5. Leverage ratio

5.1. 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.

CRR II introduces a mandatory minimum leverage ratio requirement, set at 3% of Tier 1 capital over the total exposure measure.

However, institutions that decide to exclude central bank exposures from the total exposure measure must recalibrate upwards this 3% minimum requirement such that only recently accumulated central bank exposures (only the increase in central bank exposures since the end of 2019) effectively benefit from leverage ratio relief. This exclusion has applied until March 31, 2022.

Described below are the elements making up the leverage ratio, in accordance with CRR II:

- Tier 1 capital (letter i in the following table): Section 3.2. of this Document presents details of the eligible own funds, calculated based on the criteria defined in the CRR.
- Total Exposure: As set out in Article 429 of the CRR, the total exposure measure generally follows the book value subject to the following considerations:
  - On-balance sheet exposure other than derivatives is included net of allowances and accounting valuation adjustments.
  - The measure 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 leverage ratio is composed by the sum of the exposure values of:

- Assets: the exposure value of an asset item will be its accounting value remaining after the application of specific credit risk adjustments. In general terms, securities financing transactions will not be compensated except for certain conditions.
- Derivatives contracts: the Entity calculates the exposure value of derivatives contracts in accordance with the standard method of counterparty risk (SA-CCR). When calculating the exposure value, the effects of compensation agreements (netting) will be taken into account. For the purposes of calculating the exposure value, collateral received will not be included, except under certain conditions.
- Add-ons for counterparty credit risk of securities financing transactions (SFTs): in addition to the calculation of the exposure value of securities financing transactions, included in the first point, the total exposure measure shall include an add-on due to counterparty credit risk in accordance with article 429e of the CRR II
- Off-balance sheet items: these correspond to risk and contingent liabilities and commitments, mainly collateral and undrawn balances. A minimum floor is applied to conversion factors (CCFs) of 10% in line with the provisions of the Article 429f (3) of CRR II.
- Regular-way purchases or sales awaiting settlement.

The exposures excluded from the total exposure measure are:

- 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 exposure. The main deductions are intangible assets, loss carry forwards and other deductions defined in Article 36 of CRR II and indicated in section 3.2 of this report.
- Additionally, as of December 31, 2021, the temporary exemption of certain exposures to central banks was included. This exemption ceased to be into force in March 2022.

The table below shows a breakdown of the items making up the leverage ratio as of December 31, 2022, June 30, 2022 and as of December 31, 2021.

Table 87. EU LR1 - Summary reconciliation of accounting assets and exposure corresponding to the Leverage Ratio (Million Euros)

	12-31-2022		6-30-2022		12-31-2021	
	Phased-In	Fully Loaded	Phased-In	Fully Loaded	Phased-In	Fully Loaded
(a) Total assets as published financial statements	713,140	713,140	715,294	715,294	662,885	662,885
(b) Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	(24,189)	(24,189)	(22,734)	(22,734)	(21,373)	(21,373)
(Adjustment for securitised exposures that meet the operational requirements for the recognition of risk transference)	(1,995)	(1,995)	(1,460)	(1,460)	(1,899)	(1,899)
(Adjustment for temporary exemption of exposures to central bank (if applicable))	—	—	—	—	(33,747)	(33,747)
(Adjustment for fiduciary assets recognised on the balance sheet pursuant to the applicable accounting framework but excluded from the leverage ratio total exposure measure in accordance with Article 429a(1)(i) of Regulation (EU) No 575/2013)	—	—	—	—	—	—
Adjustment for regular-way purchases and sales of financial assets subject to trade date accounting	—	—	—	—	—	—
Adjustment for eligible cash pooling transactions	—	—	—	—	—	—
(c) Adjustments for derivative financial instruments	(18,618)	(18,618)	(13,432)	(13,432)	(6,311)	(6,311)
(d) Adjustments for securities financing transactions "SFTs"	6,659	6,659	7,492	7,492	12,686	12,686
(e) Adjustment for off-balance sheet items(1)	67,971	67,971	72,244	72,244	64,107	64,107
(Adjustment for prudent valuation adjustments and general credit risk adjustments which have reduced Tier 1 capital)	—	—	—	—	—	—
(f) (Adjustment for intragroup exposures excluded from the leverage ratio exposure measure in accordance with Article 429 (7) of Regulation (EU) No 575/2013)	—	—	—	—	—	—
(g) (Adjustment for exposures excluded from the total exposure measure corresponding to the leverage ratio under Article 429(14) of Regulation (EU) No 575/2013)	—	—	—	—	—	—
(h) Other adjustments	(4,979)	(5,232)	(5,387)	(5,770)	(4,558)	(5,323)
Leverage ratio total exposure measure	**737,990**	**737,736**	**752,016**	**751,634**	**671,790**	**671,025**
i) Capital Tier 1	**47,931**	**47,677**	**46,828**	**46,445**	**45,687**	**44,922**
Leverage ratio	**6.49 %**	**6.46 %**	**6.23 %**	**6.18 %**	**6.80 %**	**6.69 %**

(1) Corresponds to the off-balance sheet exposure after applying the conversion factors obtained in accordance with Article 429(10) of the CRR.

