Spanish Banks

Santander and BBVA: implications from lower rates

Industry Overview

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Equity
Spain
Banks

Antonio Reale >>
Research Analyst
MLI (UK)
+44 20 7996 1763
antonio.reale@bofa.com

Filippo Munari >>
Research Analyst
MLI (UK)
+44 20 7995 2198
filippo.munari@bofa.com

Time to reset NII outlook, but short-term still positive

Investors' confidence in banks' net interest income (NII) is being tested (once) again, with the perils of calling 'peak' too early or too late evident. While NII growth will likely continue in the next few quarters and even in FY2024e, we believe peak is likely due by 2Q 2024; this implies a drop in NII 2025e, which seems to be largely captured by the 40-year low P/E multiples. On our sensitivity analysis NIM shocks, per-basis-point, deriving from lower rates, would be asymmetric. Instead, it is higher deposit betas, MRR changes or deposit outflows which have more scope to hurt margins. Overall, we lower our NII estimates by c.5-15% in 2025e.

Non-interest income growth will warrant higher multiple

As rates peak and are set to fall, non-interest income (asset mgmt., insurance etc.) becomes increasingly more valuable, and will carry a higher multiple, in our view. We also expect banks' trading income to normalize, up from the lows. While banks will continue to focus on using some of the excess capital to internalize/strengthen their product offerings where needed.

'Special' distribution to be the new norm

With organic capital generation running at c.250-300bps annually, banks have been growing CET1 buffers. A few banks could now afford to distribute 100% of their organic generation without affecting their CET1 level. We expect 'special' distribution to become the norm for some banks.

In-sector M&A remains a way to redeploy excess capital

The value of a bank franchise lies in its core deposits and the search for sticky, low-remunerated funding remains a driving force for M&A. Against falling rates, in-sector M&A is one option to protect earnings via market shares gains, cost synergies and more product offerings. While unrealized losses could deter short-term activity, Italy and Iberia have further scope to concentrate banking markets. Excess capital and valuation mean cash in-sector deals are more likely than stock funded transactions, we believe.

Santander a top pick

Santander is our top pick in Spain; it trades at the lowest P/PPOP multiple in Europe, and its Brazilian unit (>25% of earnings) has now turned. Lower rates should benefit margins and LLPs in its US and Brazilian units.

Exhibit 1: BofA ratings and POs
BUY SAN, Neutral on BBVA

Buy	Neutral	Underperform
Santander	BBVA	
	PO new	**PO old**
Santander	4.8	4.8
Santander ADR	5.26	5.09
BBVA	8.9	8.9
BBVA ADR	9.70	9.40

Source: BofA Global Research
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NIM = Net Interest Margin
NII = Net Interest Income
MRR = Minimum Reserve Requirement
CET1 = Common Equity Tier 1
M&A = Merger & Acquisitions
LLP = Loan Loss Provisions
LPI = Late Payment Interest
POPP = Pre-Provision Operating Profit

Timestamp: 16 January 2024 12:30AM EST

Investment thesis

Exhibit 2: Investment thesis – Santander and BBVA

Buy SAN. Neutral on BBVA

Bank	Rating	Price Objective	Investment Thesis
Santander	Buy	EUR 4.80	Santander is a 'show-me story' its shares have underperformed the synthetic valuation of its subsidiaries. It trades at the lowest P/PPOP multiple in Europe and we believe its Brazilian unit, which accounts for >25% of earnings, has inflected with SELIC cuts running at 50bps per BCB meeting. While its capital buffers will now be supported by the organic generation and although the US auto lending market remains challenged short-term, loan losses will be more resilient than cons. especially as rates fall. With Santander trading on 4.5-5x P/E '24e, we have a Buy rating.
BBVA	Neutral	EUR 8.85	Mexico represents a significant c.60% of BBVA's group profits. This has been a key source of growth for BBVA, which is set to normalize as we approach peak rates with early signs of an economic 'normalization' in Mexico and with elections this year. While Türkiye has been performing better than feared, it will continue to affect valuation both positively and negatively being a source of volatility. While inexpensive at c.6x P/E 2024e, we see limited upside near-term – Neutral rating.

Source: BofA Global Research

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NII: what is the new 'normal'?

This past year markets have played rate-sensitive names by looking predominantly at the effects on the asset side from higher rates. Italian banks, together with their German, Irish and Iberian counterparts, have been among the main beneficiaries in Europe. As rate hikes come to an end and start to normalize, non-interest income (asset mgmt., insurance and other revenues) become more valuable and will carry a higher multiple in our view. However, our comprehensive NII sensitivity analysis highlights that the market is struggling to appreciate all the moving parts affecting NII and doesn't yet adequately discriminate the value across banks. In our models we run NII sensitivities incorporating:

1. the Euribor 3-month at an average 3.2% and Euribor 12-months at 3.0%, broadly inline with the future curve. We assume first cut in June by 25bps; however, we note it's average Euribor that drives full year NII estimates;

2. ECB's Minimum Reserves Requirements (MRR) unchanged at 1% along with zero remuneration; we however, show sensitivities if MRR were to move up to 2-3% (not our base case);

3. the differing interest rate hedging strategies adopted by banks in our coverage: banks use replicating portfolios to manage interest rate risk and lock interest rates, we update for the latest euro swap curve;

4. the yield on sovereign bonds will increase carry trade as maturities are reinvested at a higher 'sustainable' carry versus the back-book on duration ranging between 4-6 years;

5. a varying portion of current accounts (c. 20-30%) will move into time deposits and retail bonds depending on the bank, otherwise exit deposit betas will remain stable from 4Q23 levels. Banks' franchises and business mix (corporate vs. retail clients) will be a key discriminating factor;

Replicating portfolios: Intesa still best positioned

Banks use replicating investment portfolios to manage the interest rate risk of variable savings deposits. These are portfolios of fixed-income assets that aim to replicate the typical interest rate maturity of sight deposits. The strategy is set so that the margin between the portfolio return, and the savings interest rate is as stable as possible. This allows banks to base their interest rate risk on investments with a fixed maturity and price, despite sight deposits don't have a contractual maturity, by turning the investments into contractual obligations. Banks tend to pay variable and receive fixed. While the euroswap curve is not immune to rate cuts, the back-book yield is, in some cases negative and well below the front-book, suggesting a positive accrual from the maturity reinvestments. Intesa is best positioned and will be one of the few banks able to offset the negative from lower rates – see Exhibit 3

Exhibit 3: Italian banks replicating portfolios

Many Italian banks use replicating portfolios (mainly swaps) to manage interest rate risk

Bank	Size	Maturities	Avg. maturity	Back-book yield	Front-book yield	NII contribution	Comments on strategy
Intesa	c.€160bn	c.€30bn per year	4 years	0.7%	Euroswap 4yr - c.2.6%	c.€0.6-0.7bn (c.4% NII '23e)	Core stable deposits (fixed rate) matched against fixed-rate bond portfolio with average maturity of 4 years
UniCredit	c.€185bn	c.€19bn per year	10 years	c.1%	Euroswap 10yr - c.2.6%	c.€0.3-0.4bn (c.2% NII '23e)	Stable deposits are defined as sticky deposits both from a behavioral and a pricing standpoint. As of 4Q22, the size of the replicating portfolio remains prudently below the amount of non-maturity, stable deposits
Banco BPM	c.€15bn	c.€3bn per year	5 years	c.1%	Euroswap 5yr - c.2.6%	c.€50m (c.1% NII '23e)	Core stable deposits (fixed rate) matched against fixed-rate bond portfolio with average maturity of 5 years
BMPS	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	Sight deposit stickiness modelling is used to feed the overall ALM position (no formal use of replicating portfolios); ALM based on NII/EVE sensitivity optimization (given cross dependency in terms of targets/constraints).
Mediobanca	€13.4bn	€2.4bn per year	5.5 years	-0.13%	Euroswap 6yr - c.3.2%	c.€80m (c.4% NII '23e)	Given the size of deposits at Mediobanca, the hedging is done directly with derivatives
Poste Italiane	c.€85bn	€3bn per year	5 years	2.4%	BTP yield 7yr - c.3.5%	c.€35m (c.1% NII '23e)	ALM based on liability duration matching. Predominantly long-only, limited use of market funding via repos. €85bn are inclusive of public administration for €10.8bn

Source: BofA Global Research

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Exhibit 4: Spanish banks ALCO portfolios and replicating portfolios in the UK

Spanish banks make limited use of interest rate swaps with the ALCO book acting as the main hedging tool. Instead in the UK, SAN & SAB have replicating portfolios

