

# **Santander's main features and views on the regulatory response to the crisis**

## **European Commission Conglomerate's Conference**

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## **1. Santander: large but not complex**

- *Business model*
- *Legal structure*
- *Corporate Governance*

## **2. Santander views on the regulatory answer to the current crisis**

- *Capital*
- *Liquidity*
- *Corporate Governance*
- *Supervision*
- *Systemic risk*

A LARGE cross-border entity but..

- NOT complex neither overly risky
- NOT a financial conglomerate

WHY



- Mainly **retail banking**
- **Diversification & Integration** among business units
- Clear **legal structure** that fits business model
- Strong **Corporate Governance**

## BUSINESS MODEL

Commercial focus

Disciplined  
use of capital  
and financial  
strength

Efficiency

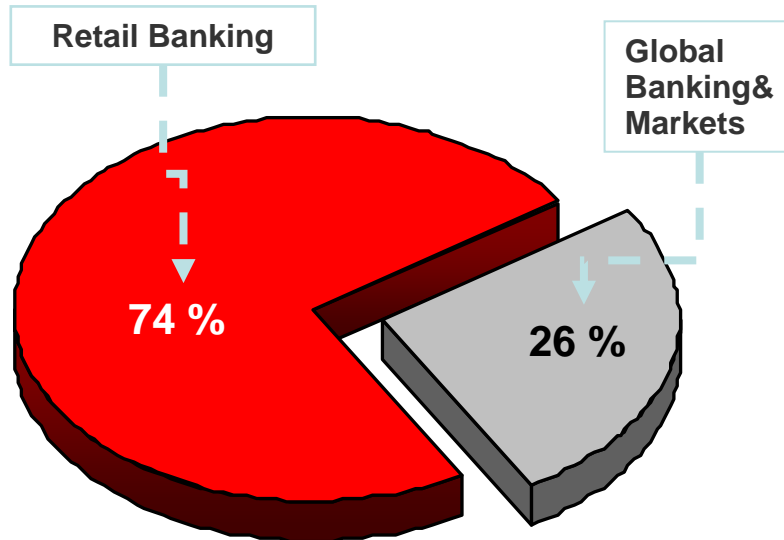


Prudence  
in risk

Geographic  
diversification

## Business Model: commercial focus

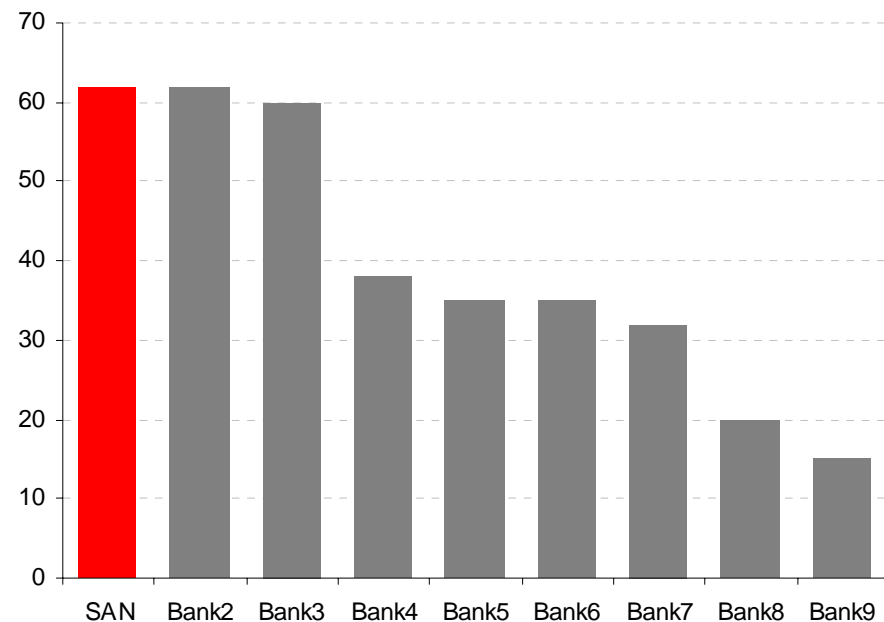
Pre-tax profit by business



**92 million customers**

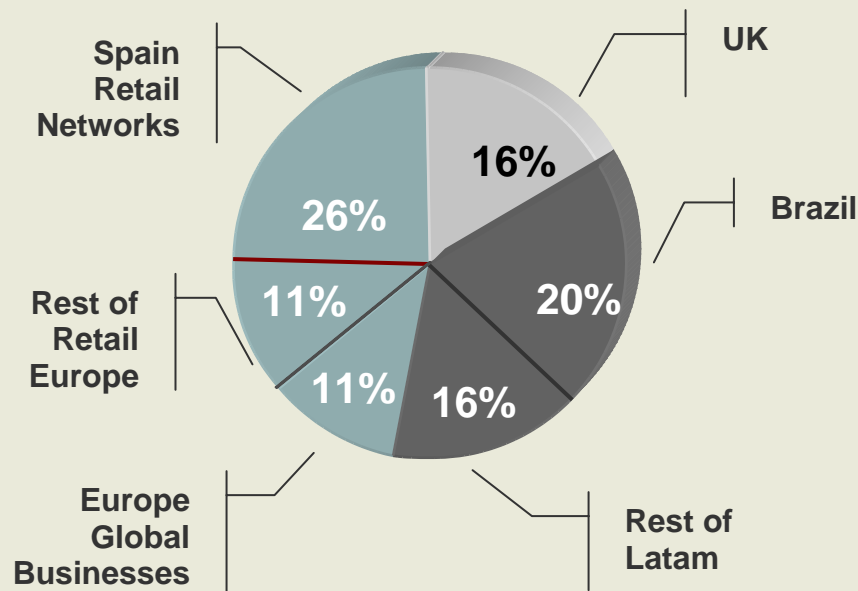
**13.660 branches**

Top European Banks: Loan/Assets (%)

