less of an effect than we anticipate, the stock could materially outperform our target.

CaixaBank SA

Company description

CaixaBank is the banking operation of "la Caixa", the fourth largest financial institution in Spain and the largest caja, with €270bn assets and 5,196 branches. CaixaBank also owns the largest life insurer in Spain, a 12.8% stake in Repsol, 5.4% in Telefonica and stakes in different international banks.

Investment strategy

We have a Sell/High Risk (3H) rating on CaixaBank. Our rating reflects the risks associated with the higher cost of bank funding. A significant increase in funding costs could: (i) accelerate the loan contraction; (ii) hasten asset depreciation; (iii) significantly increase margin pressure, given the rapid movement in rates; (iv) limit liquidity in the debt markets and (v) induce deterioration in the credit environment.

Valuation

To estimate CaixaBank's fair value, we use a scoring matrix and referenced the current valuation of its peers. The four valuation methodologies we consider include a Dividend Discount Model (€2.59), a static ROE Model (€2.59), a Discount to NAV model (€2.55) and a Sum-of-the-Parts valuation (€3.18; although we discard this as we feel it doesn't capture the holding discount the market applies to financial holdings). Our €2.60 target price is based on the average of the DDM, the static ROE and the Discount to NAV.

The DDM is the central methodology. We use the midpoint of our dividend discount model for 2012-15E (with a COE of 12.5% and an average ROE of 6.4%) combined with a tangible book-based bear case valuation as reference points of our valuation. We believe that this correctly reflects the risks to earnings from: (i) the current deleverage process of the economy; (ii) a rapid deterioration in asset quality; and (iii) margin pressures from the liability side. Note that our valuation includes an M&A discount given the consolidator profile of CaixaBank in the Spanish banking market.

Risks

We rate CaixaBank as High Risk based on our assessment of industry and company-specific risk factors. Our risk rating principally reflects the uncertainties surrounding the current sovereign debt crisis in Europe. With regards to CaixaBank, we would highlight the following specific risks which could cause the stock to deviate from our target price:

Macro-economic weakness. A weak recovery in real GDP growth and employment in Spain would pressure bank lending growth and in the asset quality indicators.

Revival of liquidity. If liquidity were to return to the market at levels similar to 2007, our forecasts for CaixaBank would have to be raised, thus supporting its shares.

M&A in the banking activities. An offer for a domestic or international bank could increase the percentage of banking and non listed activities within the group resulting in a reduction of the discount to NAV valuation.

M&A in the industrial portfolio. An offer for one of the companies held in the industrial portfolio could result in a sharp increase in the Gross Asset Value of Caixabank, increasing the final valuation of the company.

Banco Santander

Company description

Banco Santander Central Hispano SA is one of the best retail banks globally, in our view. The bank offers consumer credit, mortgage loans, lease financing, factoring, mutual funds, pension funds, insurance, commercial credit, investment banking services, structured finance, and advice on mergers and acquisitions. Santander operates in Continental Europe, UK, LatAm and US.

Investment strategy

We rate the shares Neutral/High Risk (2H). We believe Santander's key investment positives are:

Latin Strength: Santander's total 2011 LatAm profit before tax of €7bn amounted to two-thirds of group profits. With double-digit forecast revenue and profit growth for the LatAm operations, we expect regional pre-tax profits to rise to €9.5bn in 2013E, or three-quarters of group profits. Santander has the third biggest private bank in Brazil. Low banking penetration and high expected economic growth in Brazil should materially boost Santander's profit growth in the country.

Improving Capital: Santander's equity Tier 1 ratio increased to 10% at end 2011, up from 8.8% at end-2010. Despite the difficult operating environment in Europe, Santander boosted its EBA equity tier 1 ratio from 7.5% at end 3Q11 to 9% at end 2011. The company targets a 10% EBA equity tier 1 ratio by June 2012. However, the improved capital is resulting in earnings dilution. We expect the share count to increase 10% in 2012, and c55% 2007-12E.

Despite the improving capital situation and the outlook in Latam, the negative macro outlook in Europe and the dilutive impact of additional capital measures leaves our rating on the stock as Neutral.

