Introduction

Regulatory environment in 2018

As a Spanish credit institution, BBVA is subject to Directive 2013/36/EU of the European Parliament and of the Council dated June 26, 2013, on access to the activity of credit institutions and investment firms ("Directive CRD IV") amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC by means of which the EU began, as of January 1 2014, to implement the capital reforms agreed within the framework of Basel III, thus establishing a period of gradual implementation for certain requirements until January 1 2019.

The major regulation governing the solvency of credit institutions is Regulation (EU) No 575/2013 of the European Parliament and of the Council dated June 26, 2013, on prudential requirements for credit institutions and investment firms, amending Regulation (EU) No 648/2012 ("CRR" and, jointly with Directive CRD IV and any other CRD IV implementation measure, "CRD IV"), which is complemented by several binding Regulatory Technical Standards that apply directly to EU member states, there being no need to implement national measures.

Directive CRD IV was transposed to Spanish national law by means of Royal Decree-Law 14/2013 dated November 29 ("RD-L 14/2013"), Law 10/2014, Royal Decree 84/2015 dated February 13 ("RD 84/2015"), Bank of Spain Circular 2/2014 dated January 31 and Circular 2/2016 dated February 2 ("Bank of Spain Circular 2/2016").

Regulatory changes

BIS III Reform: in order to strike a balance between risk sensitivity, simplicity and comparability, the Basel Committee has reformed the Basel III framework. The main amendments are focused on internal models, the standard credit risk method, the market risk framework, operational risk and capital floors in the advanced measurement approach based on the standardised approach. The reform has been approved by the Basel Committee meeting on December 8, 2017, with an implementation date of January 1, 2022. In the case of capital floors, its introduction is gradual over a period of 5 years, from a floor of 50% on January 1, 2022 to 72.5% on January 1, 2027. The Committee also introduced an additional leverage ratio for global systemically important banks (G-SIBs).

CE reforms and provisions: in Europe, on November 23, 2016 the European Commission published a new reform package amending both the prudential banking regime (CRR) and the resolution regime (Bank Recovery and Resolution Directive, BRRD). This revision includes the implementation of international standards into European legislation (regulation later than 2010 adopted by the Basel Committee – except for standards approved in December, 2017 – and the total loss absorbing capacity (TLAC)), the final design of the Minimum Requirement for own funds and Eligible Liabilities (MREL) along with a package of technical improvements. At the same time, a proposal of directive has also been put forward to harmonize the hierarchy of senior debt creditors within the European Union. This directive was approved in December 2017.

As of today discussions continue within the European Council and Parliament with the aim of reaching an agreement on the texts that will be the subject of negotiation between the European Commission, the European Council and the European Parliament. In this respect, in December 2018 they reached an agreement on the main points of the reform. However, on December 27, 2017 the Official Journal of the European Union (OJEU) published the agreement reached by the fast-track procedure relating to the following three aspects of the reform:

1. A transitional period of 5 years (2018-2022) during which the banks will be allowed to mitigate partially the negative impact of the increased provisions under the new IFRS 9 accounting standard on their CET1 capital, in accordance with the provisions of Regulation (EU) 2017/2395 (developed by article 473 *bis* of Regulation (EU) No. 575/2013), to which BBVA Group has adhered voluntarily. In this regard and during that transitional period, information detailing the impact of not applying those transitory arrangements will be reported. For these purposes, EBA has published guidelines that specify the uniform format that should be used to disclose the information required during the transitional period (EBA/GL/2018/01).

   In this report, the phased-in capital ratios as of December 2018 are calculated taking into account the aforementioned transitional IFRS 9 treatment, whereas the fully loaded capital ratios incorporate the full impact of these new

accounting regulations.

2. An additional period of three years (2018-2020) during which exposure with respect to central governments or central banks of the Member States denominated and financed in a currency of another Member State remains exempt from calculation of thresholds of large exposures.

3. Creation of a new category of subordinated senior debt in the hierarchy of bank creditors that will be eligible for the purposes of TLAC.

Reform of the securitisation framework: with respect to securitisations, the European Commission published a proposal in 2015 aimed to facilitate the development of a securitisation market in Europe. The package consisted of two draft Regulations:

1. Securitisation Regulation: combines the rules applicable to all the securitisations including high-quality securitisation (simple, transparent and standardised (STS) securitisation), which is now dispersed across several legal provisions. This rationalizes and simplifies the existing rules and establishes a general system for defining STS securitisation.