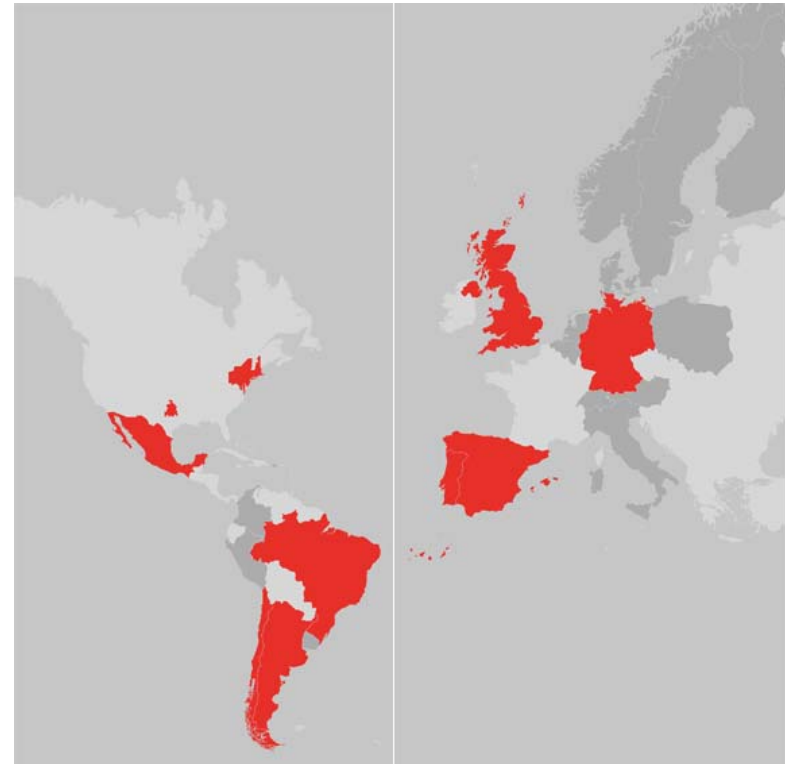


# Business Model: Geographic diversification

## 2009 Attributable profit by geographic areas



## Strong player in selected markets



## 3 Big Areas

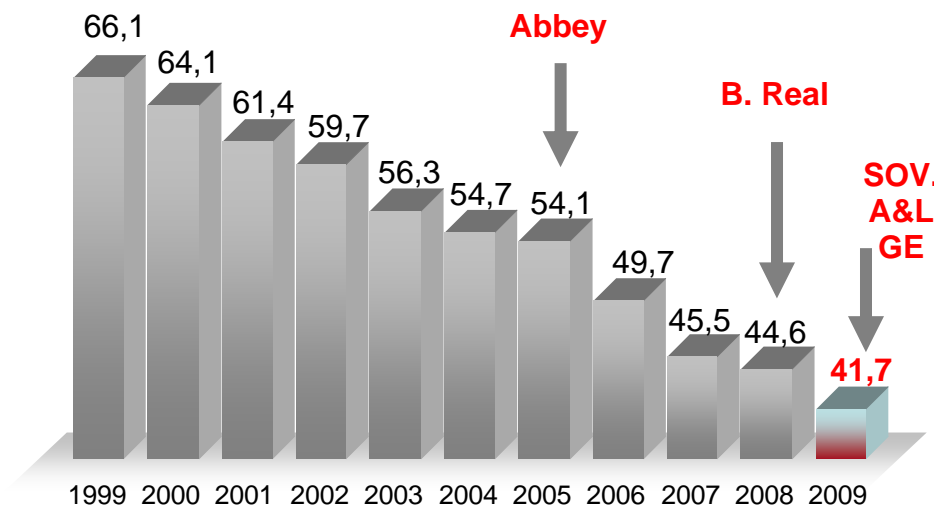


## Business Model: Efficiency

**Santander** is among the most efficient cross-border banks

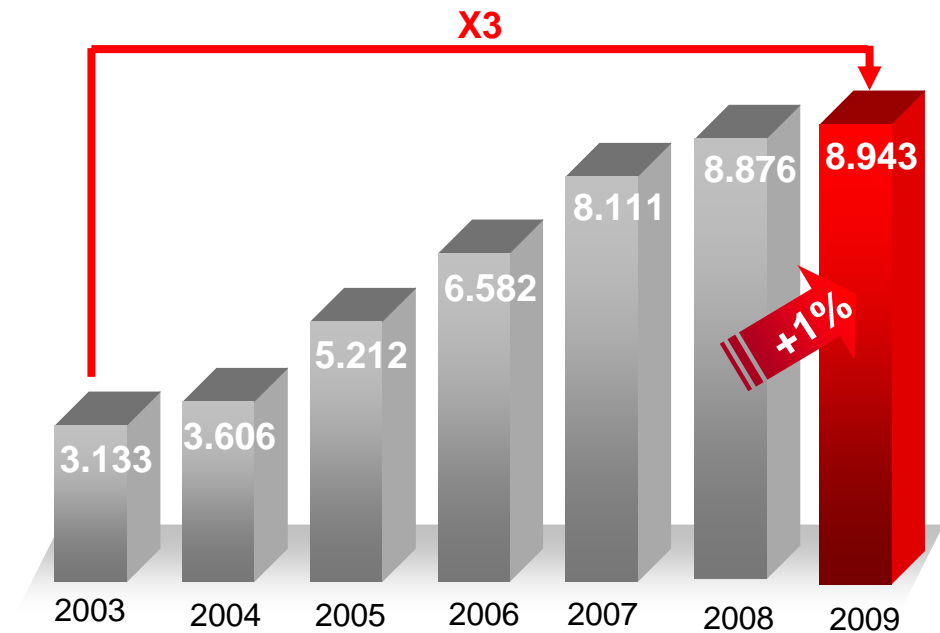