Valuation

We use a peer group SOTP model to value Santander, as explained below:

Using a peer group PE-based sum-of-the-parts approach, we derive a value of €69bn. Latin America accounts for about two-thirds of the value of Santander in our SOTP. For our model, we typically use the current traded value of relevant local comparable banks. We cross-check the valuation using: (1) justified price to book valuation, (2) comparable P/E valuation relative to the banks sector, and (3) comparable P/E valuation relative to Santander's historical trading range and growth prospects. From these methods we derive a target price for Santander of €6.4.

Risks

We rate Banco Santander as High Risk based on our assessment of industry- and company-specific risk factors. Our risk rating principally reflects the uncertainties surrounding the current sovereign debt crisis in Europe. The following risk factors could impede the share price from reaching our target price:

Spanish Stagnation and Bad Debts - We remain cautious on the outlook for the Spanish economy and asset quality.

Further Deterioration of the US Economy - A renewed deterioration in the US economic conditions could reduce the earnings expectations of Santander's local subsidiary (Sovereign Bank)

Slower-than-expected Recovery in LatAm - A weaker-than-expected recovery in Latin America (particularly Brazil) would impact our earning expectations in the region for Santander.

Conversely, if any of these factors proves to have less of an effect than we anticipate, the stock could materially outperform our target.

Banco Bilbao Vizcaya Argentaria SA

Company description

Banco Bilbao Vizcaya Argentaria S.A. is a leading global retail bank. It offers consumer and mortgage loans, private banking, asset management, insurance, mutual funds and securities brokerage services. It operates in Europe, Latin America and US. BBVA also has a 15% stake in China's CITIC Bank and a 25% stake in Garanti (Turkish bank).

Investment strategy

We rate the shares Neutral/High Risk (2H). We outline BBVA's key investment positives below:

Mexican Recovery - BBVA's Mexican bank, Bancomer, is one of the best emerging market banks globally, in our view. With the pick up in Mexico seeing at the end of 2011, we expect earnings to improve at Bancomer: 2013E net profit €1.8bn +c65% vs. 2009.

South America Resilient – BBVA owns one of the largest franchises in the region (Ex Brazil). During the last five years the business has been resilient to the business cycle and has shown a double digit CAGR. We expect this growth to continue in the 2011-2013E period, when we expect the franchise to post a €1.3bn profit.

Improving Capital – At the end of 2007 BBVA's equity Tier 1 ratio stood at 5.3%. The bank closed 2011 with an equity Tier 1 of 10.3%. We expect the bank to cover the EBA capital deficit without problems ahead of the June 2012 deadline. Additionally, we expect BBVA to comply with the new Spanish provisioning rules without additional share count dilutive measures.

Valuation

We use a two-stage dividend discount model (DDM) to value BBVA, as explained below. We cross check this using a peer-group sum of the parts. SOTP Model - using a peer group P/E-based sum-of-the-parts approach; DDM Valuation - We use a DDM model with the present value of 2012-14E dividends and a terminal value assuming an ROE of 10.2%. We assume a 12.1% cost of equity for the group. The DDM approach, gives us a target value of €33bn or €6.8 per share for BBVA.

We cross-check the valuation using: (1) justified price to book valuation, (2) comparable P/E valuation relative to the banks sector, and (3) comparable P/E valuation relative to BBVA's historical trading range and growth prospects. From these methods, we derive a target price for BBVA of €6.8.

Risks

We rate BBVA as High Risk based on our assessment of industry and company-specific risk factors. Our risk rating principally reflects the uncertainties surrounding the new bank regulation and the economic environment in Spain. Risks to the share price reaching our target price could come in our view from the following:

Spanish Macro Deterioration – The Spanish macro situation remains weak, the adjustment packages approved by the Government will add pressure to the current difficult situation. The deleverage process taking place in the country completes this difficult macro scenario.

