1. GOVERNANCE STRUCTURE AND STRATEGY OVERVIEW

1.1. Organizational structure

Banco Sabadell is one of Spain's leading banks, with assets totalling €163,346 million at 31 December 2014.

It offers a broad range of banking products and financial services, including deposits, personal banking, personal loans, mortgage loans, short- and medium-term funding, insurance, brokerage services, electronic payment services, and credit and debit cards. Our main customers are small- and medium-sized enterprises (SMEs) and individuals in Spain. At the close of 2014 Banco Sabadell had a total of 6.4 million customers, compared with 6.5 million in 2013. At the end of the year we had 2,267 operating branches in Spain. Retail banking services are primarily provided through the branch network. The group's largest business line is Commercial Banking, with 2,253 branches having this as their main activity at 2014 year-end. We operate in Spain through a set of brands, each of which is focused on a specific customer base and/or geographical region.

The group is organized into the following business units:

- Commercial Banking: is the group's largest single business line; it focuses on offering financial products and services (including bancassurance products) to large and medium-sized enterprises, SMEs, small retailers, sole proprietors, individuals, and professional and other associations.

  In most parts of Spain, the Commercial Banking line operates under the group's flagship brand, SabadellAtlántico.

It also operates under the following brands:

-SabadellHerrero, in Asturias and León.
-SabadellGuipuzcoano, in the Basque Country, Navarra and La Rioja.
-SabadellCAM, in Valencia and Murcia.
-SabadellSolbank, in the Canary Islands, the Balearic Islands and the southern and south-eastern coastal areas of mainland Spain, meeting the needs of European residents in Spain.
-ActivoBank serves customers who prefer to do their banking exclusively by telephone or on line.
-SabadellGallego, for the Bank's branches in Galicia.

- Corporate Banking and Global Businesses: this unit offers products and services to large corporations and financial institutions, both Spanish and international. Its activities encompass corporate banking, structured finance, corporate finance, development capital, international trade and consumer finance.

- Markets and Private Banking: this unit offers savings and investment management services to Banco Sabadell customers, including the analysis of investment options, market trading, active wealth management and custody services. Markets and Private Banking comprises the following businesses, which are managed on an integrated basis: SabadellUrquijo Banca Privada, the Investment, Products and Analysis unit, Treasury and Capital Markets, and Securities Trading and Custody services.

- Asset Transformation: In late 2014, in view of changing market trends and the high regard in which the group's Solvia unit is held in the property market, the asset management business was split into two areas: Banco Sabadell Asset Transformation, which handles the overall management of the Bank's real estate assets taking an integrated view of the whole process; and Solvia, which will provide services for real estate asset portfolios for both the group and third parties with a focus on business and leveraging value.
  Asset Transformation has the prime task of taking an integrated approach to the group's real estate assets and designing and carrying out its asset transformation strategy. Solvia, the group's real estate business, focuses on real estate services through all stages of the product cycle —property sales and servicing, land management, preparation and development —and has positioned itself as a key player in Spain's real estate market.

Banco Sabadell is also developing its business in foreign countries, where it currently has a total of 53 branches and representative offices within its different areas of business.

- BS America: this area is made up of a number of business units, affiliates and representative offices that engage in corporate banking, private banking and commercial banking. The Bank has the capacity and experience to provide all types of banking services, from the most complex and specialized for large corporations, including structured project finance operations, to products for individuals. The business is carried on through the Banco Sabadell Miami Branch, Sabadell United Bank and Sabadell Securities.

- BancSabadell d'Andorra: incorporated in the Principality of Andorra, BancSabadell d'Andorra is owned 50.97% by Banco Sabadell. Its customers consist of medium-to-high earners and leading companies in the Principality of Andorra.

Banco Sabadell is the parent of a corporate group which at 31 December 2014 comprised 232 companies of which 165 were treated as group undertakings and 67 were associated undertakings; at 31 December 2013, the group consisted of 305 companies of which 177 were group undertakings and 128 were associates.