2. Text modifying the CRR with respect to the capital requirements for securitisation positions. Gives a more risk-sensitive treatment to STS securitisations.

These two regulations were published in the OJEU on December 28, 2017, with an application date of January 1, 2019 for securitisations issued as of that date. For securitisations made before January 2019, entities will continue to apply the current regime until December 31, 2019.

Management and framework of NPLs: in July 2017, the European Council published a package of measures to address non-performing loan assets (NPL) in Europe. For this purpose, the European Central Bank (ECB) has established supervisory expectations for Pillar II on prudential provisions for non-performing loan exposures classified as such as of April 1, 2018. Its application date is from 2021 SREP exercise onwards (Supervisory Review and Examination Process). The supervisory expectations on prudential provisions applicable to stock (non-performing loan exposures classified as such before April 1, 2018) will be treated by the ECB within the individual dialog with each bank.

Meanwhile, the EC is working on a Pillar I proposal for a regulation modifying the CRR with regard to the minimum coverage of losses arising from non-performing loan exposures. After a negotiation period between the EC, the European Council and the European Parliament, an agreement has been reached in December 2018 that is expected to be applicable throughout 2019. With regard to transparency, the European Banking Authority (EBA) has released guidelines on the NPLs information disclosure that will apply as of December 31, 2019, and guidelines regarding the NPLs management that will be applicable as of June 30, 2019.

Changes in the Pillar III disclosure framework: the Basel Pillar III framework is being revised by the Basel Committee on Banking Supervision (BCBS), which has divided the process into three phases.

- Phase I: the disclosure requirements of the first phase of review were published in January 2015, and they replace the disclosure requirements published in 2014 (modified in July 2009). It includes standardised templates related to credit and market risks, as well as the distinction between the accounting perimeter and regulatory perimeter.

- Phase II: on a second phase, the BCBS has reviewed the disclose requirements collected on the Basel rules that are currently in force and has consolidated them under the document "Disclosure requirements for the Third Pillar – consolidated and enhanced framework", published in March 2017. It includes standardised templates related to countercyclical buffer, prudent valuation, LCR, etc.

- Phase III: as of December, 11, 2018, BCBS has published the requirements of the third phase of revision of the Pillar 3 framework under the document "Disclosure requirements for the Third Pillar – updated framework", which includes, among others, new information disclosure requirements derived from the conclusion of the Basel III reforms.

The disclosure requirements for the first phase of the review of Pillar 3 entered into force in December 2017, while the disclosure requirements for the second phase have different implementation dates, with the first phase coinciding with the close of 2017. Furthermore, the implementation date of the third phase is, in general, on January 1, 2022, with the exception of certain forms that have been moved forward to the end of 2020.

Contents of the 2018 Prudential Relevance Report

Article 13 of the CRR establishes that the parent entities of the European Union are subject based on their consolidated situation to the disclosure requirements contained in the eighth part of the CRR.

This report includes the prudential information of BBVA consolidated group as of December 31, 2018. This report has been prepared in compliance with the requirements set by Part Eight of the CRR, as well as any applicable guidelines published by the European Banking Authority.

Furthermore, the data published in the Prudential Relevance Report (Pillar III) was prepared in accordance with internal control processes described in the following standard templates.

These policies ensure that the information included in Pillar III is subject to the internal control framework defined by the Group, as well as adequate internal and external revision (by an independent expert), in compliance with the Guidelines on disclosure requirements under Part Eight of Regulation (EU) No.575/2013 (EBA/GL/2016/11).

In general, the following EBA guidelines are highlighted:

- Guidelines on materiality, proprietary information, and confidentiality, and on the frequency of disclosure of information according to Article 432, sections 1 and 2, and Article 433 of Regulation (EU) No. 575/2013 (EBA/GL/2014/14). These guidelines detail the process and the criteria to be followed regarding the principles of materiality, proprietary information, confidentiality and the right to omit information. They also provide guidance for entities to evaluate the need to publish information more frequently than the annual. The Executive Commission of the Bank of Spain adopted these guidelines in February 2015.

- Guidelines on disclosure requirements under Part Eight of Regulation (EU) No. 575/2013 (EBA/GL/2016/11). These guidelines provide guidance in relation to the information that entities must disclose in application of the corresponding articles of the Part Eight and with the presentation of said information. The Executive Commission of the Bank of Spain adopted these guidelines in October 2017.