Appendix A-1

Analyst Certification

The research analyst(s) primarily responsible for the preparation and content of this research report are named in bold text in the author block at the front of the product except for those sections where an analyst's name appears in bold alongside content which is attributable to that analyst. Each of these analyst(s) certify, with respect to the section(s) of the report for which they are responsible, that the views expressed therein accurately reflect their personal views about each issuer and security referenced and were prepared in an independent manner, including with respect to Citigroup Global Markets Inc and its affiliates. No part of the research analyst's compensation was, is, or will be, directly or indirectly, related to the specific recommendation(s) or view(s) expressed by that research analyst in this report.

IMPORTANT DISCLOSURES

Banco Bilbao Vizcaya Argentaria SA (BBVA.MC)

Ratings and Target Price History
Fundamental Research

Analyst: Ronit Ghose

	Date	Rating	Target Price	Closing Price
1	30-Apr-09	2M	*7.93	7.95
2	30-Jul-09	2M	*10.57	10.88
3	6-Aug-09	2M	*11.53	11.03
4	7-Oct-09	*1M	*13.45	11.62
5	25-Oct-09	1M	*14.41	12.01
6	6-Jan-10	1M	*15.85	12.60
7	29-Jan-10	1M	*14.41	10.66

	Date	Rating	Target Price	Closing Price
8	30-Apr-10	1M	*12.97	9.55
9	21-Jun-10	1M	*11.29	9.04
10	20-Jul-10	1M	*10.33	9.13
11	3-Aug-10	1M	*11.05	10.37
12	1-Nov-10	1M	*10.57	8.75
13	17-Jan-11	1M	*10.00	8.20
14	9-May-11	1M	*9.75	8.19

	Date	Rating	Target Price	Closing Price
15	15-Jul-11	*1H	*8.75	7.20
16	30-Jul-11	*2H	*8.30	7.35
17	4-Oct-11	*2S	*6.75	5.90
18	7-Oct-11	Stock rating system changed		
19	7-Oct-11	*2H	6.75	6.45
20	28-Oct-11	2H	*6.50	6.93
21	3-Feb-12	2H	*6.80	7.19

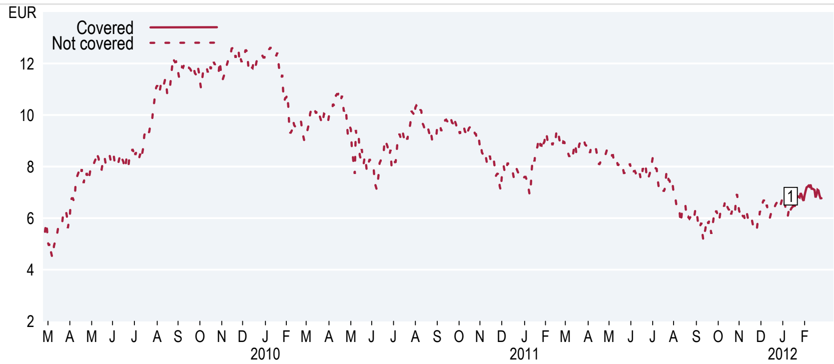
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Banco Bilbao Vizcaya Argentaria SA (BBVA.MC)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ronit Ghose



	Date	Rating	Target Price	Closing Price
1	12-Jan-12	*ADD LP	-	6.33

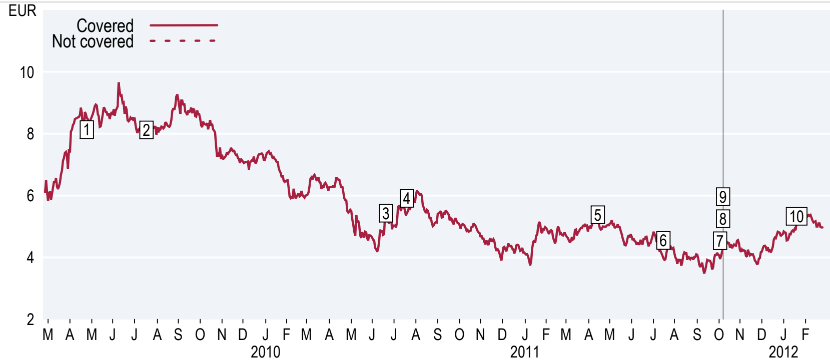
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Bankinter SA (BKT.MC)