Bank	Size	Maturities	Avg. maturity	Back-book yield	Front-book yield	NII contribution	Comments on strategy
Santander - Spain (ALCO book)	c.€30bn	c.€4.5bn per year	5.2 years	3.3%	Spanish 5yr - c.2.8%	- c.€23m	No replicating portfolio in place. ALCO portfolio to increase slightly in 2024 to get incremental income and lower sensitivity. ALCO composition: 75% of HTC bonds with >7yrs maturity & >3.3% yield and 25% of short-term bonds with maturity c.1yr & <3% yield
Santander - UK (replicating portfolio)	c.£110bn	c.£22bn per year	5 years	1.2%	5-year GBP swap rate - c.3.6%	c.£0.4-0.5bn (c.1% NII '23)	Structural hedge on core stable deposits carried out with a portfolio of 5-year rolling swaps
BBVA - Spain	c.€25bn	c.€5bn per year	5 years	3.1%	Spanish 5yr - c.2.8%	- c.€15m	No replicating portfolio in place. ALCO portfolio mainly used as a hedging tool to reduce balance sheet sensitivity and get duration
CaixaBank (ALCO portfolio)	c.€43bn	c.€9.5bn per year	4.5 years	1.0%	Spanish 5yr - c.2.8%	c.€170m (c.2% NII '23)	ALCO portfolio thought as a hedging tool and not a material income driver. Might increase the size depending on yield curve shape & balance sheet sensitivity needs (sensitivity already partially lowered by issuing fixed-rate loans)
CaixaBank (hedge on deposits)	c.€20bn	€5bn in 1Q24, rest end-26 / start-27	c.3 years (ex. 1Q24 maturities)	n.a.	n.a.	c.€40m incremental q/q in 2Q24	Portfolio of fixed-to-variable swaps used to turn a portion of deposits into variable. €5bn maturing by end of 1Q and driving c.€40m of incremental income in 2Q from lower deposit costs
Sabadell - Spain (ALCO portfolio)	c.€16bn	c.€2.5bn per year	6.5 years	3.1%	Spanish 5yr/10yr - c.2.8%-3.2%	- c.€2.5m	ALCO thought as a hedging tool, c.40% of the portfolio swapped to variable
Sabadell - UK (replicating portfolio)	c.€26bn	c.£5.2bn per year	5 years	1.2%	5-year GBP swap rate - c.3.6%	c.£100-150m (c.3% NII '23)	Structural hedge on core stable deposits carried out with a portfolio of 5-year rolling swaps
Bankinter	c.€11bn	c.€1.3bn per year	8.5 years	2.2%	Spanish 5yr/10yr - c.2.8%-3.2%	c.€10.5m (c.0.5% NII '23)	Not seen as a significant income driver but tool to manage interest rate risk. c.85% of the portfolio is reported amortized cost. No specific plan to increase the size to lock in duration for the future

Source: BofA Global Research

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Replicating portfolio explained: Illustrative case – Intesa Sanpaolo

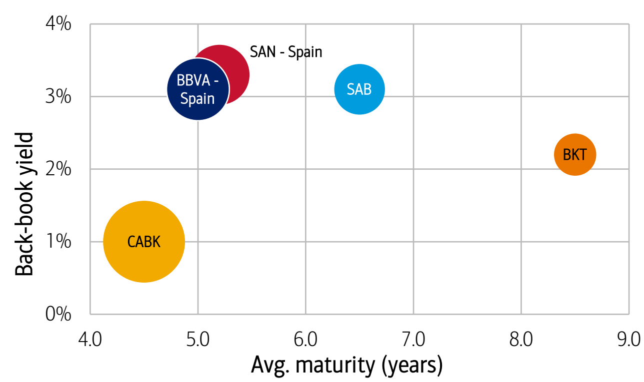
Intesa has c.€400bn in deposits, of which the bulk are current accounts and an additional €16bn are certificates of deposits which illustratively pay c.2.5% yield. Intesa's management determines based on its own quantitative models and time series of deposit flows patterns, that through-the-cycle c.40% of these current accounts should be hedged. In numbers, it's c.40% x c.€400bn = c.€160bn which is the size of Intesa's replicating portfolio. Intesa then enters into interest rate swap contracts/underwrites bonds and loans worth c.€160bn or a combination of all of the above. When entering a swap contract, Intesa pays a variable rate linked to Euribor and receives a fixed rate depending on the swap maturity which normally matches the expected maturity of its deposit base. In Intesa's case it's the Euroswap and 4 years maturity. Every year, c.€30bn of the portfolio matures and the bank rolls over into another swap with an average back-book yield of 0.7% - in reality the back-book of what is maturing now is even negative in some cases. This is reinvested at the Euroswap 4 years, currently at 2.5%. So the interest accrual from the reinvestment is €0.7bn for Intesa and it is not captured by consensus NII estimates yet.

Domestic Spanish banks most vulnerable to rate cuts

In Spain, banks operate for the most part on a variable rate market with about two-third of loans tied to Euribor. Hence, Spanish banks have predominantly retained a variable book, with mortgages running on a 20-25 year duration, usually with a fixed spread over Euribor 12m which reprices once a year (or Euribor 6m repricing twice a year. That means that Spanish banks are almost naturally matched against interest rate risks as the bulk of both assets and liabilities are on variable rates. This means domestic Spanish banks have fewer mitigants and are most vulnerable to rate cuts. They only make limited use of interest rate swaps, with replicating portfolios that are small in size and the ALCO (Assets and Liabilities Committee) book that ends up acting as the main hedging tool. Most of these ALCO portfolios are made up of domestic sovereign bonds with an average of 5-7 years maturity and a yield of c.2-3% which is already relatively high. We also note that the benefit from the repricing of sovereign bonds will not be linear and is overall limited. We note nonetheless that Caixabank has the lowest average yield at 1%. While Santander Spain, BBVA Spain and Sabadell have the highest yielding bond portfolio at >3%, limiting the repricing potential.

Exhibit 5: ALCO portfolios by maturity and yield

Limited ALCO repricing tailwinds ahead, with avg. yields at 2-3% (ex. CABK)



Source: BofA Global Research, Company reports. Notes: Bubble size = portfolio amount

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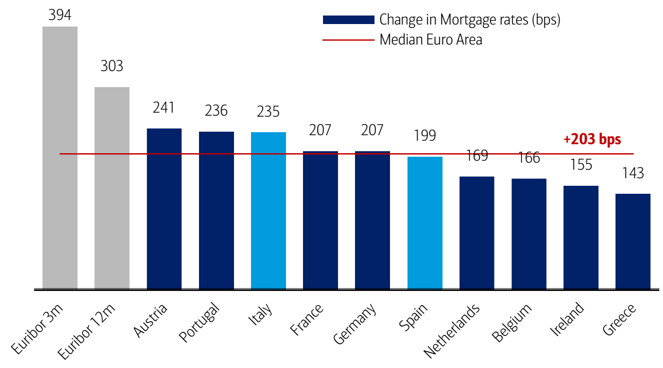
Therefore, rate cuts will come through to lending margins, on the mortgage book, these will be mainly mechanical, albeit with a lag of 3-6 months. While the lower liquidity in the system will have an impact on credit spreads, which should help somewhat defend margins on the corporate book and on consumer loans.

Exhibit 6: Change in front-book mortgage rates since Jul-22

Change in Italian mortgage rates ahead of EU peers; Spain broadly in line



Source: BofA Global Research, Haver Analytics. Notes: change in rates from Jul-22 to Nov-23

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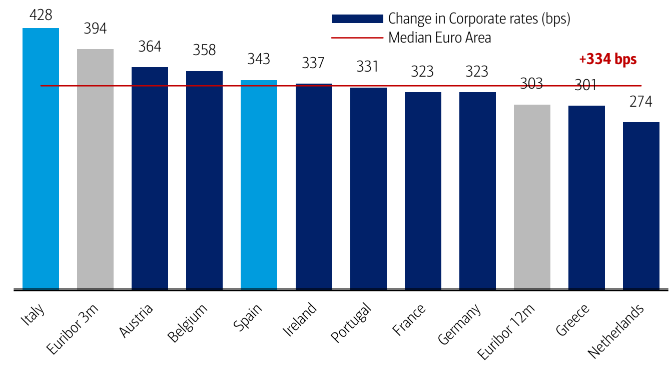
Exhibit 7: Change in front-book corporate rates since Jul-22

Change in Italian corporate rates ahead of EU peers; Spain also slightly ahead



Source: BofA Global Research, Haver Analytics. Notes: change in rates from Jul-22 to Nov-23

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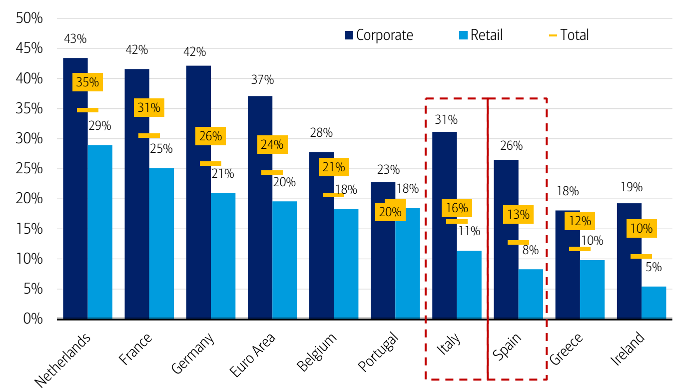
Year-end deposit betas to drive NII in 2024-25e

Deposit remuneration has been surprisingly resilient. While some commercial campaigns exist, they are mainly aimed at affluent/premier clients or are in the context of cross-selling ancillary products e.g. structured insurance or certificates. We believe deposit betas will continue to affect NII levels in 2024-25, especially for those banks needing to manage maturities and liquidity ratios. Over time, we expect a change in the overall deposit mix as some current accounts will gradually move to term deposits. In our NII sensitivity modelling, we factor in 20-30% of current accounts moving gradually to term deposits (in a 3–5-year horizon), which is the normalized level experienced before negative rates. Spanish banks have managed to retain one of the lowest deposit betas in Europe at around 12% vs. the euro area at 23% and Italian banks at 15% (as of November). Overall, we forecast deposit betas to be at around c.25-30% in 2024-25. Caixabank and Intesa stand out as the respective national champions, having the highest stack of low-remunerated current accounts in Spain and Italy, with their retail portion amounting to c.70% of the total (more in the case of Caixabank).