### Efficiency Ratio

(%)



### Attributable profit

(€ Bn)

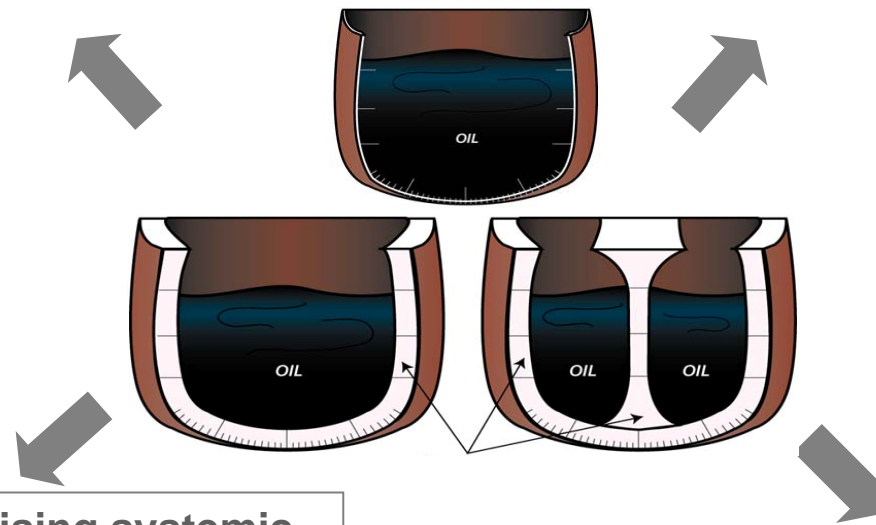


## Legal Structure Model

Stand alone subsidiaries fully autonomous in capital and liquidity terms

Full support from the parent company  
(group best practices & product development,  
plus IT operational framework)