Ratings and Target Price History
Fundamental Research

Analyst: Ignacio Moreno
Covered since May 19 2010



	Date	Rating	Target Price	Closing Price
1	24-Apr-09	3M	*4.70	8.50
2	17-Jul-09	3M	*5.00	8.29
3	21-Jun-10	3M	*4.00	5.43
4	20-Jul-10	3M	*3.80	5.45
5	14-Apr-11	3M	*4.00	5.17
6	15-Jul-11	*3H	*3.00	3.97
7	4-Oct-11	*3S	3.00	3.95
8	7-Oct-11	Stock rating system changed		
9	7-Oct-11	*3H	3.00	4.31
10	19-Jan-12	3H	*3.40	5.21

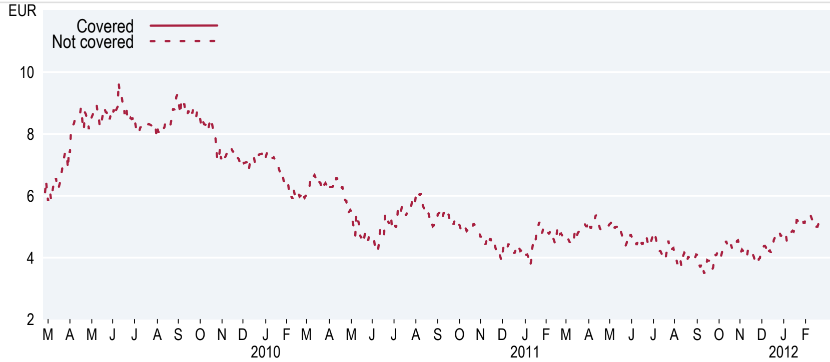
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Bankinter SA (BKT.MC)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ignacio Moreno
Covered since May 19 2010



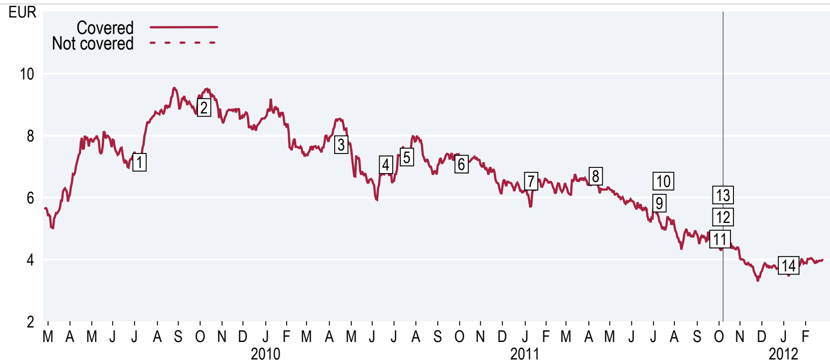
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Banesto (BTO.MC)

Ratings and Target Price History
Fundamental Research

Analyst: Ignacio Moreno
Covered since May 19 2010



	Date	Rating	Target Price	Closing Price
1	8-Jul-09	*2M	*7.00	7.14
2	7-Oct-09	2M	*9.00	9.40
3	19-Apr-10	2M	*9.30	8.46
4	21-Jun-10	2M	*7.50	7.00
5	20-Jul-10	2M	*7.25	7.45
6	5-Oct-10	2M	*7.00	7.34
7	11-Jan-11	2M	*6.00	5.73
8	12-Apr-11	2M	*6.30	6.67
9	11-Jul-11	2M	*5.75	5.22
10	15-Jul-11	*2H	5.75	5.06
11	4-Oct-11	*2S	*4.50	4.33
12	7-Oct-11	Stock rating system changed		
13	7-Oct-11	*2H	4.50	4.55
14	9-Jan-12	2H	*4.00	3.46