Exhibit 8: Deposit betas by country and deposit type

Italy and Spain still showing contained deposit betas as of Nov-23



Source: BofA Global Research, Haver Analytics. Notes: Deposit betas calculated as the change in average deposit cost divided by the change in ECB deposit facility rate over Jul-22 to Nov-23

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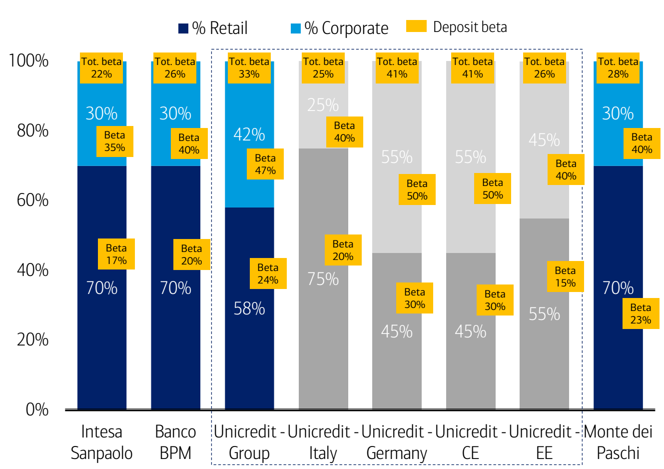
Exhibit 9: Deposit betas assumed 2024 for Italian banks (BofA est)

We expect deposit betas in Italy to stay at/below c.30% in 2024



Source: BofA Global Research

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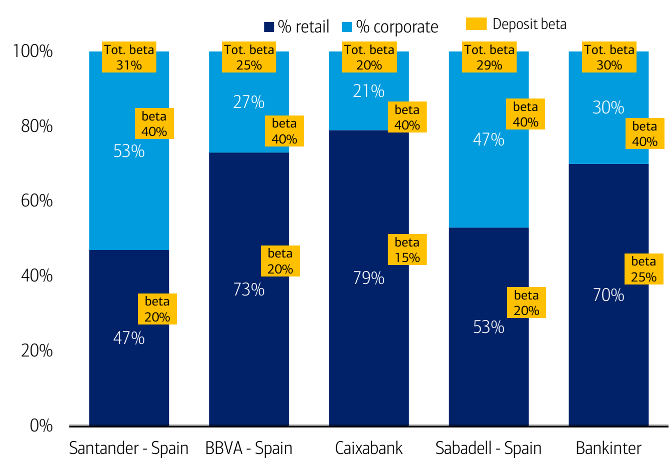
Exhibit 10: Deposit betas assumed 2024 for Spanish banks (BofA est)

We expect deposit betas in Spain to stay at/below c.30% in 2024



Source: BofA Global Research

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Minimum reserves requirements: running sensitivities

We work on the assumption that pragmatism will prevail, and the ECB will stay away from lifting mandatory reserves. However, this will be part of the ECB's operational framework review due later this year in 2024 (Spring was the last we heard from Lagarde but we understand it's a moving target). Once the ECB agrees on the framework for the future (which includes some idea on the endpoint for the balance sheet and how policy will be steered) it can adjust the minimum reserve ratio to whatever fits that framework. We work on the assumption that minimum reserve requirements are unlikely to change from 1% currently along with zero remuneration. We nonetheless show below sensitivities to NII if MRR were to change to 2% and 3%.

Exhibit 11: 2025 NII sensitivity to Minimum Reserve Requirement (MRR) and Terminal Rate (TR) year-end 2024e

Most rate sensitive banks range from -4-5% to +4-6% impact on 2025 NII (vs. BofA estimates) across MRR & TR scenarios

	BofA estimates (based on MRR 1% & TR '24e 2.3%)		Implied impact on BofAest NII from:							Sensitivity scenarios				
			MRR % @			Terminal rate 2024 @				Implied NII 2025 vs BofA estimate				
	NII 2025e	Adj net profit 2025e	1%	2%	3%	2.0%	2.3%	2.5%	3.0%	Scenario: MRR 3%, TR 2%	Scenario: MRR 2%, TR 2%	Scenario: MRR 2%, TR 2.5%	Scenario: MRR 1%, TR 2.5%	Scenario: MRR 1%, TR 3%
Intesa Sanpaolo	13,816	7,765	--	-150	-300	-259	--	173	605	-4.0%	-3.0%	0.2%	1.3%	4.4%
UniCredit	12,557	7,680	--	-170	-340	-180	--	120	420	-4.1%	-2.8%	-0.4%	1.0%	3.3%
Banco BPM	2,940	1,087	--	-43	-86	-90	--	60	210	-6.0%	-4.5%	0.6%	2.0%	7.1%
Mediobanca	2,013	1,234	--	-12	-24	-17	--	11	39	-2.0%	-1.4%	0.0%	0.5%	1.9%
Monte dei Paschi	2,053	749	--	-26	-52	-42	--	28	98	-4.6%	-3.3%	0.1%	1.4%	4.8%
Santander	45,110	11,984	--	-160	-320	-300	--	200	700	-1.4%	-1.0%	0.1%	0.4%	1.6%
BBVA	23,269	8,080	--	-92	-184	-102	--	68	238	-1.2%	-0.8%	-0.1%	0.3%	1.0%
CaixaBank	9,092	3,941	--	-145	-290	-153	--	102	358	-4.9%	-3.3%	-0.5%	1.1%	3.9%
Sabadell	4,384	921	--	-45	-90	-92	--	61	214	-4.1%	-3.1%	0.4%	1.4%	4.9%
Bankinter	2,077	746	--	-30	-60	-30	--	20	70	-4.3%	-2.9%	-0.5%	1.0%	3.4%

Source: BofA Global Research estimates; MRR = Minimum reserve requirement; TR = Terminal interest rates

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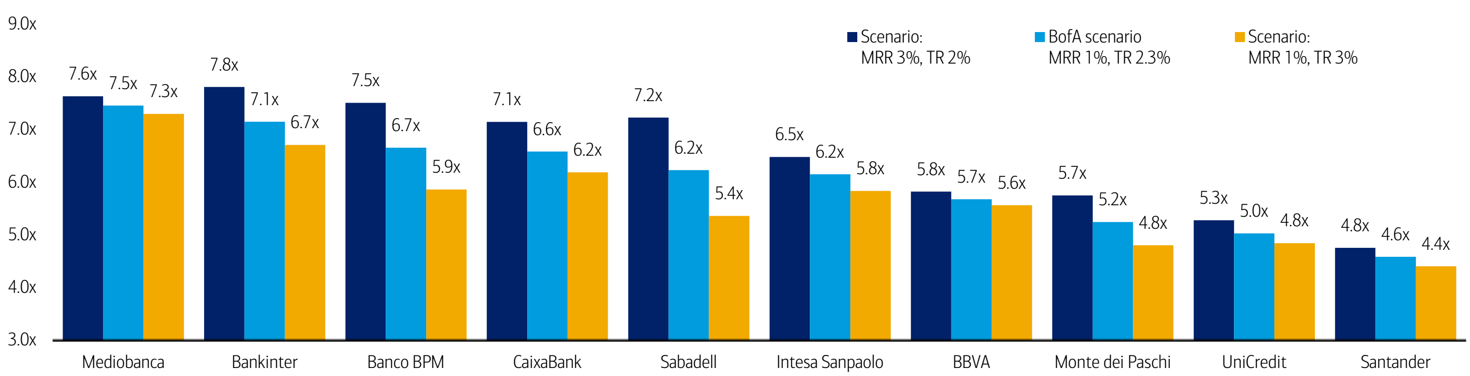
Exhibit 12: Implied P/E 2025e multiples across different MRR and terminal rate scenarios

Average multiples remain subdued even in the most bearish scenarios for MRR and terminal rate



Source: BofA Global Research estimates; MRR = Minimum reserve requirement; TR = Terminal interest rates; Price as of 12/01/2024

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Exhibit 13: Net interest income estimates – BofA vs. Consensus

We are 1-4% below consensus NII 2025 at SAN and BBVA

	BofA estimates		VA Consensus		BofA vs Cons	
	2024e	2025e	2024e	2025e	2024e	2025e
Santander	44,031	45,110	44,788	45,428	-2%	-1%
BBVA	23,960	23,269	24,618	24,345	-3%	-4%

Source: BofA Global Research, Visible Alpha consensus

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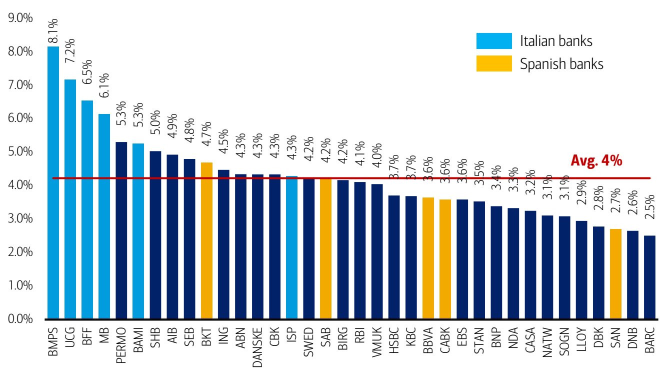
Capital: the prime currency

With earnings increasing structurally, loan growth muted and the regulatory framework set, the organic capital generation can be distributed in full, without affecting current CET1 levels. This is not just for UniCredit and Intesa, but even historical capital laggards like Santander or BMPS have capital ratios that are now in excess of 12% and growing. We believe this will result in higher capital distribution, which could include 'special' elements at year-end. While we believe Italian banks are better positioned here, we expect more buybacks and higher payouts also for some of the Spanish banks. At Caixabank we expect an additional €1bn buyback to be announced in 4Q, but this is broadly in-line with consensus. Similarly, for BBVA, expectations are for an additional €600m buyback (€660m BofA est). We mostly deviate from consensus estimates at Intesa, UniCredit, BMPS and Caixabank when it comes to capital distribution.