- Guidelines LCR disclosure to complement the information on liquidity risk management in accordance with Article 435 of Regulation (EU) No. 575/2013 (EBA/GL/2017/01). These guidelines specify the general framework for the disclosure of information on risk management under Article 435 of Regulation (EU) No. 575/20132 in relation to liquidity risk, establishing a harmonised structure for the disclosure of the information required by Article 435, point 1 of said Regulation. The Executive Commission of the Bank of Spain adopted these guidelines in July 2017.

- Guidelines on disclosure of encumbered and unencumbered assets in accordance with Article 443 of Regulation (EU) No. 575/2013 (EBA/GL/2014/03). The Executive Commission of the Bank of Spain adopted these guidelines in September 2014.

- Guidelines on uniform disclosure of information under Article 473-a of Regulation (EU) No 575/2013 with regard to the transitional provisions for mitigating the impact on own funds from the introduction of IFRS 9 (EBA/GL/2018/01). The Executive Committee of the Bank of Spain has adopted these guidelines in February 2018.

- Guidelines on sound remuneration policies under Articles 74, paragraph 3, and 75, paragraph 2, of Directive 2013/36/EU and disclosure of information under Article 450 of Regulation (EU) No 575/2013 (EBA/GL/2015/22). The Executive Commission of the Bank of Spain adopted these guidelines in July 2016.

Annex V of this report, available on the Group's website, gathers the correspondence of the articles of Part Eight of the CRR on information disclosure with the different headings of the document (or other public documents) where the required information is located.

In an exercise of transparency, as of December 31, 2018, BBVA includes the following standard templates on disclosure of information recommended by the different regulators. They can be seen in the following table:

Disclosure requirements

Template	Guidelines on disclosure requirements EBA/GL/2016/11	Pillar III Section
EU OV1	Overview of RWAs	2.5
EU LI1	Differences between the accounting and regulatory scopes of consolidation and mappping of financial statement categories with regulatory risk categories	1.1.3
EU LI2	Main sources of differences between regulatory exposure amounts and carrying values in financial statements	1.1.3
EU LI3	Outline of the differences in the scopes of consolidation (entity by entity)	Pillar III Annexes
EU INS1	Non-deducted participations in insurance undertakings	N/A
EU CR1-A	Credit quality of exposures by exposure class and instrument	3.2.3.4
EU CRB-B	Total and average net amount of exposures	3.2.3.2
EU CRB-C	Geographical breakdown of exposures	3.2.3.3
EU CR1-C	Credit quality of exposures by geography	3.2.3.3
EU CRB-D	Concentration of exposures by industry or counterparty types	3.2.3.5
EU CR1-B	Credit quality of exposures by industry or counterparty types	3.2.3.5
EU CRB-E	Maturity of exposures	3.2.3.6
EU CR1-D	Ageing of past-due exposures	3.2.3.6
EU CR2-A	Changes in stock of general and specific credit risk adjustments	3.2.3.8
EU CR2-B	Changes in stock of defaulted and impaired loans and debt securities	3.2.3.8
EU CR1-E	Non-performing eand forborne exposures	3.2.3.9
EU CR4	Standardised approach: credit risk exposure and credit risk mitigation effects	3.2.4.3
EU CR5	Standardised approach	3.2.4.3
EU CR6	IRB approach: credit risk exposures by exposure class and PD range	3.2.5.2
EU CR9	IRB approach: backtesting of PD per exposure class	3.2.5.2
EU CR8	RWA flow statements of credit risk exposures under the IRB approach	3.2.5.2
EU CR10 (1)	IRB: specialised lending	3.2.5.4
EU CR10 (2)	IRB: equity	3.2.5.5
EU CCR5-A	Impact of netting and collateral held on exposure values	3.2.6.2
EU CCR1	Analysis of the counterparty credit risk exposure by approach	3.2.6.2
EU CCR3	Standardised approach: counterparty credit risk exposures by regulatory portfolio and risk	3.2.6.2.1
EU CCR4	IRB: counterparty credit risk exposure by portfolio and PD scale	3.2.6.2.2
EU CCR5-B	Composition of collateral for exposures to counterparty credit risk	3.2.6.2.3
EU CCR6	Credit derivatives exposures	3.2.6.2.4
EU CCR7	RWA flow statements of CCR exposures under the IMM	N/A
EU CCR2	Credit valuation adjustment (CVA) capital charge	3.2.6.3
EU CCR8	Exposures to central counterparty clearing houses	3.2.6.4
EU CR3	Credit risk mitigation techniques overview	3.2.8.3
EU MR1	Market risk under standardised approach	3.3.3
EU MR3	IMA values for trading portfolios	3.3.4.2.2
EU MR2-A	Market risk under the internal model approach (IMA)	3.3.4.2.2
EU MR2-B	RWA flow statements of market risk exposures under an IMA	3.3.4.2.2
EU MR4	Comparison of VaR estimates with gains/losses	3.3.4.2.3