As regards the Bank's governance structure, the Board of Directors is the highest decision-making body in the Company and its consolidated group, as it is responsible under the law and the Articles of Association for managing and representing the institution in all aspects related to the banking business, supervision and oversight as set out in the Articles of Association and based on the powers granted by the General Meeting.

Its responsibilities include:

a) approving decisions on business and financial transactions of particular importance to the Company and the Bank's general strategies;

b) appointing and, as necessary, removing senior executives of the Company and other undertakings in the consolidated group;

c) identifying the main risks facing the Company and the consolidated group and implementing and monitoring the operation of appropriate internal control and reporting systems;

d) setting policy on the reporting and disclosure of information to shareholders, the markets and the general public;

e) setting policy on treasury shares in accordance with any guidelines laid down by the General Meeting;

f) authorizing transactions between the Company and directors or significant shareholders that could lead to conflicts of interest; and

g) any other responsibilities set out in the Articles of Association.

The members of the Board of Directors at 31 December 2014 were as follows:

Members of the Board of Directors	Position
José Oliu Creus	Chairman
José Manuel Lara Bosch	First Deputy Chairman
José Javier Echenique Landiribar	Second Deputy Chairman
Jaime Guardiola Romojaro	Managing Director
Héctor María Colonques Moreno	Director
Joaquin Folch-Rusiñol Corachán	Director
María Teresa García-Milá Lloveras	Director
Joan Llonch Andreu	Director
David Martínez Guzmán	Director
José Manuel Martínez Martínez	Director
José Ramón Martínez Sufrategui	Director
Antonio Vitor Martins Monteiro	Director
José Luis Negro Rodríguez	Director - General Manager
José Permanyer Cunillera	Director
Miquel Roca i Junyent	Secretary to the Board (non-director)
Maria José García Beato	Deputy Secretary to the Board (non-directo

The Board of Directors has implemented a set of clear and transparent rules and regulations on corporate governance as required by Spanish law. Eleven of the 14 members of the Board are non-executive directors and include eight independent directors.

At present, there are five committees to which the Board of Directors delegates functions by making use of the powers conferred on it in the Articles of Association; meetings of the committees are attended by members of senior management.

These committees are:

The Executive Committee

The Audit and Control Committee

The Appointment and Remuneration Committee

The Risk Control Committee

The Strategy Committee

The composition of these committees at 31 December 2014 is shown in the table below:

Board Committees - membership

Position	Executive	Audit and Control	Appointment and Remuneration	Risk Control	Strategy
Chairman	José Oliu Creus	Joan Llonch Andreu	Héctor María Colonques Moreno	José Manuel Martínez Martínez	José Oliu Creus
Deputy Chairman	-	-	-	José Permanyer Cunillera	-
Member	José Javier Echenique Landiribar	María Teresa Garcia-Milà Lloveras	José Javier Echenique Landiribar	María Teresa Garcia-Milà Lloveras	José Javier Echenique Landiribar
Member	Jaime Guardiola Romojaro	José Ramón Martínez Sufrategui	Joaquín Folch-Rusiñol Corachán	Joan Llonch Andreu	Joaquín Folch-Rusiñol Corachán
Member	José Luis Negro Rodríguez	-	José Manuel Lara Bosch	-	Jaime Guardiola Romojaro
Member	José Permanyer Cunillera	-	-	-	José Manuel Lara Bosch
Member	-	-	-	-	José Manuel Martínez Martínez
Secretary	María José García Beato	Miquel Roca i Junyent	Miquel Roca i Junyent	María José García Beato	Miquel Roca i Junyent
Number of meetings held in 2014	33	6	11	7	6

Executive Committee

The Executive Committee is responsible for the coordination of the Bank's executive management, adopting to this end any resolutions and decisions within the scope of the powers vested in it by the Board of Directors; decisions adopted by the Committee are reported to the Board of Directors.

