4. Leverage Ratio

4.1. Leverage Ratio definition and composition

The leverage ratio (LR) is a regulatory measure (not risk-based) complementing capital designed to guarantee the soundness and financial strength of institutions in terms of indebtedness.

In January 2014, the Basel Committee on Banking Supervision published the final version of the "Basel III leverage ratio framework and disclosure requirements", which has been included through a delegated act that amends the definition of leverage ratio in the CRR regulation.

Pursuant to article 451, section 2 of the CRR, on June 15, 2015 the EBA published the final draft of the Implementing Technical Standard (ITS) on leverage ratio disclosures for breaking down the leverage ratio, which has been applied in this report.

The leverage ratio is defined as the quotient of eligible Tier 1 capital and exposure.

Described below are the elements making up the leverage ratio, in accordance with the "EBA Final Draft Implementing Technical Standards on disclosure of the leverage ratio under Article 451(2) of Regulation (EU) No. 575/2013 (Capital Requirements Regulation – CRR) - Second submission following the EC's Delegated Act specifying the LR ," published by the EBA on June 15, 2015:

- Tier 1 capital (letter h in the following table): section 2.2. of this Document presents details of the eligible capital, which has been calculated based on the criteria defined in the CRR.
- Exposure: as set out in article 429 of the CRR, the exposure measurement generally follows the carrying amount subject to the following considerations:
  - On-balance-sheet exposures other than derivatives are included net of allowances and accounting valuation adjustments.
  - Measurement of the Group's total exposure is composed of the total assets as per financial statements adjusted for reconciliation between the accounting perimeter and the prudential perimeter.

Total exposure for the purpose of calculating the Group's leverage ratio is composed of the sum of the following items:

- On-balance asset positions: book balance of assets corresponding to the financial statements, excluding the derivative headings.
- Adjustments for reconciliation between the accounting perimeter and the solvency perimeter: the balance resulting from the difference between the accounting balance sheet and the regulatory balance sheet is included.
- Exposure in derivatives: the exposure referring to the EAD used in the measurement of capital use for counterparty risk, which includes both the replacement cost (market-to-market) and the future potential credit exposure (add-on). The cost of replacement is reported adjusted by the margin of variation in cash and by effective notional amounts.
- Securities financing transactions (SFTs): in addition to the exposure value, an addition for counterparty risk determined as set out in article 429 of the CRR in included.
- Off-balance-sheet items: these correspond to risks and contingent liabilities and commitments associated with collateral, which are mainly available. A minimum floor of 10% is applied to the conversion factors (CCF), in line with article 429.10 a) of the CRR.
- The exposures of the Group's financial institutions and insurance companies that are consolidated at accounting but not at regulatory level.
- Tier 1 deductions: all those amounts of assets that have been deducted in the determination of the eligible Tier 1 capital are deducted, in order not to duplicate exposures. The main deductions are intangible assets, loss carry forwards and other deductions defined in article 36 of the CRR and indicated in section 2.1 of this report.

The table below shows a breakdown of the items making up the leverage ratio as of December 31, 2018 and December 31, 2017:

Table 87. LRSum - Summary reconciliation of accounting assets and and exposure corresponding to the Leverage Ratio (Million Euros)

Summary table of accounting assets and leverage ratio exposure conciliation	12-31-18 Phased-in	12-31-18 Fully Loaded	31-12-17 Phased-In	12-31-17 Fully Loaded
(a) Total assets as published financial statements	676,689	676,689	690,059	690,059
(b) Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	(19,326)	(19,326)	(17,079)	(17,079)
(Adjustment for fiduciary assets recognised on the balance sheet pursuant to the operative accounting framework but excluded from the leverage ratio exposure measure in accordance with Article 429 (13) of Regulation (EU) No 575/2013)	-	-	-	-
(c) Adjustments for derivative financial instruments	(7,410)	(7,410)	(14,772)	(14,772)
(d) Adjustments for securities financing transactions "SFTs"	2,949	2,949	(1,248)	(1,248)
(e) Adjustment for off-balance sheet items (1)	61,409	61,409	62,441	62,441
(f) (Adjustment for intragroup exposures excluded from the leverage ratio exposure measure in accordance with Article 429 (14) of Regulation (EU) No 575/2013)	-	-	-	-
(g) Other adjustments	(9,012)	(10,080)	(9,643)	(9,920)
Leverage ratio total exposure measure	**705,299**	**704,231**	**709,758**	**709,480**
h) Capital Tier 1	45,947	45,047	46,980	46,316
Leverage ratio total exposure measure	**705,299**	**704,231**	**709,758**	**709,480**
Leverage ratio	**6.5%**	**6.4%**	**6.6%**	**6.5%**

(1) This corresponds to off-balance sheet exposure after application of the conversion factors obtained in accordance with Article 429, paragraph 7 of the CRR

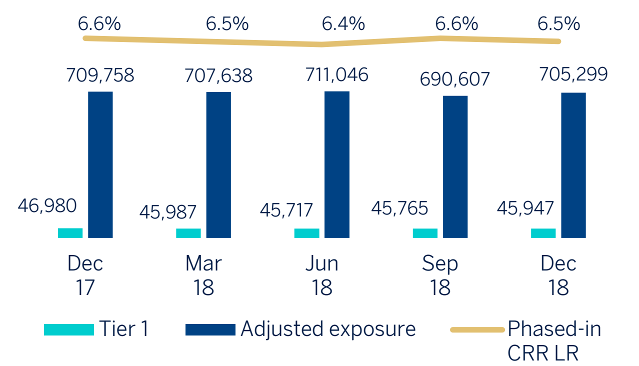
As can be seen, the Group maintains a phased leverage ratio of 6.5% and a fully-loaded ratio of 6.4%, well above the minimum level required.

4.2. Trends in the ratio

The phased-in leverage ratio decreased by 11 basis points during the year. As indicated in section 2.2., Tier 1 was reduced by approximately EUR 1 billion, resulting in an impact on leverage of -16 basis points. On the other hand, exposures were reduced by approximately 5.5 billion (+5 basis points), mainly derived from the sale of the Group's interest in BBVA Chile.

As of December 2018, the phased-in ratio was 6.6% (6.5% in fully-loaded terms), easily above the minimum required of 3%. The leverage level reflects the nature of the business model that is geared toward the retail sector.

Chart 29: Leverage ratio evolution



4.3. Governance

The activities making up the Group's regulatory reporting include monthly measurement and control of the leverage ratio by assessing and monitoring this measurement in its more restrictive version (fully-loaded), to guarantee that leverage remains far from the minimum levels (which could be considered risk levels), without undermining the return on investment.

The estimates and the development of the leverage ratio are reported on a regular basis to different governing bodies and committees to guarantee an adequate control of the entity's leverage levels and ongoing monitoring of the main capital indicators.

In line with the risk appetite framework and structural risk management, the Group operates by establishing limits and operational measures to achieve a sustainable development and growth of the balance sheet, maintaining at all times tolerable risk levels. This can be seen in the fact that the regulatory leverage level itself is well above the minimum required levels.