Exhibit 14: Excess capital buffers vs CET1 SREP requirement

Italian banks screen as the most capitalized banks in Europe



Source: BofA Global Research, Company reports

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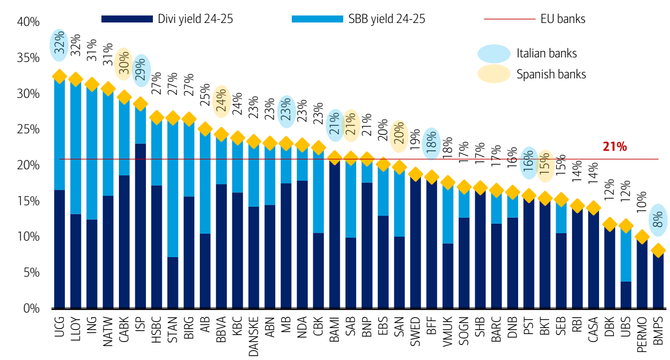
Exhibit 15: Total yield (dividend + buyback) 2024-25

Most of Italian and Spanish banks yielding >20% over 2024-25e



Source: BofA Global Research. Notes: Prices as of 12/01/2024

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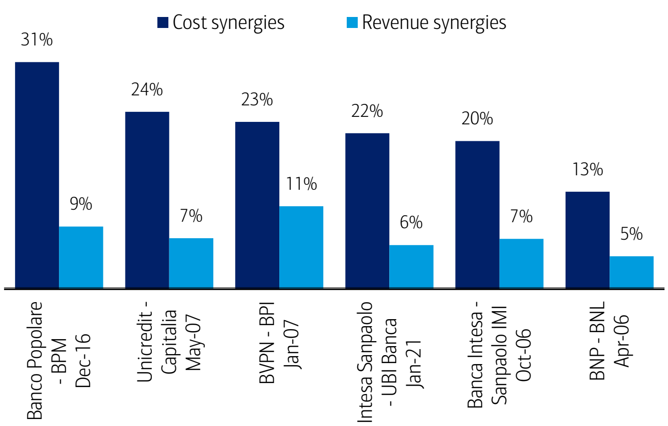
In-sector M&A still a way to redeploy excess capital

Both Italy and Spain's banking sectors have undergone a series of consolidation waves, experienced a sharp reduction in the number of branches and banks. This process enabled banks to improve profitability and capital levels, as well as achieve greater scale and efficiencies. Cost savings achieved both in Spain and Italy have been significant, see Exhibit 16 and Exhibit 17. We believe this process also supported pricing discipline and deposit beta resilience however it's far from finished, with more scope for in-sector consolidation.

Exhibit 16: Announced cost & revenue synergies precedent M&A Italy
Average 22% & 7% cost & revenue synergies in precedent Italian M&A



Source: BofA Global Research, M&A presentations

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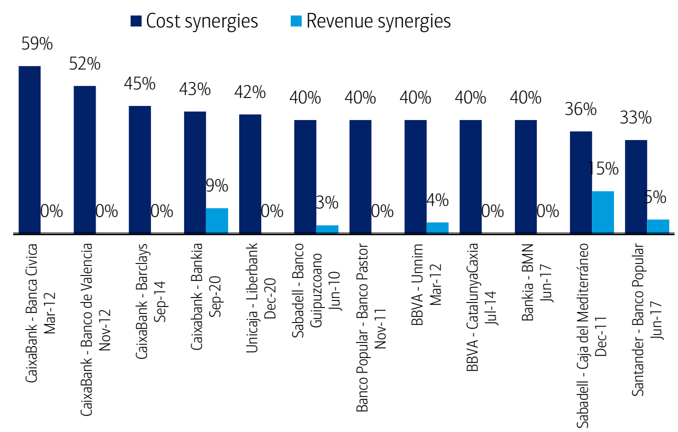
Exhibit 17: Announced cost & revenue synergies precedent M&A Spain
Average 43% cost synergies in precedent Spanish M&A



Source: BofA Global Research, M&A presentations

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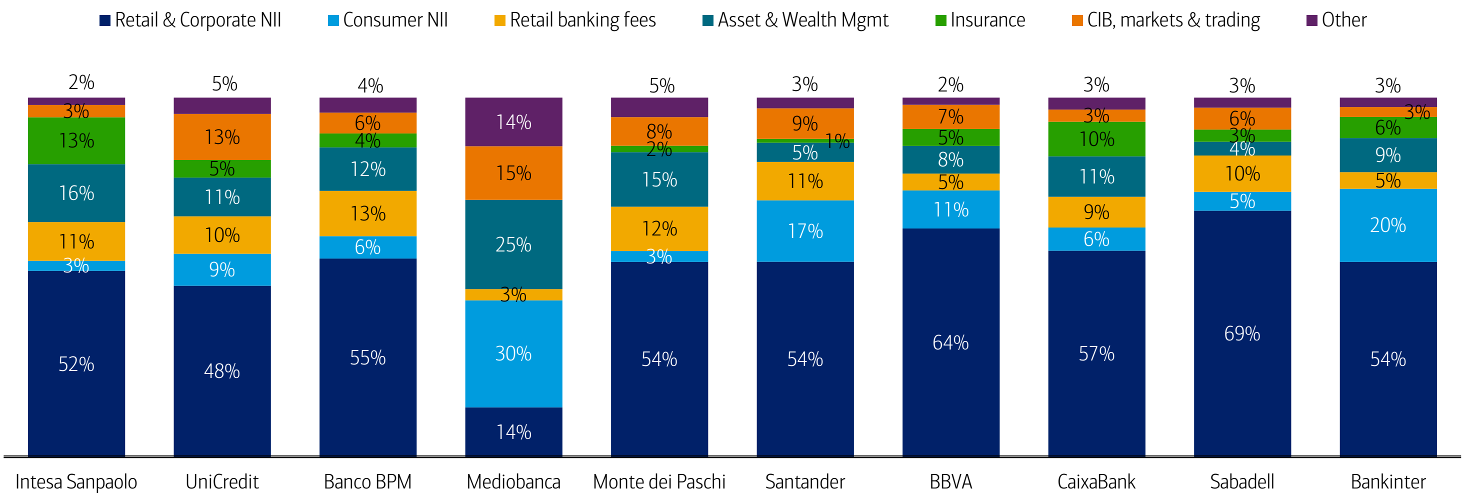
Product factories remain in focus

Over the last decade we have seen banks make significant disposals of product factories, to bolster capital and/or fund cost savings. As rate hikes come to an end, non-interest income revenues (asset mgmt., insurance & payment revenues) become more valuable, and we believe they will carry a higher multiple over time. As a result, we expect banks to focus on internalizing/strengthen some of the products to improve customer retention, optimize capital (Danish Compromise framework is now set) and foster a vertical integration model in their product offering. Below we provide details around the revenue mix across Italian and Spanish banks.

Exhibit 18: Revenue mix across Italian & Spanish banks
Non-NII income streams will likely warrant higher multiples as rates normalize



Source: BofA Global Research

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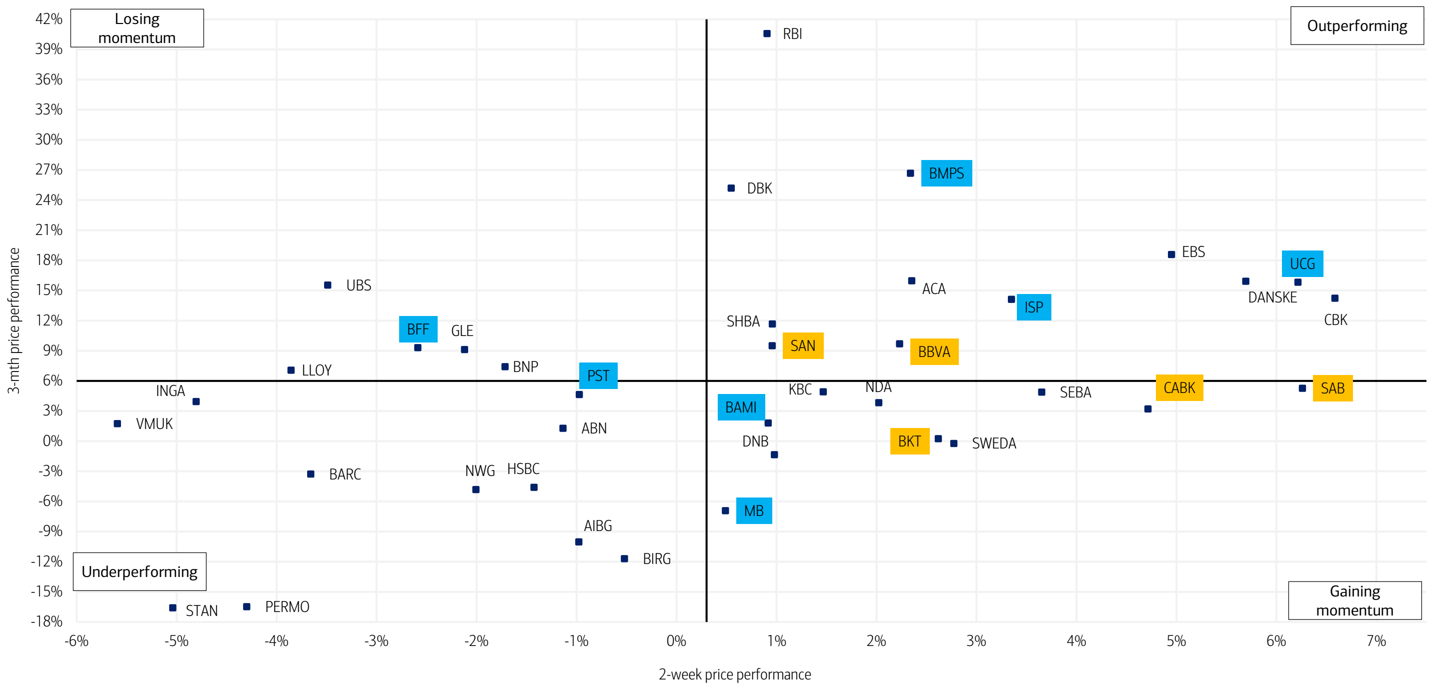
Share price performance