Audit and Control Committee

The purpose of the Audit and Control Committee is to review reports from the Internal Audit Department or the Comptroller General to verify that good banking and accounting practices are being followed in all parts of the organization, as well as to ensure that general management and other executive functions take suitable measures to address improper conduct or practices by persons in the organization. It is also a watchdog, ensuring that the measures, policies and strategies defined by the Board are duly implemented; the committee meets not less than once a quarter.

Without prejudice to any other tasks being assigned to it by the Board of Directors, the Committee's basic responsibilities are:

a) reporting to the General Meeting on all issues raised by shareholders that are within its remit;

b) monitoring the effectiveness of the company's internal controls, any internal audit carried out and the risk management systems in place, and discussing with auditors or auditing firms any significant internal control weaknesses identified in the course of the audit;

c) overseeing the preparation and presentation of statutory financial information;

d) making recommendations to the Board of Directors, for submission to the General Meeting, on the appointment of external auditors and their terms of engagement, the scope of their professional mandate and, if applicable, the termination or non-renewal of their engagement; reviewing performance of the auditing agreement and ensuring that the opinion on the annual accounts and the main findings of the Auditor's report are expressed in a clear and precise way;

e) advising on the annual accounts and the quarterly and half-yearly financial statements and any prospectuses required to be filed with the regulatory or supervisory authorities; monitoring regulatory compliance; ensuring that generally accepted accounting principles have been correctly applied, and reporting on any proposed amendments to those principles;

f) maintaining working relations with external auditors to receive information on, and enquire into, any issues that could compromise their independence and keeping itself informed of any other matters related to the audit process and to auditing standards;

g) advising on any issues referred to the Committee by the Board of Directors that are within its terms of reference; and

h) any other matters for which the Committee is responsible by law or under the Articles of Association or any regulations made in accordance therewith, or under any generally applicable rules on corporate governance.

The Committee also has the following tasks in connection with compliance with regulatory provisions, legal requirements and the precepts of corporate governance codes:

1. Overseeing compliance with the law, internal codes and regulatory provisions governing Company activities;

2. Assessing the effectiveness of, and compliance with, the Regulations of the General Meeting, the rules of procedure of the Board of Directors, the Code of Conduct and, particularly, the Internal Code of Conduct for trading on the stock markets;

3. Reviewing compliance with the rules on corporate governance and submitting recommendations for improvement to the Board as it sees fit; and

4. Supervising the corporate governance report to the Board for approval and inclusion in the annual report.

Appointment and Remuneration Committee

The Appointment and Remuneration Committee is responsible for evaluating the profiles of the persons judged most suitable for membership of the different committees and for taking these proposals to the Board. It meets not less than once a year.

Without prejudice to any other tasks assigned to it by the Board of Directors, the Committee's basic responsibilities are:

a) drafting and reviewing the criteria to be followed with regard to the composition of the Board of Directors and the selection of candidates;

b) presenting proposals for appointing members to the Board so that it may directly appoint them (co-optation) or present these proposals for consideration by the General Meeting;

c) proposing to the Board of Directors the system and amount of annual remuneration for the Chairman of the Board of Directors, the executive directors and the Bank's senior managers, and the systems under which the Board shares in the company's profits; and advising on director remuneration policy;

d) periodically reviewing the general principles of the group's remuneration policy and ensuring that remuneration programmes are in line with those principles for all employees;

e) ensuring that remuneration is transparent; and

f) fostering gender diversity as far as possible.