Template	Guidelines on LCR disclosure (EBA/GL/2017/01)	Pillar III Section
EU LIQ1	LCR disclosure template	3.7.5

Template	RTS on Asset Encumbrance disclosure (EBA/RTS/2017/03)	Pillar III Section
Encumbered and unencumbered assets		3.7.6
Collateral received		3.7.6
Sources of encumbrance		3.7.6

Template	Guidelines on uniform disclosure of IFRS9 transitional arrangements (EBA/GL/2018/01)	Pillar III Section
IFRS9 - FL	Comparison of own funds and capital leverage ratios of entities with and without the application of the transitional arrangements of IFRS9 or similar Expected Credit Losses (ECL)	2.3

Template	RTS on prudent valuation (EBA/RTS/2014/06)	Pillar III Section
Prudent Valuation Adjustments		3.3.4.2.1

Template	Leverage Ratio - Commission Implementing Regulation (EU) 2016/200	Pillar III Section
LRSum	Summary reconciliation of accounting assets and leverage ratio exposures	4.1
LRCom	Leverage ratio common disclosure	Pillar III Annexes
LRSpl	Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)	Pillar III Annexes

Template	ITS on Disclosure for Own Funds by institutions (EBA/ITS/2013/01)	Pillar III Section
Capital instruments' main features template		Pillar III Annexes
Transitional own funds disclosure template		Pillar III Annexes

Template	Countercyclical capital buffer - Commission Delegated Regulation (EU) 2015/1555	Pillar III Section
Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer		Introduction
Amount of institution-specific countercyclical capital buffer		Introduction

Template	Disclosure requirements for the Third Pillar – Revised framework - Basel Committee	Pillar III Section
SEC1	Securitisation exposures in the banking book	3.2.7.5
SEC4	Securitisation exposures in the banking book and associated regulatory capital requirements – bank acting as originator or as sponsor	3.2.7.6
SEC3	Securitisation exposures in the banking book and associated capital requirements – bank acting as investor	3.2.7.7.2

Template	Disclosure requirements for the Third Pillar – Consolidated and enhanced framework - Basel Committee	Pillar III Section
CC1	Composition of regulatory capital	Pillar III Annexes
CC2	Reconciliation of regulatory capital to balance sheet	1.1.3

Composition of Capital

Capital requirements

The regulations require institutions to have a higher and better quality capital level, increase capital deductions and review the requirements associated with certain assets. Unlike the previous framework, the minimum capital requirements are complemented with requirements for capital buffers and others relating to liquidity and leverage. Bank capital under CRD IV mainly comprises of the elements described in section 2.1 herein.

The most relevant aspects affecting the elements making up minimum capital requirements and risk-weighted assets are detailed in greater depth in section 2.4 of this document.

In this regard, article 92 of the CRR establishes that credit institutions must maintain at all times the following own funds requirements:

a. Common Equity Tier1 capital ratio of 4.5%, obtained as Common Equity Tier1 capital expressed as a percentage along the total amount of risk-weighted assets.

b. Tier1 capital ratio of 6%, calculated as the percentage between the Tier 1 capital expressed as a percentage along the total amount of risk-weighted assets.

c. Total capital ratio of 8%, expressed as the percentage of the own funds along the total amount risk-weighted assets.

Notwithstanding the application of the Pillar 1 requirement, CRD IV allows competent authorities to require that credit institutions maintain more own funds than the Pillar 1 requirements to cover risks other than those already covered by the Pillar 1 requirement (this power of the competent authority is commonly known as Pillar 2).