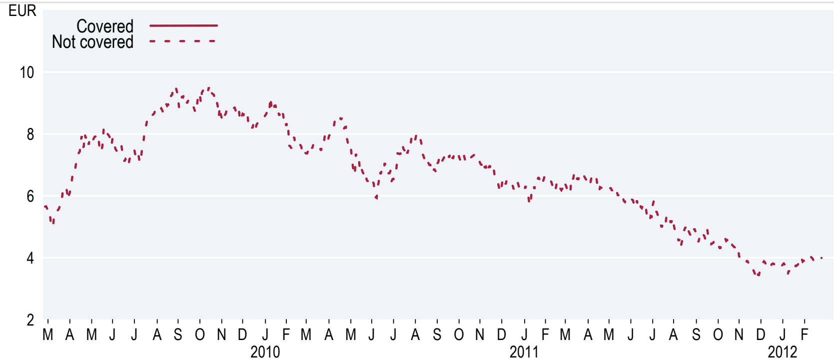
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Banesto (BTO.MC)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ignacio Moreno
Covered since May 19 2010



* Indicates change

Rating/target price changes above reflect Eastern Standard Time

CaixaBank SA (CABK.MC)

Ratings and Target Price History
Fundamental Research

Analyst: Ignacio Moreno
Covered since September 15 2011

	Date	Rating	Target Price	Closing Price
1	2-Mar-09	2M	*2.27	2.15
2	3-Aug-09	2M	*3.31	3.38
3	8-Sep-11	Coverage terminated		
4	14-Sep-11	*3H	*2.80	3.20
5	4-Oct-11	*3S	2.80	3.11
6	7-Oct-11	Stock rating system changed		
7	7-Oct-11	*3H	2.80	3.34
8	20-Jan-12	3H	*2.70	3.91

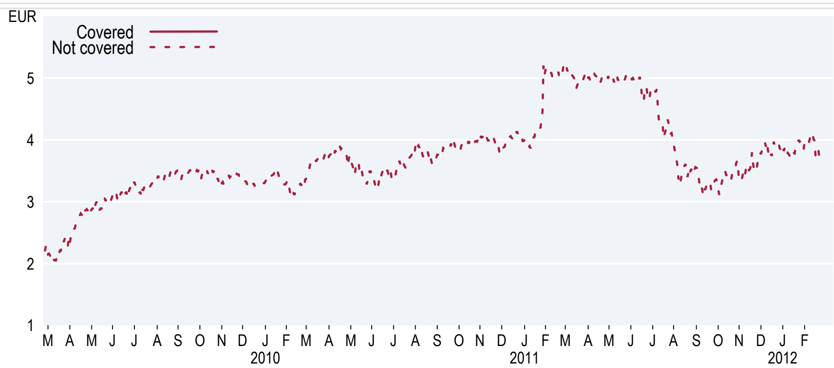
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

CaixaBank SA (CABK.MC)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ignacio Moreno
Covered since September 15 2011



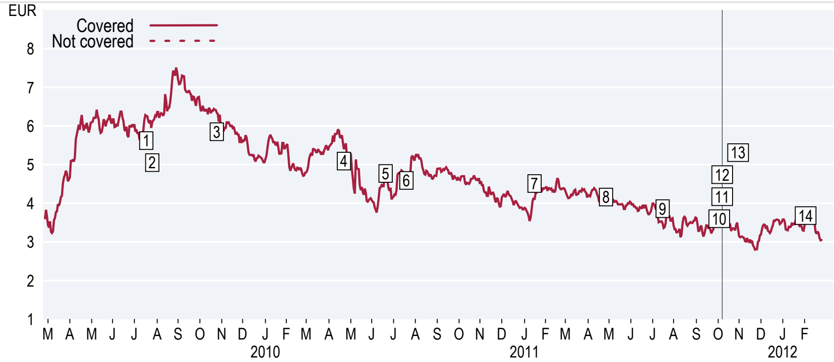
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Banco Popular Espanol (POP.MC)

Ratings and Target Price History
Fundamental Research

Analyst: Ignacio Moreno
Covered since May 19 2010



	Date	Rating	Target Price	Closing Price
1	17-Jul-09	3M	*4.68	6.26
2	27-Jul-09	3M	*5.18	6.10
3	26-Oct-09	3M	*5.42	6.34
4	22-Apr-10	*2M	*5.92	5.40
5	21-Jun-10	2M	*4.93	4.74
6	20-Jul-10	2M	*4.50	4.69
7	17-Jan-11	2M	*4.40	4.09
8	27-Apr-11	2M	*4.10	4.03
9	15-Jul-11	*3H	*3.00	3.48
10	4-Oct-11	*3S	*2.75	3.42
11	7-Oct-11	Stock rating system changed		
12	7-Oct-11	*3H	2.75	3.57
13	31-Oct-11	3H	*2.70	3.33
14	2-Feb-12	3H	*2.60	3.49