Exhibit 19: 2-week vs. 3-month share price performance across EU Banks with SX7P as intersecting axes

Most Italian and Spanish banks outperforming the index over the last 2 weeks. More mixed performance over the last 3 months



Source: BofA Global Research, Bloomberg

Notes: 1. SX7P performance = axes interception; 2. Prices as of 11/01/2024

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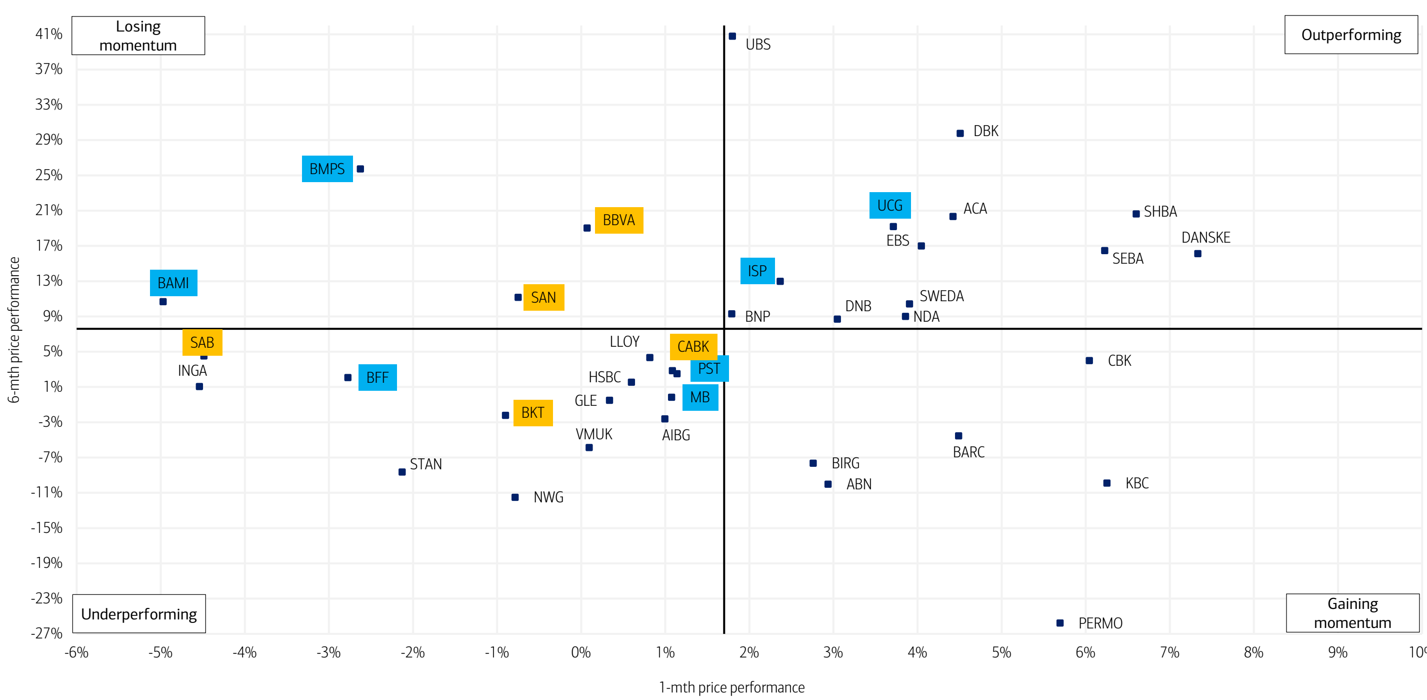
Exhibit 20: 1-month vs. 6-month share price performance across EU Banks with SX7P as intersecting axes

Most Italian & Spanish banks underperforming the index in the last month, ex. UCG and ISP



Source: BofA Global Research, Bloomberg

Notes: 1. SX7P performance = axes interception; 2. Prices as of 11/01/2024

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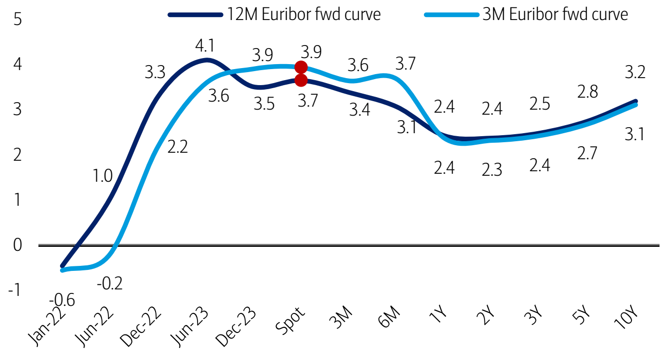
Exhibit 21: Euribor 3m/12m forward curves
Market pricing peak Euribor behind us



Source: BofA Global Research, Bloomberg. Notes: as of 12/01/2024

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Exhibit 22: BofA ratings, price objectives and EPS estimates new vs. old, 2023-25e
EPS estimates move down in 2025e manly on lower forward curve-implied rates

Company	BofA rating		Price Objective		Upside / Downside	Adj. EPS FY23e			Adj. EPS FY24e			Adj. EPS FY25e		
	New	Old	New	Old	%	New	Old	*% change*	New	Old	*% change*	New	Old	*% change*
Santander	Buy	Buy	4.80	4.80	*25%*	0.64	0.65	*-2%*	0.76	0.77	*0%*	0.83	0.84	*-2%*
BBVA	Neutral	Neutral	8.85	8.85	*5%*	1.29	1.25	*3%*	1.42	1.41	*1%*	1.46	1.52	*-4%*

Source: BofA Global Research

BofA GLOBAL RESEARCH

Exhibit 23: BofA EPS estimates vs. consensus, 2023-25e
We are mainly ahead of consensus on UniCredit, Santander, BBVA and CaixaBank

Company	Adj. EPS FY23e			Adj. EPS FY24e			Adj. EPS FY25e		
	BofA est.	Cons	*BofA vs Cons*	BofA est.	Cons	*BofA vs Cons*	BofA est.	Cons	*BofA vs Cons*
Santander	0.64	0.63	*1.8%*	0.76	0.69	*10.9%*	0.83	0.74	*11.9%*
BBVA	1.29	1.29	*0.0%*	1.42	1.33	*7.0%*	1.46	1.32	*10.2%*

Source: BofA Global Research, Visible Alpha. Notes: Mediobanca EPS estimates refer to MB FY24-26e (ending June 2026)

BofA GLOBAL RESEARCH

Rationale behind our ratings

Santander – Buy (unchanged), PO €4.80 (unchanged)

We don't move numbers materially over 2024-25e but adjust 4Q23 for hyperinflation and FX depreciation in Argentina. NII falls 2% as a result in 2023e and feeds through to EPS. We have group NII growing 2% YoY in 2024e and group earnings up 13% YoY supported by progressive margin/volume improvement in Brazil and resilient asset quality in the US. Overall, we are c.10% ahead of consensus net profit in 2024-25e. Reiterate Buy and top pick in Spain – Santander is positively geared to rate cuts in key regions (Brazil, US) and shares trade at an undemanding 4.5x P/E 2025e.

BBVA – Neutral (unchanged), PO €8.85 (unchanged)

We adjust numbers to reflect hyperinflation accounting & strong currency depreciation in Argentina and Turkey, higher staff costs in Spain and Mexico on higher variable pay and deposit cost pressure in Turkey. NII estimates fall by c.3% over 2023-25e, more than offset by lower costs and provisions in 2023-24e, while dropping through to -4%

EPS in 2025e. We have another c.€660m buyback to be announced in 4Q and overall, the shares yield a total of c.25% 2024-25e. Reiterate Neutral.