Furthermore, in accordance with CRD IV, credit institutions must comply with the "combined requirement of capital buffers" from 2016 onwards. The "combined buffer requirement" has incorporated five new capital buffers: (i) the capital conservation buffer; (ii) the buffer for global systemically important banks (the "G-SIB buffer"); (iii) the countercyclical capital buffer specific to each bank; (iv) the buffer for other systemically important financial institutions (the "D-SIB buffer"); and (v) the buffer against systemic risks. The "combined capital buffer requirement" must be met with Common Equity Tier 1 capital ("CET1") in addition to that which is provided to meet the minimum capital required by "Pillar 1" and "Pillar 2".

Both the capital conservation buffer as well as the G-SIB buffer (where appropriate) will apply to credit institutions, as it establishes a percentage over 0%.

The buffer for global systemically important banks applies to those institutions on the list of global systemically important banks, which is updated annually by the Financial Stability Board ("FSB"). Given that BBVA is not considered as G-SIB since November 2015 (effective January 1, 2017), this buffer does not apply to BBVA.

For more details on the quantitative indicators for assessing the global systemically important banks, see the document "G-SIBs Information" in the section **Shareholders and Investors / Financial Information** on the BBVA Group website.

The Bank of Spain has extensive discretionary powers as regards the countercyclical capital buffer peculiar to each bank, the buffer for other systemically important financial

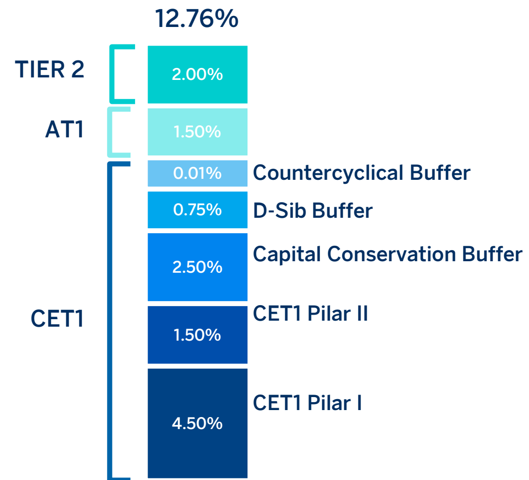
institutions (which are those institutions considered to be systemically important local financial institutions "D-SIB") and the buffer against systemic risks (to prevent or avoid systemic or macroprudential risks). The European Central Bank (ECB) has the powers to issue recommendations in this respect following the entry into force on November, 4, 2014 of the Single Supervisory Mechanism (SSM).

In December 2015, the Bank of Spain agreed to set the countercyclical capital buffer that applies to credit exposures in Spain at 0% as of January 1 2017. These percentages will be reviewed every quarter, as the Bank of Spain decided in December 2018 to keep the countercyclical capital buffer at 0% for the first quarter of 2019.

As far as BBVA is concerned, after the supervisory review and evaluation process ("SREP") conducted in 2018, ECB has notified on February, 14, 2019, that BBVA Group, starting from March, 1, 2019 maintain a phased-in and fully loaded ratio (given that the transitional period of capital buffers has ended in December 2018) (i) CET1 of 9.26% at the consolidated level and 8.53% at the individual level and (ii) a total capital ratio of 12.76% at the consolidated level and 12.03% at the individual level.

The consolidated total capital requirement includes: i) the minimum capital requirement of Common Equity Tier 1 (CET1) of Pillar 1 (4.5%); ii) the capital requirement of Additional Tier 1 (AT1) of Pillar 1 (1.5%); iii) the capital requirement of Tier 2 of Pillar 1 (2%); iv) the CET1 requirement of Pillar 2 (1.5%), which remains at the same level as established after the last SREP; v) the capital conservation buffer (2.5% of CET1); vi) the capital buffer for Other Systemically Important Institutions (O-SIIs) (0.75% of CET1); and vii) the countercyclical capital buffer (0.01% of CET1).

Chart 1: Capital Requirements (Fully loaded)



As of December 31, 2018, BBVA maintains fully loaded CET1 ratio and total ratio of 11.3% and 15.5%, respectively (in phased-in terms, CET1 and total ratio of 11.6% and 15.7%, respectively) reinforcing its equity position in the Group.