Global corporate policies +  
Incentives for local management  
of risks

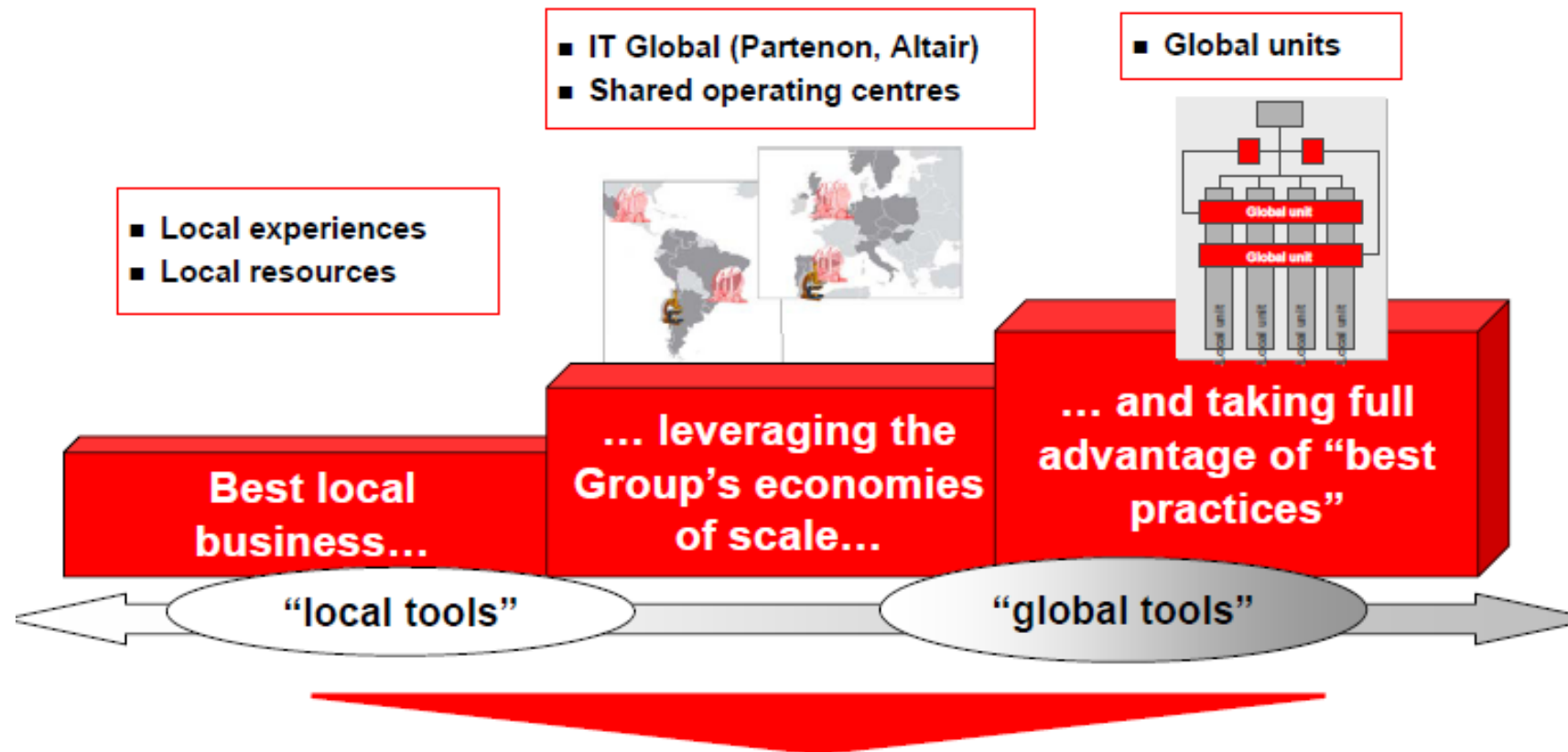


“Firewall”, neutralising systemic  
risk contagion  
(facilitates crisis management  
and Living Wills)