Risk Control Committee

The Risk Control Committee is responsible for:

a) determining and making recommendations to the full Board on overall levels of exposure to particular countries, business sectors and risk categories, for approval by the Board;

b) determining and proposing to the full Board the application of maximum levels of risk for specific transactions with credit institutions and customers, and setting maximum risk levels for portfolios or individual investments in government bonds, shares, bonds, options, swaps and generally all types of instruments or securities that represent a default, investment, interest rate or liquidity risk for the Group;

c) determining and making recommendations to the full Board on annual limits for investment in the real estate market and on the principles and volumes applicable to different types of real estate investment;

d) determining and making recommendations to the full Board on any delegations of authority considered appropriate for the approval and acceptance of individual risks, within the limits established as described above;

e) deciding on any individual risks for the approval of which the Risk Control Committee is responsible by virtue of the delegation of authority referred to above;

f) monitoring and overseeing the proper implementation of any delegation of authority under d) above;

g) reporting on a monthly basis to the full Board regarding the performance of its functions under this article or any other applicable provisions of law or the Articles of Association;

h) providing quarterly reports to the full Board on the levels of risk incurred, the investments made and the performance of those investments, and on any impacts that could be caused to group revenues by changes in interest rates; also on whether risk levels are appropriate to the VaRs approved by the Board;

i) submitting for the Board's approval any change in the limits referred to in a) and b) that exceed authorized levels by more than 10% and 20%, respectively; and

j) advising the Appointment and Remuneration Committee on whether employee compensation schemes are consistent with the Bank's risk, capital and liquidity levels.

Strategy Committee

The committee's brief is to report on any matter of a general nature or of particular significance in relation to strategy. It meets not less than once every six months.

1.2. Operating review: objectives achieved and actions implemented

The group's development objectives are focused on profitable growth and the generation of shareholder value through a strategy of business diversification based on high returns, efficiency and quality of service together with a conservative risk profile, while maintaining high standards of ethics and professional conduct combined with sensitivity to stakeholders' interests.

The Bank has a business model that fosters long-term customer relationships through constant efforts to promote customer loyalty by adopting an initiative-based, proactive approach. The Bank offers a comprehensive range of products and services, competent, highly qualified personnel, an IT platform with ample capacity to support future growth and a relentless focus on quality.

Since the onset of the financial crisis, Spain's banking sector has been going through an unprecedented process of consolidation. Higher levels of capital, stricter provisioning requirements, the economic recession and pressure from the capital markets are some of the factors that have driven Spanish banks to merge and gain in scale, maximize efficiency and strengthen their balance sheets.

During the last decade, Banco Sabadell has expanded its geographic presence and increased its market share in Spain through several acquisitions, the largest of which was Banco CAM in 2012, which enabled it to notably expand its balance sheet. In 2013 Banco Sabadell was able to undertake further corporate actions on economically acceptable terms in a context of banking sector restructuring. Following the acquisition of the Penedès branch network, Banco Gallego and Lloyds España in 2013, Banco Sabadell is well positioned to grow organically and to benefit from the economic recovery in Spain.

Synergies from the Banco CAM merger exceeded expectations, with the systems and operational integration of the Penedès branch network into that of Banco Sabadell being successfully completed in 2013, followed by the integration of Banco Gallego and Lloyds España in 2014.

Acquisitions and organic growth in recent years have enabled Banco Sabadell to reinforce its position in some of Spain's most prosperous regions (e.g. Catalonia, Valencia and the Balearic Islands) and to increase its market share in other key areas. As of September 2014 Banco Sabadell had shares of 15.1%, 14.2% and 9.2%, respectively, of the credit markets in these regions, which in 2013 together accounted for 31% of Spanish GDP. At national level, Banco Sabadell has market shares of 7.4% in lending and 7.2% in deposits according to the most recent information available (October 2014). Banco Sabadell also has a strong position in other products such as ICO funding, with a market share of 17.5% (December 2014); commercial loans, with a share of 12.3% (October 2014); direct salary payments, with 5.7% (November 2014) and POS terminal transactions, with 15.5% (September 2014).