Santander – summary of financials

Exhibit 24: Santander – Summary of financials
P&L, Balance Sheet, key ratios

Income Statement					
€ in millions, year-end Dec	**FY21**	**FY22**	**FY23e**	**FY24e**	**FY25e**
Net interest income	33,370	38,619	42,970	44,031	45,110
% change	4%	16%	11%	2%	2%
Fees & Commissions	10,502	11,790	12,203	12,720	13,293
% change	5%	12%	4%	4%	4%
Trading revenues	1,563	1,653	2,347	2,068	2,005
% change	-29%	6%	42%	-12%	-3%
Other revenues	969	57	--	--	--
% change	140%	-94%	-100%	n.a.	n.a.
Total Revenues	**46,404**	**52,119**	**57,520**	**58,819**	**60,407**
% change	4%	12%	10%	2%	3%
Staff expenses	(11,043)	(12,547)	(13,244)	(13,587)	(14,022)
% change	3%	14%	6%	3%	3%
Other expense	(10,372)	(11,356)	(11,987)	(12,298)	(12,691)
% change	2%	9%	6%	3%	3%
Total expenses	**(21,415)**	**(23,903)**	**(25,231)**	**(25,885)**	**(26,713)**
% change	2%	12%	6%	3%	3%
Pre-provision profit	**24,989**	**28,216**	**32,290**	**32,934**	**33,695**
% change	6%	13%	14%	2%	2%
Loan loss provisions	(7,436)	(10,474)	(12,386)	(12,463)	(12,863)
Other provisions	(2,293)	(2,492)	(2,949)	(2,141)	(2,145)
Other non-recurrent pre-tax	0	--	7	940	1,076
Profit before taxes	**15,260**	**15,250**	**16,961**	**19,270**	**19,763**
% change	58%	0%	11%	14%	3%
Taxes	(5,076)	(4,486)	(4,940)	(5,737)	(5,884)
% Tax rate	33%	29%	29%	30%	30%
Minorities, g'will + other	(1,530)	(1,159)	(1,122)	(1,289)	(1,401)
Underlying net profit	**8,654**	**9,605**	**10,899**	**12,244**	**12,478**
One-off gains & provisions	(530)	--	--	--	--
Reported net profit	**8,124**	**9,605**	**10,899**	**12,244**	**12,478**
BofA adjusted net profit	**8,170**	**9,122**	**10,405**	**11,750**	**11,984**

Balance Sheet					
€ in millions, year-end Dec	**FY21**	**FY22**	**FY23e**	**FY24e**	**FY25e**
ASSETS					
Net customer loans	972,682	1,036,004	1,035,988	1,058,953	1,086,431
% change	6%	7%	0%	2%	3%
Loan loss reserves	22,964	22,684	23,467	23,222	23,591
Bond portfolio	163,854	193,716	227,954	224,347	222,310
Other earnings assets	282,672	313,736	324,679	311,322	300,259
Avg. earnings assets	1,368,879	1,481,332	1,566,039	1,591,622	1,601,811
% change	4%	8%	6%	2%	1%
Goodwill & intangibles	16,584	18,645	19,635	19,635	19,635
Other assets	160,043	172,558	178,724	178,678	178,638
Total assets	**1,595,835**	**1,734,659**	**1,786,981**	**1,792,935**	**1,807,273**
RWA / assets	36%	35%	35%	36%	37%
LIABILITIES					
Customer funding	1,164,507	1,305,740	1,328,113	1,324,400	1,325,814
% change	7%	12%	2%	0%	0%
o/w Customer deposits	918,344	1,025,402	1,029,001	1,026,614	1,028,951
o/w Securities issued	246,163	280,339	299,112	297,786	296,863
Shareholders' equity	**86,930**	**89,104**	**93,081**	**95,673**	**97,940**
Minorities	10,123	8,481	8,897	9,895	10,981
Total liabilities & equity	**1,595,835**	**1,734,659**	**1,786,981**	**1,792,935**	**1,807,273**

Source: BofA Global Research

Ratio Analysis					
	FY21	**FY22**	**FY23e**	**FY24e**	**FY25e**
Per Share Data					
EPS reported	0.50	0.57	0.67	0.80	0.86
EPS Adjusted (for valuation)	0.47	0.54	0.64	0.76	0.83
% change	72%	14%	19%	19%	8%
DPS	0.10	0.12	0.17	0.20	0.22
% change	n.m.	18%	46%	19%	9%
Dividend yield	2.8%	3.2%	4.4%	5.0%	5.1%
Payout ratio %	20%	20%	25%	25%	25%
Buyback per share	0.10	0.12	0.17	0.20	0.22
Buyback yield	1.4%	3.0%	3.6%	4.7%	5.0%
Buyback as % of earnings	20%	20%	25%	25%	25%
Total yield	4.2%	6.2%	8.1%	9.7%	10.1%
BV per share	5.02	5.28	5.74	6.23	6.76
TBV per share	4.06	4.17	4.53	4.95	5.41
Avg shares outstanding	17,308	16,892	16,203	15,369	14,484
Valuation metrics					
P/E	8.0x	7.0x	5.9x	5.0x	4.6x
P/BV	0.76x	0.72x	0.66x	0.61x	0.56x
P/TBV	0.93x	0.91x	0.84x	0.77x	0.70x
Profitability					
ROE	9.7%	10.4%	11.4%	12.4%	12.4%
ROTE	12.0%	13.0%	14.5%	15.7%	15.5%
ROA	0.5%	0.5%	0.6%	0.7%	0.7%
RoRWA	1.4%	1.5%	1.7%	1.8%	1.8%
NIM (NII / AIEA)	2.44%	2.61%	2.74%	2.77%	2.82%
Total revenues / RWAs	8%	9%	9%	9%	9%
NII / Tot revenues	72%	74%	75%	74%	73%
Fees / Tot revenues	23%	23%	21%	21%	22%
Efficiency					
Cost / income	46%	46%	44%	43%	43%
Cost / assets	1.4%	1.4%	1.4%	1.4%	1.5%
Cost / RWAs	3.8%	4.0%	4.1%	4.1%	4.0%
Balance sheet gearing					
Loan / deposit	106%	101%	101%	103%	106%
Bond securities / assets	10%	11%	13%	13%	12%
Customer loans / assets	61%	60%	58%	59%	60%
Customer deposits / funding	79%	79%	77%	78%	78%
Bonds issued / funding	21%	21%	23%	22%	22%
Asset quality					
Gross NPEs	33,234	34,673	34,673	35,241	35,823
% change	5%	4%	0%	2%	2%
Gross NPE ratio	3.2%	3.1%	3.2%	3.2%	3.2%
Texas ratio %	35%	37%	35%	35%	35%
Coverage ratio - Stage 3	41%	41%	40%	37%	37%
Cost of risk (bps)	79	104	120	119	120
Capital					
Core Tier 1 Capital (Basel III)	70,208	73,350	75,908	79,387	81,825
RWAs (Basel III)	579,478	609,404	624,100	653,247	676,912
% change	3%	5%	2%	5%	4%
RWAs density	60%	59%	60%	62%	62%
Leverage ratio %	5%	5%	5%	5%	5%
Core Tier 1 fully loaded %	12.1%	12.0%	12.2%	12.2%	12.1%
Buffer over SREP %		3.19%	3.25%	2.55%	2.49%

BofA GLOBAL RESEARCH

BBVA – summary of financials

Exhibit 25: BBVA – Summary of financials
P&L, Balance Sheet, key ratios

Income Statement					
€ in millions, year-end Dec	**FY21**	**FY22**	**FY23e**	**FY24e**	**FY25e**
Net interest income	14,686	19,153	23,824	23,960	23,269
% change	-13%	30%	24%	1%	-3%
Fees & Commissions	4,765	5,353	6,264	6,367	6,500
% change	3%	12%	17%	2%	2%
Trading revenues	1,910	1,938	1,824	1,441	1,400
% change	13%	1%	-6%	-21%	-3%
Other revenues	(295)	(1,555)	(2,014)	(1,055)	(407)
% change	118%	n.m.	30%	-48%	-61%
Total Revenues	**21,066**	**24,890**	**29,897**	**30,713**	**30,762**
% change	-8%	18%	20%	3%	0%
Staff expenses	(5,046)	(5,612)	(6,498)	(6,782)	(6,919)
% change	-11%	11%	16%	4%	2%
Other expense	(4,483)	(5,149)	(5,888)	(6,071)	(6,255)
% change	-12%	15%	14%	3%	3%
Total expenses	**(9,530)**	**(10,761)**	**(12,387)**	**(12,853)**	**(13,173)**
% change	-11%	13%	15%	4%	2%
Pre-provision profit	**11,536**	**14,129**	**17,510**	**17,860**	**17,589**
% change	-6%	22%	24%	2%	-2%
Loan loss provisions	(3,034)	(3,378)	(4,510)	(4,882)	(4,843)
Other provisions	(264)	(291)	(342)	(309)	(179)
Other non-recurrent	2	31	(10)	(10)	(10)
Profit before taxes	**8,240**	**10,490**	**12,648**	**12,659**	**12,556**
% change	58%	27%	21%	0%	-1%
Taxes	(2,207)	(3,461)	(4,143)	(3,747)	(3,703)
% Tax rate	27%	33%	33%	30%	29%
Minorities, g'will + other	(965)	(407)	(490)	(464)	(477)
Underlying net profit	**5,069**	**6,622**	**8,015**	**8,448**	**8,376**
Discontinued ops & other	(416)	(201)	--	--	--
Reported net profit	**4,653**	**6,420**	**8,015**	**8,448**	**8,376**
BofA adjusted net profit	**4,710**	**6,309**	**7,720**	**8,152**	**8,080**

Balance Sheet					
€ in millions, year-end Dec	**FY21**	**FY22**	**FY23e**	**FY24e**	**FY25e**
ASSETS					
Net customer loans	318,939	358,023	371,238	374,398	386,027
% change	-13%	12%	4%	1%	3%
Loan loss reserves	11,116	11,237	12,406	13,918	15,287
Bond portfolio	34,781	43,606	44,042	44,482	44,927
Other earnings assets	271,761	270,751	284,374	278,869	278,709
Avg. earnings assets	658,828	648,931	686,017	698,702	703,706
% change	-2%	-2%	6%	2%	1%
Goodwill & intangibles	2,197	2,156	2,310	2,310	2,310
Other assets	35,207	38,604	42,880	42,543	42,444
Total assets	**662,885**	**713,140**	**744,844**	**742,603**	**754,417**
RWA / assets	46%	47%	48%	50%	53%
LIABILITIES					
Customer funding	405,525	449,285	449,377	444,968	450,770
% change	-14%	11%	0%	-1%	1%
o/w Customer deposits	349,761	393,856	393,394	388,424	393,661
o/w Securities issued	55,763	55,429	55,983	56,543	57,109
Shareholders' equity	**43,907**	**46,990**	**48,628**	**49,978**	**50,494**
Minorities	4,853	3,624	3,871	4,335	4,812
Total liabilities & equity	**662,885**	**713,140**	**744,844**	**742,603**	**754,417**