The following table presents the distribution by geographic areas of the credit exposure for calculation of the countercyclical capital buffer:

Table 1. Geographical breakdown of relevant credit exposures for the calculation of the countercyclical capital buffer (Million Euros. 12-31-18)

	General credit exposures [1]		Trading book exposure		Securitisation exposure		Own funds requirements					
	Exposure value for SA	Exposure value for IRB	Sum of long and short position of trading book	Trading book exposure value for internal models	Exposure value for SA	Exposure value for IRB	Of which: General credit exposures	Of which: Trading book exposures	Of which: Securitisation exposures	Total	Own funds requirements weights	Countercyclical capital buffer rate
Geographical breakdown												
Sweden	36	193	-	5	-	-	6	0	-	7	0,0%	2,0%
Norway	20	16	-	10	-	-	1	0	-	1	0,0%	2,0%
Slovakia	6	153	-	-	-	-	17	-	-	17	0,1%	1,3%
Iceland	0	0	-		-	-	0	0	-	0	0,0%	1,3%
Lithuania	0	0	-	-	-	-	0	-	-	0	0,0%	0,5%
United Kingdom	526	5.214	8	116	-	-	198	4	-	202	1,0%	1,0%
Czech Republic	2	5	-	-	-	-	0	-	-	-	0,0%	1,0%
Hong Kong	51	1.175	-	-	-	-	16	-	-	16	0,1%	1,9%
Total countries with countercyclical capital buffer stablished	**641**	**6.757**	**8**	**131**	**-**	**-**	**239**	**5**	**-**	**243**	**1,2%**	
Peru	20.485	568	3.579	-	-	-	940	2	-	943	4,5%	-
Germany	268	4.370	1	74	-	-	165	2	-	167	0,8%	-
Argentina	8.174	209	1.452	0	-	-	340	14	-	353	1,7%	-
Spain	30.606	167.840	31	7	-	5.593	5.230	5	431	5.666	27,2%	-
United States	80.901	13.231	6.741	73	4.595	-	4.448	8	368	4.824	23,2%	-
France	974	6.906	0	86	-	-	220	4	-	224	1,1%	-
Italy	248	6.358	-	23	-	-	209	1	-	210	1,0%	-
Mexico	43.202	37.528	50	254	28	-	3.200	24	2	3.226	15,5%	-
Portugal	4.448	663	11	1	-	-	273	0	-	273	1,3%	-
Turkey	56.603	566	11.347	0	-	-	2.829	2	-	2.831	13,6%	-
Colombia	14.291	622	36.276	3	-	-	761	7	-	768	3,7%	-
Total countries with a 0% countercyclical buffer or without countercyclical capital buffer (with own funds requirements greater than 1%)	**260.200**	**238.859**	**59.489**	**521**	**4.623**	**5.593**	**18.616**	**67**	**800**	**19.484**	**93,6%**	
Other areas	12.344	15.032	145	194	-	-	1.084	5	-	1.090	5,2%	-
Total countries without countercyclical capital buffer (with own funds requirements less than 1%)	**12.344**	**15.032**	**145**	**194**	**-**	**-**	**1.084**	**5**	**-**	**1.090**	**5,2%**	
Total	**273.186**	**260.649**	**59.642**	**846**	**4.623**	**5.593**	**19.939**	**78**	**800**	**20.817**	**100%**	

(1) Credit exposures exclude exposures to Central Governments or Central Banks, Regional Governments or Local Authorities, Public sector entities, Multilateral Development Banks, International Organizations and Institutions in accordance with art. 140.4 of Directive 2013/36/EU

	Amount
Total risk exposure amount	348,264
Institution specific countercyclical buffer rate [2]	0.01%
Institution specific countercyclical buffer requirement	45

(2) Countercyclical capital buffer calculated as of December 2018 in accordance with Commission Delegated Regulation (EU) 2015/1555

Leverage Ratio

In order to provide the financial system with a metric that serves as a backstop to capital levels, irrespective of the credit risk, a measure complementing all the other capital indicators has been incorporated into Basel III and transposed to the solvency regulations. This measure, the leverage ratio, can be used to estimate the percentage of the assets financed with Tier 1 capital.

Although the carrying amount of the assets used in this ratio is adjusted to reflect the bank's current or potential leverage with a given balance-sheet position, the leverage ratio is intended to be an objective measure that may be reconciled with the financial statements.

As of December 31, 2018, BBVA Group had a Leverage Ratio of 6.4% (fully loaded), and a phased-in ratio of 6.5%, above the minimum requirement set at 3%, and continuing to compare very favourably with the rest of its peer group.