Two-tiered supervision:  
Home & Host supervisors

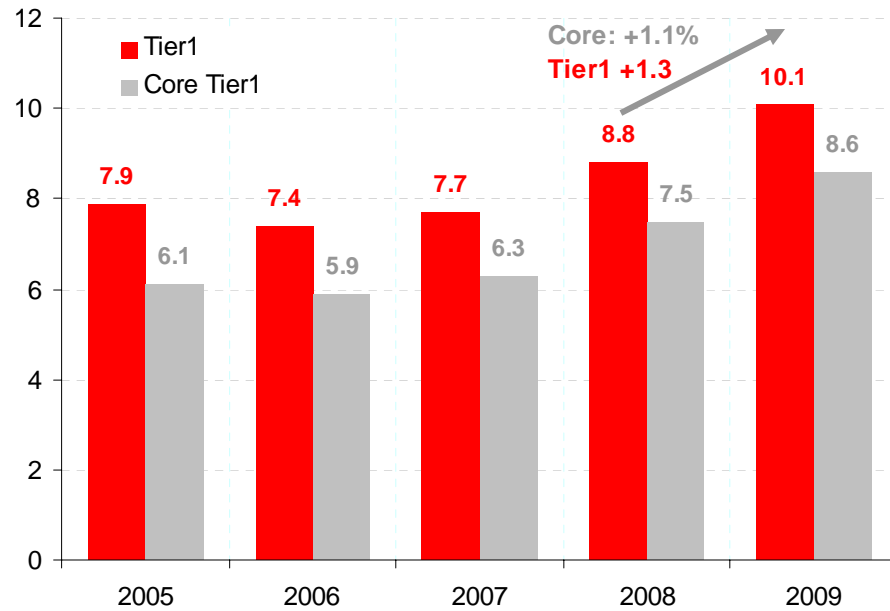
## Legal Structure Model

.... that in conjunction with providing firewalls, ensures the integration of the individual business units and, therefore, contributes to financial system integration



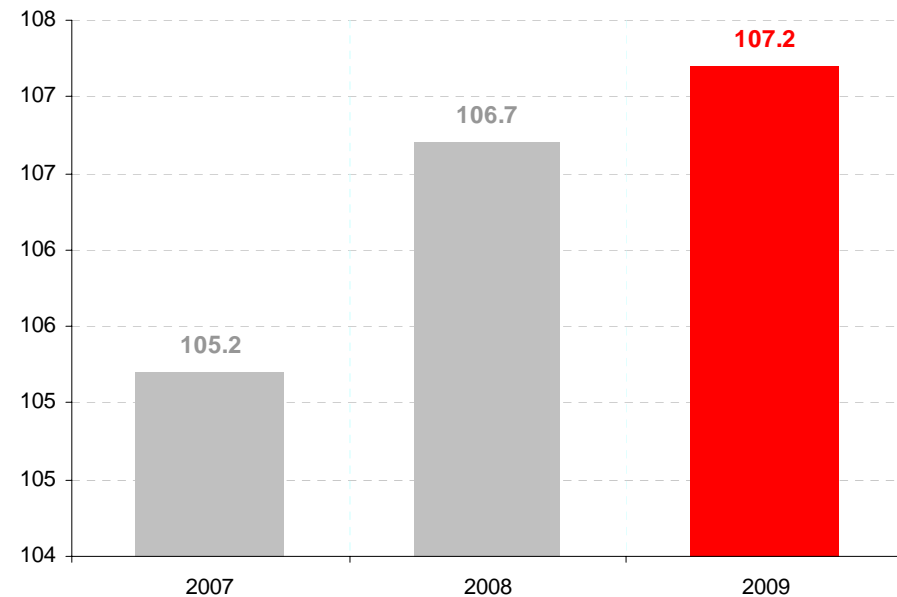
## Business Model: Strength in capital and liquidity

### Santander Core and Tier 1 ratios (in %)



Source: Santander and Bankscope  
2008 and 2009 According to BIS II, Previous data according to BIS I