Ratio Analysis					
	FY21	**FY22**	**FY23e**	**FY24e**	**FY25e**
Per Share Data					
EPS reported	0.70	1.03	1.34	1.47	1.51
EPS Adjusted (for valuation)	0.71	1.01	1.29	1.42	1.46
% change	74%	43%	28%	10%	3%
DPS	0.31	0.43	0.69	0.75	0.77
% change	n.m.	39%	59%	9%	3%
Dividend yield	4.3%	5.4%	8.3%	8.7%	8.7%
Payout ratio %	44%	40%	50%	50%	50%
Buyback per share	0.52	0.07	0.29	0.30	0.31
Buyback yield	0.0%	6.5%	2.9%	3.4%	3.5%
Buyback as % of earnings	75%	7%	21%	20%	20%
Total yield	4.3%	11.9%	11.2%	12.2%	12.2%
BV per share	6.60	7.53	8.14	8.70	9.11
TBV per share	6.27	7.19	7.75	8.30	8.70
Avg shares outstanding	6,654	6,237	5,974	5,744	5,540
Valuation metrics					
P/E	11.7x	8.2x	6.4x	5.8x	5.7x
P/BV	1.25x	1.10x	1.02x	0.95x	0.91x
P/TBV	1.32x	1.15x	1.07x	1.00x	0.95x
Profitability					
ROE	10.6%	13.9%	16.1%	16.5%	16.1%
ROTE	11.5%	14.6%	16.9%	17.3%	16.9%
ROA	0.7%	0.9%	1.1%	1.1%	1.1%
RoRWA	1.4%	2.0%	2.2%	2.2%	2.1%
NIM (NII / AIEA)	2.23%	2.95%	3.47%	3.43%	3.31%
Total revenues / RWAs	6%	8%	9%	8%	8%
NII / Tot revenues	70%	77%	80%	78%	76%
Fees / Tot revenues	23%	22%	21%	21%	21%
Efficiency					
Cost / income	45%	43%	41%	42%	43%
Cost / assets	1.4%	1.6%	1.7%	1.7%	1.8%
Cost / RWAs	2.9%	3.3%	3.6%	3.5%	3.4%
Balance sheet gearing					
Loan / deposit	91%	91%	94%	96%	98%
Bond securities / assets	5%	6%	6%	6%	6%
Customer loans / assets	48%	50%	50%	50%	51%
Customer deposits / funding	86%	88%	88%	87%	87%
Bonds issued / funding	14%	12%	12%	13%	13%
Asset quality					
Gross NPEs	15,443	14,463	13,981	13,493	12,989
% change	0%	-6%	-3%	-3%	-4%
Gross NPE ratio	4.1%	3.4%	3.2%	3.0%	2.8%
Texas ratio %	29%	26%	24%	22%	20%
Coverage ratio - Stage 3	47%	52%	60%	73%	85%
Cost of risk (bps)	89	100	124	131	127
Capital					
Core Tier 1 Capital (Basel III)	39,184	42,486	45,337	47,469	49,762
RWAs (Basel III)	307,335	336,920	354,436	372,264	397,010
% change	-13%	10%	5%	5%	7%
RWAs density	97%	94%	95%	99%	103%
Leverage ratio %	7%	7%	7%	7%	7%
Core Tier 1 fully loaded %	12.7%	12.6%	12.8%	12.8%	12.5%
Buffer over SREP %		4.01%	4.07%	3.66%	3.44%

Source: BofA Global Research

BofA GLOBAL RESEARCH

Exhibit 26: Companies mentioned
Companies mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
BBVA	BBVA US	BBVA	US$ 9.07	B-2-7
BBVXF	BBVA SQ	BBVA	EUR 8.252	B-2-7
BCDRF	SAN SQ	Santander	EUR 3.76	B-1-7
SAN	SAN US	Santander	US$ 4.12	B-1-7

Source: BofA Global Research

BofA GLOBAL RESEARCH

Price objective basis & risk

BBVA (BBVXF / BBVA)

We derive our PO of €8.85 (ADR USD 9.70) using a SoTP on 2025e estimates where we value each geography using a Gordon growth-implied P/CET1 multiple assuming 13% CET1 allocation to each region's RWAs. We assume 13% CoE for Spain, 14% for Mexico, 30% for Türkiye and a blended 18% for South America. We then add the market value of the stake in Telefonica, the cumulative dividends over 2024-25 and capital excess/deficit to steady-state CET1, and discount back to 1yr fwd from today.
Upside risks to our forecasts:
1. Positive earnings revision deriving from NII and cost of risk, provide upside to capital distribution
2. More stable markets would favour a recovery in AUMs, driving fee growth
3. Stronger real GDP growth in Spain and Mexico

Downside risks to our forecasts:
1. Deterioration in sovereign risk in key geographies
2. Türkiye risk could still affect capital and shareholders' returns
3. Asset quality deteriorating more than we forecast

Santander (BCDRF / SAN)

We derive our PO of €4.80 (ADR USD 5.26) using a SoTP on 2025e estimates where we value each geography using a Gordon growth-implied P/CET1 multiple assuming 13% CET1 allocation to each region's RWAs. We assume 13% CoE for Spain, 13.5% for the UK and the US, 14% for Mexico and 15% for Brazil. We then add cumulative dividends over 2024-25 and capital excess/deficit to the steady-state CET1, and discount back to 1yr fwd from today.
Upside risks to our forecasts:
1. Geared to interest rates in Spain
2. Positive earnings revision deriving from NII and cost of risk, from more resilient US and better growth in Brazil
3. Better asset quality than market fears
Downside risks to our forecasts:
1. Selic rate in Brazil may not drop as fast as we forecast
2. Deposit beta may be higher than we forecast affecting funding mix
3. Higher default rates may affect cost of risk normalization and capital levels

Analyst Certification

I, Antonio Reale, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

EMEA - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Allied Irish Banks	AIBRF	AIBG ID	Alastair Ryan
	Bank of Ireland Group	XBOIF	BIRG ID	Alastair Ryan
	BFF Banking Group	XBBZF	BFF IM	Antonio Reale
	BNP Paribas	BNPQF	BNP FP	Tarik El Mejjad
	BNP Paribas	BNPQY	BNPQY US	Tarik El Mejjad
	CaixaBank	CIXPF	CABK SQ	Antonio Reale
	Credit Agricole	CRARF	ACA FP	Tarik El Mejjad
	Danske Bank	DNSKF	DANSKE DC	Tarik El Mejjad
	Erste Bank	EBKOF	EBS AV	Alastair Ryan
	Erste Bank	EBKDY	EBKDY US	Alastair Ryan
	HSBC	XHSBF	5 HK	Alastair Ryan
	HSBC	HBCYF	HSBA LN	Alastair Ryan
	HSBC -A	HSBC	HSBC US	Alastair Ryan
	Intesa Sanpaolo	IITSF	ISP IM	Antonio Reale
	Intesa Sanpaolo	ISNPY	ISNPY US	Antonio Reale
	KBC Group	KBCSF	KBC BB	Tarik El Mejjad
	KBC Group NV	KBCSY	KBCSY US	Tarik El Mejjad
	NatWest Group	RBSPF	NWG LN	Rohith Chandra-Rajan
	Natwest Group PLc	NWG	NWG US	Rohith Chandra-Rajan
	Nordea	NBNKF	NDA FH	Tarik El Mejjad
	Nordea	XSABF	NDA SS	Tarik El Mejjad
	Nordea Bank Abp	NRDBY	NRDBY US	Tarik El Mejjad
	Santander	SAN	SAN US	Antonio Reale
	Santander	BCDRF	SAN SQ	Antonio Reale
	Societe Generale	SCGLF	GLE FP	Tarik El Mejjad
	Societe Generale	SCGLY	SCGLY US	Tarik El Mejjad
	Unicredit	UNCFF	UCG IM	Antonio Reale
	Unicredit	UNCRY	UNCRY US	Antonio Reale
NEUTRAL				
	ABN AMRO	ABMRF	ABN NA	Tarik El Mejjad
	Banco Bilbao Vizcaya Argentaria	BBVA	BBVA US	Antonio Reale
	Banco BPM	BNCZF	BAMI IM	Antonio Reale
	Bankinter	BKIMF	BKT SQ	Antonio Reale
	BBVA	BBVXF	BBVA SQ	Antonio Reale
	Commerzbank	CRZBF	CBK GY	Rohith Chandra-Rajan
	Handelsbanken	SVNLF	SHBA SS	Tarik El Mejjad
	ING Groep NV	ING	ING US	Tarik El Mejjad
	ING Groep NV	INGVF	INGA NA	Tarik El Mejjad
	Lloyds Banking Group	LLDTF	LLOY LN	Rohith Chandra-Rajan
	Lloyds Banking Group	LYG	LYG US	Rohith Chandra-Rajan
	Monte dei Paschi	BMDPF	BMPS IM	Antonio Reale
	Raiffeisen Bank International	RAIFF	RBI AV	Alastair Ryan
	StanChart	SCBFF	STAN LN	Alastair Ryan
	StanChart	XCHBF	2888 HK	Alastair Ryan
	Svenska Handelsbanke	SVNLY	SVNLY US	Tarik El Mejjad
	UBS	XUHJF	UBSG SW	Alastair Ryan
	UBS	UBS	UBS US	Alastair Ryan
UNDERPERFORM				
	Banco Sabadell	BNDSF	SAB SQ	Antonio Reale
	Barclays	BCLYF	BARC LN	Rohith Chandra-Rajan
	Barclays	BCS	BCS US	Rohith Chandra-Rajan
	Deutsche Bank	DB	DB US	Rohith Chandra-Rajan
	Deutsche Bank	XDUSF	DBK GY	Rohith Chandra-Rajan
	DNB	DNBBF	DNB NO	Tarik El Mejjad
	DNB ASA	DNBBY	DNBBY US	Tarik El Mejjad
	Mediobanca	MDIBF	MB IM	Antonio Reale
	Permanent TSB	ILPMF	PTSB ID	Alastair Ryan
	Poste Italiane	PITAF	PST IM	Antonio Reale
	SEB	SVKEF	SEBA SS	Tarik El Mejjad
	Swedbank	SWDBF	SWEDA SS	Tarik El Mejjad
	Swedbank AB	SWDBY	SWDBY US	Tarik El Mejjad
	Virgin Money UK PLC	CBBYF	VMUK LN	Rohith Chandra-Rajan
	Virgin Money UK PLC	CYBBF	VUK AU	Rohith Chandra-Rajan