The full series of the reconciliation of the leverage ratio exposure, during the year 2022, is available in the editable file "Pillar 3 2022 - Tables & Annexes".

The table below includes the breakdown of on balance sheet exposures, excluding derivatives and securities financing transactions.

Table 88. EU LR3 - Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures) (Millon euros)

	12-31-2022		6-30-2022		12-31-2021	
	Phased-In	Fully Loaded	Phased-In	Fully Loaded	Phased-In	Fully Loaded
Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:	595,477	599,631	599,631	599,631	516,179	516,179
Trading book exposures	28,199	35,968	35,968	35,968	41,234	41,234
Banking book exposures, of which:	567,278	563,663	563,663	563,663	474,945	474,945
Covered bonds	35	35	35	35	405	405
Exposures treated as sovereigns	163,963	172,882	172,882	172,882	117,682	117,682
Exposures to regional governments, MDB, international organisations and PSE not treated as sovereigns	10,190	8,829	8,829	8,829	8,396	8,396
Institutions	18,630	20,545	20,545	20,545	16,856	16,856
Secured by mortgages of immovable properties	114,849	103,257	103,257	103,257	100,550	100,550
Retail exposures	83,332	79,095	79,095	79,095	71,193	71,193
Corporates	138,715	129,508	129,508	129,508	118,158	118,158
Exposures in default	4,057	4,796	4,796	4,796	4,937	4,937
Other exposures (eg equity, securitisations, and other non-credit obligation assets)	33,508	44,716	44,716	44,716	36,769	36,769

5.2. Evolution of the ratio

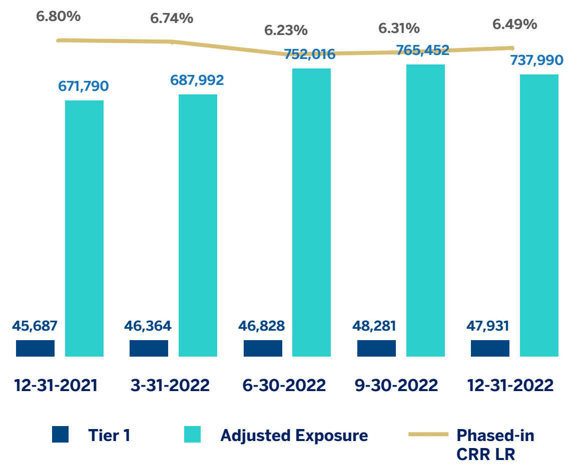
As of December 31, 2022, the leverage ratio stands at 6.49% (6.46% in fully loaded terms), increasing by 19 basis points compared to September 2022. This increase is mainly due to the decrease in the exposure measurement, impulsed by the evolution of currencies in the last quarter of 2022, which contributed to a negative impact of 23 basis points on the leverage ratio.TheTier1 decrease represents a negative impact of 5 basis points on the leverage ratio.

Additionally, during the year, it is worth highlighting the completion on March 31, of the transitional period for the exclusion of certain exposures to central banks from the total exposure measure, in accordance with Regulation (EU) 2019/876. This effect have contributed to the leverage ratio decreasing by 31 basis points compared to December 31, 2021 (6.80% phased-in).

The complete series of exposures to the leverage ratio, during the year 2022, is available in the editable file "Pillar 3 2022 - Tables & Annexes".

On the following chart, it is showed the leverage ratio evolution along the year, as well as its components:

Chart 23. Trends in the leverage ratio



5.3. Governance

The activities making up the Group's regulatory reporting include monthly measurement and control of the leverage ratio by assessing and monitoring this measure, to guarantee comply with the regulatory minimum levels and intern objectives. Additionally, the Group have identified measures to ensure the restoration of its levels given unexpected events which could affect the compliance of this objectives.

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 tolerable risk levels at all times. This can be seen in the fact that the regulatory leverage level itself is well above the minimum required levels.