### Santander Consolidated Deposits & Long-Medium Term Financing/Total credits

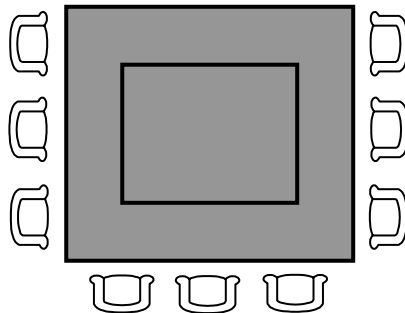


Source: Santander

# Business Model: Strong Risk Culture & Discipline

## Global Credit/Market/... Committees

Meet every day

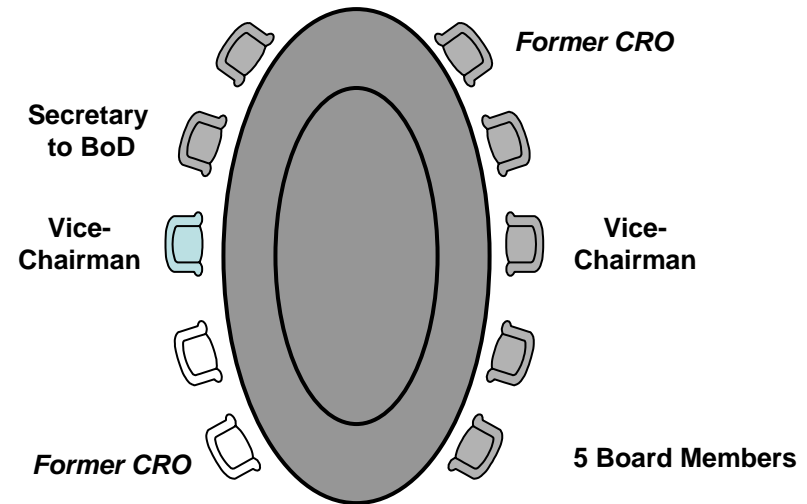


Senior Risk Team Members



## Global Risk Committee

Meets twice a week



## Board Executive Committee

Meets once a week

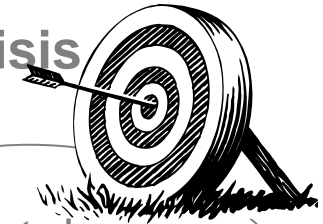
## Corporate Risk Management Principles

- Independence from business decisions
- Focus on capital preservation
- Committee based decisions
- Consistent along the Group
- Highest involvement of all levels

**INDEPENDENCE + CAPACITY TO SUPERVISE GROUP POLICIES  
CONSISTENT WITH BUSINESS STRATEGIES**

## The response to the crisis

Any reform needs to be **ON TARGET**: attack the roots of the crisis



**Two  
CAUSES of  
the crisis...**

1

Insufficient **CAPITAL** in many business models

2

**LIQUIDITY**: (“carry trade”)-  
balance sheets funded in  
the short end of the curve

... that drove  
many banks to  
the **VERGE OF  
BANKRUPTCY**  
...