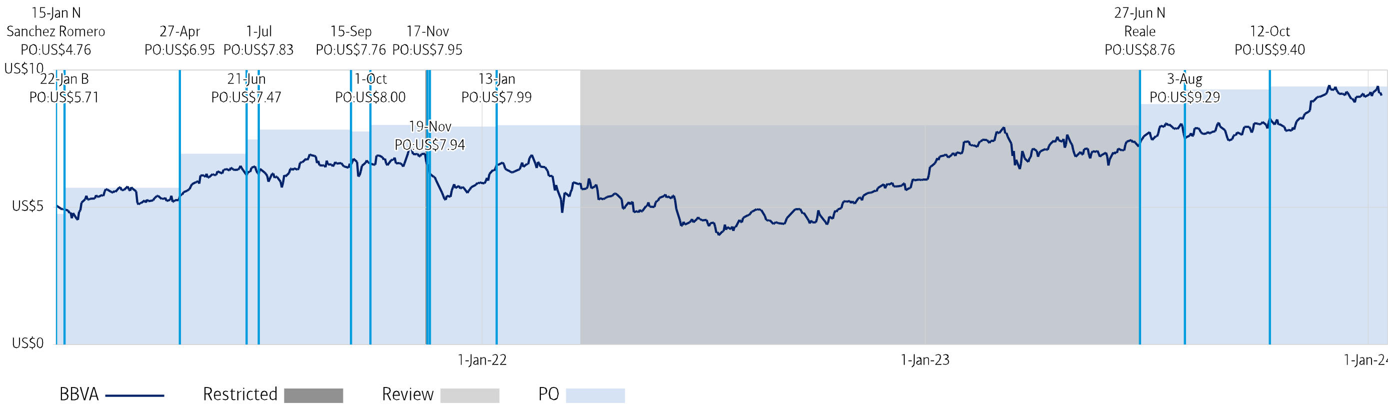
EMEA - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst

Disclosures

Important Disclosures

BBVA (BBVA) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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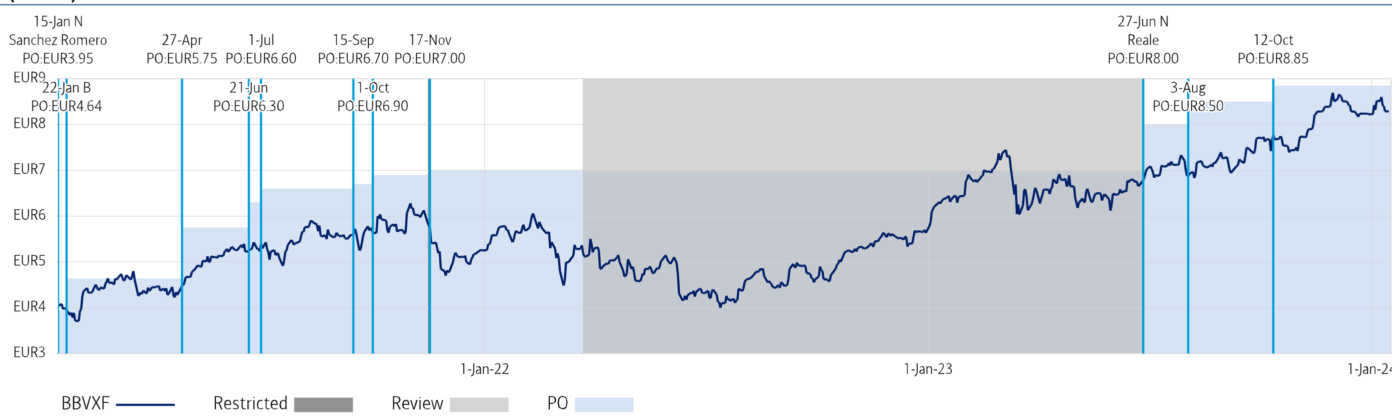
BBVA (BBVXF) Price Chart



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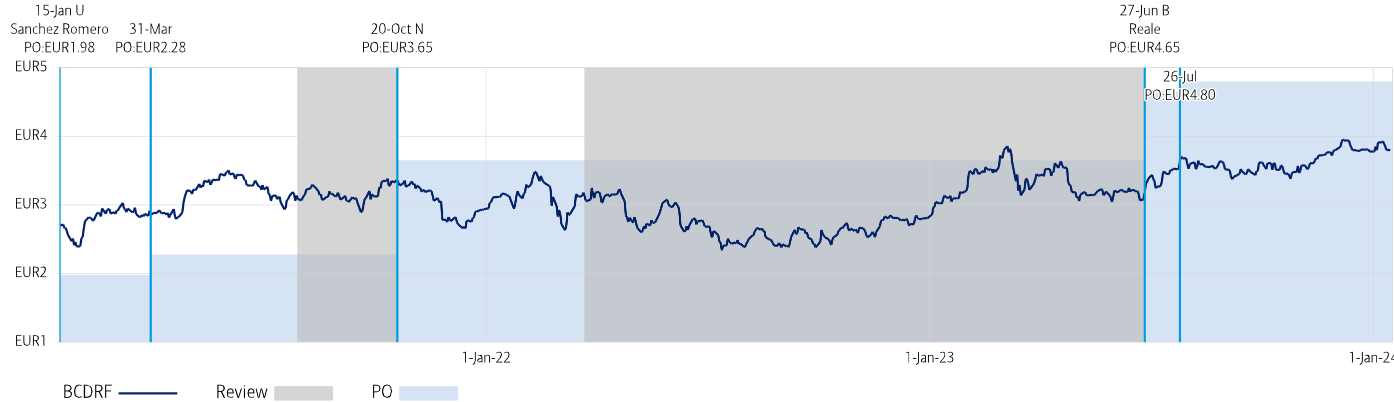
Santander (BCDRF) Price Chart



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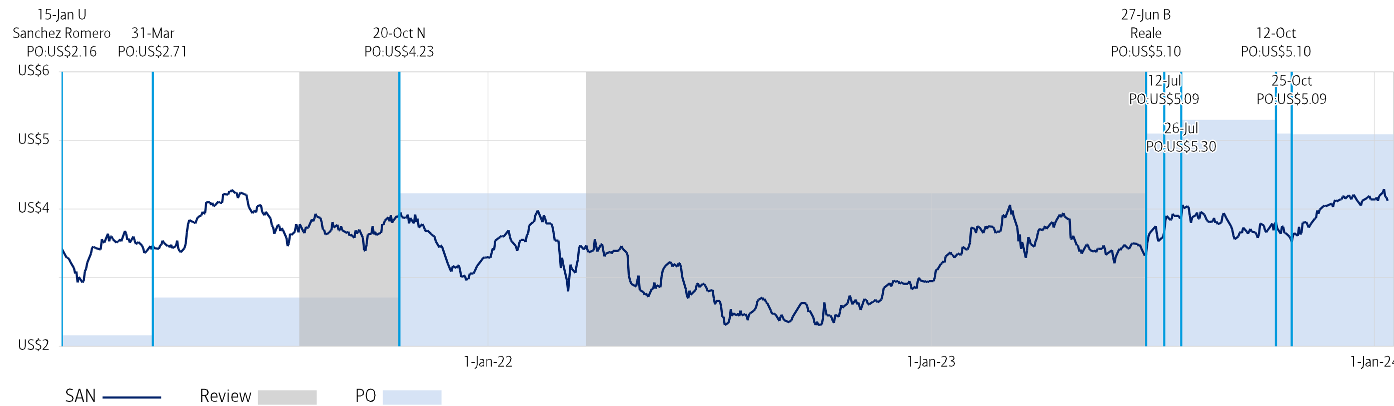
Santander (SAN) Price Chart



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Equity Investment Rating Distribution: Banks Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	100	49.75%	Buy	84	84.00%
Hold	54	26.87%	Hold	41	75.93%
Sell	47	23.38%	Sell	35	74.47%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R2]
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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R2]Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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