Banco Sabadell remains a leader in cross-border operations through its presence in strategic markets and by serving companies as they expand abroad; as of November 2014 it had market shares of 25.6% for documentary credits for exports and 16.9% for imports

In 2014 Banco Sabadell experienced growth in deposit-taking driven by the flight to quality and further supported by marketing campaigns. As of October 2014 the Bank held an 8.3% share of time deposits by households and a 13.9% of time deposits by non-financial companies. It was particularly successful in attracting off-balance sheet funds, which increased as a proportion of the overall balance sheet. Its share of assets in mutual funds increased from 4.1% to 5.1% during the year.

Since 2007 deposits have been the Bank's primary source of funding, thereby reducing its dependence on capital markets. Other developments during the year were the successful completion of a €1,250 million public offering of covered bonds on the wholesale market in November and two senior debt issues for €360 and €500 million for small investors in November and December respectively, which aroused great interest.

Another aim for 2014 that Banco Sabadell more than accomplished was to reduce the gap between customers of the former Banco CAM and Banco Sabadell customers in terms of funding margin and customer loyalty. This was achieved by using a customer-centric business model, personalized customer management standards based on value creation, and sales processes which included top-flight advisory and sales support, backed by product-specific sales campaigns.

In 2014, Banco Sabadell also surpassed the service quality level attained in 2011, which had declined due to the integration of Banco CAM in 2012, and its commercial banking brands were among the first 11 in the Top 50 brands at 2014 year-end according to a survey by Stiga-Equos.

The global financial crisis has led to stricter regulatory requirements as to capital and reserves; Banco Sabadell has made notable efforts to improve its position in both respects.

The bank booked €2,500 million in allowances in 2014, enabling it to increase its reserves and attain an overall coverage ratio (loans and real estate) of 13.1%.

On 26 October 2014, the ECB published the results of its Comprehensive Assessment of European banks, including the Asset Quality Review (AQR) and the stress test, which underlined Banco Sabadell's sound capital position.

Banco Sabadell is the only Spanish bank whose initial capital ratio was not adjusted as a result of the AQR, which is the best proof of the rigour and transparency of our provisioning policy. This clearly evidenced the bank's solvency, beyond any stress test, an aspect which positively surprised the market.

The stress test concluded that Banco Sabadell has a common equity tier 1 (CET1) ratio of 10.26% and that, in the most adverse scenario considered, that ratio would be 8.33%, well above the required minimum of 5.5%. With these ratios, it was estimated that Banco Sabadell had surplus capital amounting to over €1,700 million under the baseline scenario and over €2,200 million under the most adverse scenario.

These results did not consider the effect of the mandatory convertible bonds (not included in the stress test even though they mature in 2015) or all of the deductions envisaged under Basel III. If those items had been considered, the CET1 ratio in the adverse scenario would have been 9.38% (including convertibles) or 8.8% (fully loaded).

This assessment was a condition precedent for the ECB to undertake its new functions as supervisor of the Euro area's principal banks in November 2014. Far from being a limited, straightforward exercise, the comprehensive assessment took almost a year and covered a very significant portion of the Bank's processes and procedures, requiring a team of some 250 Bank employees to be wholly or partly occupied on the project.

2. BUSINESS PERFORMANCE AND RESULTS

2.1. Global economic and financial environment

In the course of 2014 Europe took decisive steps towards banking union and this helped to maintain continuity in the normalization of financial conditions in the region. In particular, agreement was reached on establishing a bank resolution mechanism and single resolution fund. The European Central Bank (ECB) began to perform its functions as a single banking supervisor. Prior to this it carried out a comprehensive assessment of the European banking system.

In the global arena political and geopolitical developments were a major focus of attention. Geopolitical tensions flared in the Middle East and, more especially, in Ukraine. In Europe political events were the prime cause of uncertainty. The fragmentation revealed by national voting intention surveys has raised questions over the future governability of certain countries. One example of this is Greece, where an early election was held at the beginning of 2015. At the time this report went to press the left-leaning Syriza coalition had just emerged victorious from the 25 January election. The coalition came close to obtaining an absolute majority. In the end Syriza made an agreement with another party (Independent Greeks) to form a coalition government.