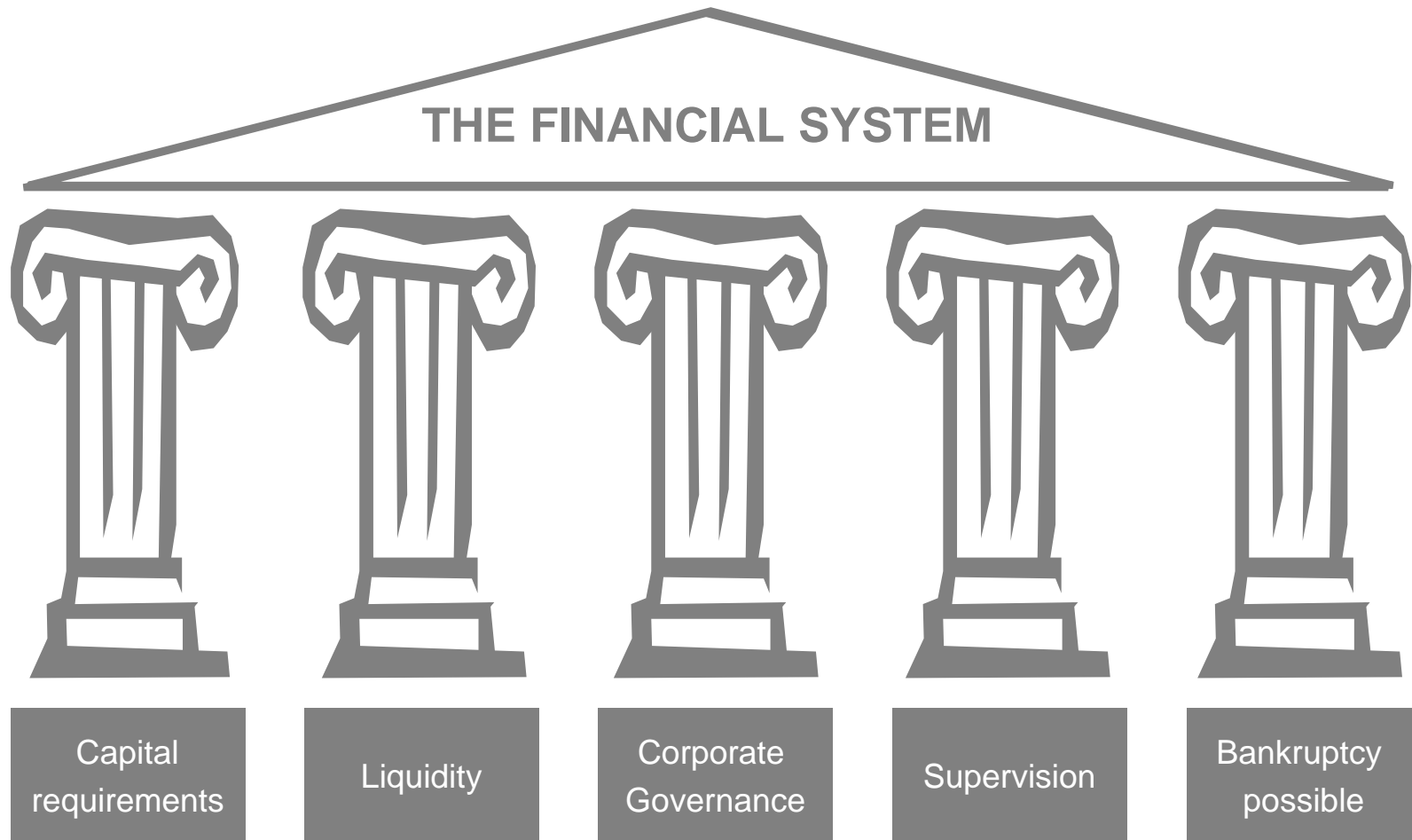
**... and one  
reason why  
banks  
needed to  
be  
RESCUED**

3

High **SYSTEMIC RISK**:

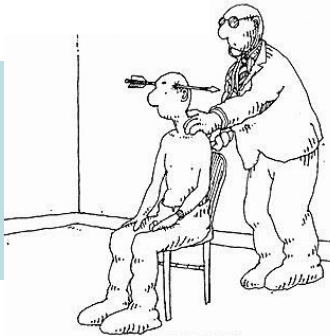
- **High level of INTERCONNECTIVITY AND COMPLEXITY**
- Lack of a system allowing banks to **FAIL IN AN ORDERLY WAY**

Re-inforcing the foundations



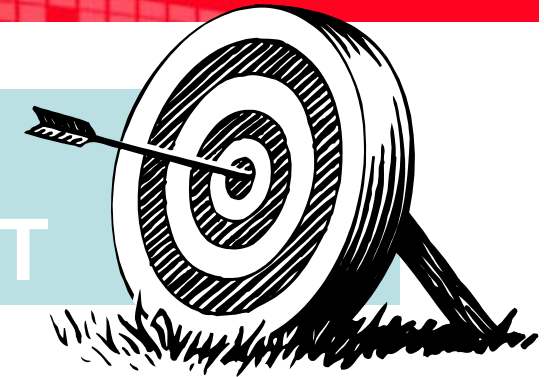
## Reinforcing the foundations: how?

### OFF TARGET



- **Too much too soon**
- Focusing on features such as **size** instead of risk
- **Two layered** supervision/regulation:- Ex. A **list** of banks “Too Big to Fail”
  - ➔ Unlevel playing field and Moral hazard

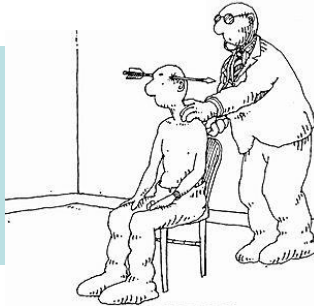
### ON TARGET



- Enhance **regulation** in line with Basel III/CRDIV
  - Enhance **supervision and corporate governance**
  - Properly assess **systemic risk**. The “too important / complex to fail” debate should end
- Consistent across sectors and jurisdictions**