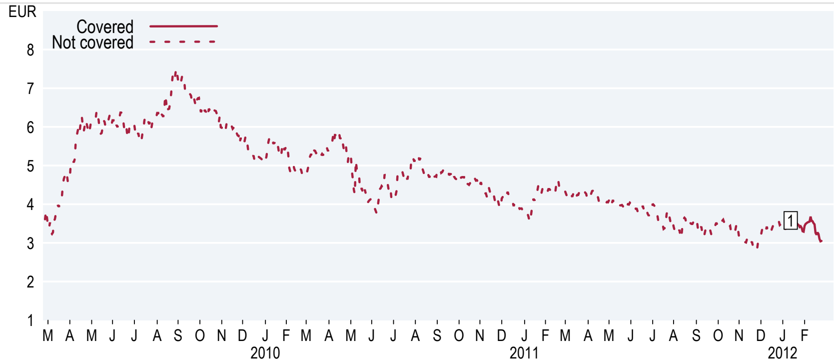
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Banco Popular Espanol (POP.MC)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ignacio Moreno
Covered since May 19 2010



	Date	Rating	Target Price	Closing Price
1	12-Jan-12	*ADD LP	-	3.39

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Banco Santander (SAN.MC)

Ratings and Target Price History
Fundamental Research

Analyst: Ronit Ghose

	Date	Rating	Target Price	Closing Price
1	19-Jun-09	1M	*9.08	8.25
2	27-Jul-09	1M	*10.31	9.71
3	30-Jul-09	1M	*11.29	9.82
4	7-Oct-09	1M	*12.27	10.86
5	25-Oct-09	1M	*12.76	11.19
6	6-Jan-10	1M	*13.25	11.75
7	5-Feb-10	1M	*11.78	9.06
8	8-Mar-10	1M	*12.27	10.24
9	3-May-10	1M	*11.78	9.09
10	21-Jun-10	1M	*11.04	9.25
11	20-Jul-10	*2M	*10.31	9.62
12	4-Aug-10	2M	*10.06	10.15
13	15-Feb-11	2M	*9.32	8.73
14	15-Jul-11	*2H	*7.85	7.12
15	28-Jul-11	2H	*7.36	7.23
16	4-Oct-11	*2S	*6.38	5.80
17	7-Oct-11	Stock rating system changed		
18	7-Oct-11	*2H	6.38	6.22
19	20-Jan-12	2H	*6.20	5.91

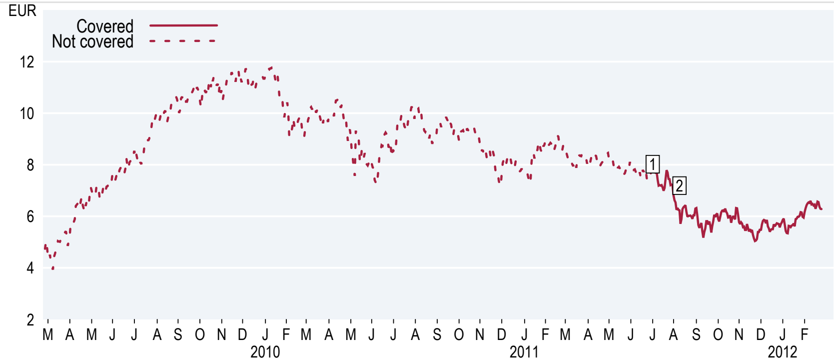
* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Banco Santander (SAN.MC)

Ratings and Target Price History
Best Ideas Research
Relative Call (3 Month)

Analyst: Ronit Ghose



	Date	Rating	Target Price	Closing Price
1	1-Jul-11	*ADD LP	-	8.02
2	9-Aug-11	*REM LP	-	6.23

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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