In 2014 the world economy was characterized by modest growth, with inflation remaining muted. The sharp fall in the price of oil in the latter months of the year increased the downward pressure on inflation. Oil prices, affected by demand as well as supply factors, fell by nearly 50% and now stand at the levels they were at in 2009. The financial markets continued to be supported by accommodative monetary policies although there were occasional bouts of instability.

In terms of economic activity, the global slowdown in growth masked divergent growth paths in different countries. In the US the economy staged a gradual recovery and the labour market surprised on the upside. The Eurozone barely showed any increase in activity as investment remained weak. Investor and business confidence was weighed down by geopolitical uncertainty over the conflict in Ukraine. The United Kingdom continued to show robust growth and steadily falling unemployment. In Europe the European Commission presented a programme, the Juncker plan, whose aim is to mobilize €315 billion for investment over the period 2015-2017. In Japan an increased tax on consumer spending put a brake on economic activity in the middle of the year. The emerging markets continued to see a slowdown in their economic growth. China saw a continuation of the structural deceleration of its economy, which was constrained by a weak real estate market. In Latin America the dominant theme was economic fragility and political uncertainty in Brazil. In Mexico, meanwhile, activity saw an upturn albeit at a pace that was slower than anticipated. The country continued to make progress in implementing structural reforms. The Russian economy suffered damage from geopolitical instability and falling oil prices. This fall was a factor affecting oil exporting countries generally.

The Spanish economy stood out as a success story within the Eurozone. Activity recovered after bottoming out in 2013 and began to create employment for the first time since 2008. Domestic demand was the main driver behind growth. Rising levels of activity were supported by a more benign financial climate and a slackening in the pace of budgetary consolidation. At the same time, the construction industry steadied itself after the dramatic correction it had gone through in the preceding years. Meanwhile, the process of private sector deleveraging continued throughout the year. The most significant reform was to make changes in the tax legislation, mainly affecting the Personal Income Tax ("IRPF") and corporation tax. These changes resulted in lower rates of tax and greater restrictions on certain deductions. In the financial arena, the European Union's financial assistance programme came to an end in January.

Inflation fell back in all the main developed economies. In the Eurozone, inflation was one of the most keenly scrutinized variables. Inflation indices consistently surprised on the downside and sank to very low levels, especially on the European periphery. Surplus capacity, lower commodity prices and the sluggish growth in bank lending all contributed to the decline. Against this backdrop, forecasts for long-term inflation in the Eurozone slipped lower. In the US the lack of pressure for pay increases helped inflation to remain firmly below the Federal Reserve's target. In the UK inflation plunged to levels not seen since the year 2000. Finally, in Japan inflation rose after the increase in the tax on consumer spending before falling back into a gradual decline.

The monetary policies pursued by the principal central banks remained accommodative, albeit with regional variations. The ECB again resorted to stimulus measures to counteract the low level of inflation. Policy rates of interest were set at historically low levels (0.05%) and the deposit facility rate was taken into negative territory (-0.20%). The ECB also set up a programme of long-term liquidity-boosting operations (TLTROs) to encourage banks to increase lending. It also launched programmes for the purchase of asset-backed securities (ABS's) and covered bonds. The ECB has indicated its general aim of increasing the size of its balance sheet to levels last seen in early 2012. In such conditions, given the persistent low level of inflation, it has left the door open for further stimulus measures. As this report went to press, the ECB was announcing an extension of its asset purchase programme following its meeting of 22 January 2015. The institution also said that it would buy €60,000 million worth of assets per month and that it would do so at least until September 2016. The assets to be purchased will include government bonds. In the US, the Fed brought its asset purchasing programme (US bonds and mortgage-backed securities) to an end. Despite keeping its key rate at historically low levels, the Fed thus marked a change of direction in its monetary policy. In the UK, the Bank of England kept base rates unchanged at 0.50% although some members were in favour of an increase. The BoE also announced a number of macroprudential measures to cool the property market. In Japan, the central bank moved aggressively to pull the country out of deflation, including a substantial increase in government bond purchases. These purchases will absorb virtually the whole of the government's borrowing requirement for 2015.