## Reinforcing the foundations: capital

### OFF TARGET



**Neglecting the loss absorption capacity of some assets in a crisis**

- DTAs, MI, software *do* have and retain value

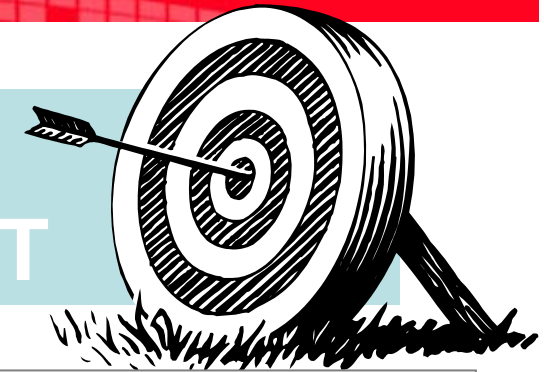
**Capital requirements related to other factors than risk**

- e.g., size

**Avoid “one size fits all” measures and unnecessary complex answers**

- Contingent capital
- Capital buffers instead of provisions

### ON TARGET



• **Homogeneity in capital calculations**

• **Better quality capital ratios**

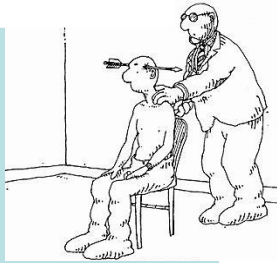
• Increased relevance of

**Common Equity and Tier1**

• **Level playing field**

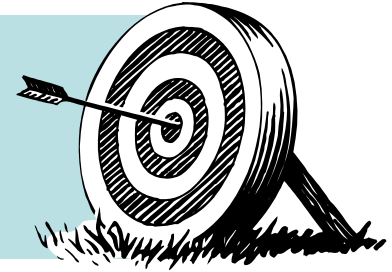
• Enhanced risk management and **supervisory oversight**

### OFF TARGET



- A **too restrictive and limiting** (“Armageddon” – type) liquidity stress scenario
- Too restrictive definition of eligible assets
- The **role of Central Banks** should not be neglected
- **Penalizing banking models** disregarding risk profile
- The NSFR needs an **adjustment to reality**

### ON TARGET



- Enhanced **supervision and good corporate governance**
- Guarantee short and long term liquidity **without jeopardizing the maturity transformation function**
- **LCR** (or similar)
- **Monitor the liquidity soundness** of the system



## Reinforcing the foundations: supervision

Transferring direct supervision of certain entities is not the right answer.

We need:

- ☑ **Macro-supervision** to be reinforced at an international level so that it provides a global view of risks in the financial sector.
- ☑ Micro-supervision must be **intrusive, close, rigorous, pro-active, and comprehensive.**
- ☑ Enhanced and harmonized **early intervention tools and resolution regimes**
- ☑ Homogeneous supervision and **single rulebook** to achieve convergence.
- ☑ **College of Supervisors** for cross-border entities to achieve co-operation among supervisors.



## Reinforcing the foundations: corporate governance

Apart from good supervision and a prudential framework to control risks we need to improve Corporate Governance.

As per the Basel Committee report on Principles for the improvement on Corporate Governance Practices in Banking Institutions (March 2010) this can be achieved by:

- ✓ **Identifying, controlling and managing risk**, both in individual institutions and groups, in accordance with risk management systems and internal control tools that are appropriate for the business and risk profile of the institution
- ✓ **Having independent risk management functions** with sufficient authority, prestige, independence, resources and access to the Board
- ✓ **Promoting an active monitoring by the Board** of the design and implementation of the institution's remuneration policies, including gradual adaptation to long-term principles and prudent risk-taking



## Reinforcing the foundations: systemic risk

- ALL institutions should be able to fail without imposing an undue social burden
  - ➔ Establish recovery and resolution plans (living wills)
  - ➔ Enhanced early intervention tools and resolution regimes
  - ➔ Strengthen international consistency and co-ordination in crisis management
- ANY additional requirement because of systemic risk should be proportionate to this risk in order to provide the right incentives:
  - ➔ Should be continuous to avoid moral hazard and arbitrage
  - ➔ Should be *systemic-risk sensitive* and take into account not just size but interconnectedness, complexity and herd behavior.

**The new regulation should encourage banks to be Manageable, Transparent, Supervisable, and “Resolvable”**



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