In the long-dated bond markets, yields fell sharply in the main developed economies. US bonds found support in fears over global economic growth and a more uncertain geopolitical environment. German bond yields sank to all-time lows. The German long bond was boosted by falling inflation, Eurozone economic weakness and the ECB's accommodative policy stance. On the European periphery, with the exception of Greece, risk premium continued to tighten significantly. This was spurred by the ECB's accommodative approach and expectations that it would finally adopt a broad programme of bond purchases. In Spain bond yields fell to historic lows — lower, even, than in the US. During the year the three main credit rating agencies upgraded their ratings for Spanish sovereign debt. And Greece was able to issue long-term debt for the first time since the country was bailed out. Both Portugal and Ireland gradually regained normal access to global debt markets. In May Portugal exited from its assistance plan without making any request for further support. In Japan too, yields on government bonds fell, reaching their lowest-ever level. Massive bond purchases by the Bank of Japan gave rise to distortions, causing the market to become illiquid at times.

In the currency markets the euro weakened against the dollar and sterling. The divergence between the monetary policies pursued by the ECB and the two other central banks were the main factor behind these movements. The weak economic performance of the Eurozone compared with the US and the UK contributed to the decline. The yen showed a significant depreciation against the dollar in the second half of the year, sinking to the levels of 2007. The Bank of Japan's policy of monetary easing and the deterioration of the country's economy after the tax increase drove the yen lower.

In the equity markets, key US stock indices showed gains over the period. The S&P 500, in particular, rose by 26.9% in euro terms. Some of this improvement in euro terms is explained by the strength of the dollar. In Europe the Euro Stoxx 50 closed the year without a well-defined rent. The index barely managed a rise of 1.2%. In Spain the IBEX index was up by 3.7%, in sharp contrast to the 21.4% gain it had made in 2013.

Financial markets in the emerging markets were affected by high degrees of volatility and sharp currency-related falls. This was fuelled by uncertainty over the extent of the economic slowdown in China. Further causes of weakness were political instability and worries over the possible start of interest rate hikes by the Fed. Dramatic falls in the oil price also stoked financial turmoil in countries such as Russia and Venezuela. In the case of Venezuela, this even aroused market fears that the country might have to seek a restructuring of its external debt.

2.2. Key financial and non-financial indicators

Some key numbers and ratios for the Bank, including financial and non-financial data of critical importance to the running of the organization, are set out below:

		2014	2013	Change YoY (%)
Balance sheet (Thousand euro)	(A)			
Total assets		163,345,673	163,522,541	(0.1)
Gross loans and advances to customers, excluding reverse repos		121,140,838	124,614,933	(2.8)
Gross loans and advances to customers		121,728,435	125,302,943	(2.9)
On-balance sheet funds	(1)	121,806,632	123,753,008	(1.6)
Of which:On-balance sheet customer funds	(2)	94,460,668	94,497,187	(0.0)
Mutual funds		15,705,612	11,018,570	42.5
Marketing of pension funds and insurance		11,755,126	12,423,646	(5.4)
Funds under management	(3)	152,185,441	149,122,858	2.1
Shareholders' funds		10,223,743	10,037,368	1.9
Income Statement (Thousand euro)	(B)			
Net interest income		2,259,706	1,814,694	24.5
Gross income		4,800,526	3,831,198	25.3
Profit before impairment and other provisions		2,749,104	1,879,690	46.3
Profit attributed to the parent company		371,677	145,915	154.7
Ratios (%)	(C)			
ROA	(4)	0.23%	0.10%	
ROE	(5)	3.70%	1.58%	
ROTE	(6)	4.14%	1.75%	
Cost/income ratio	(7)	53.14%	64.19%	
Cost/income ratio excluding non-recurring expenses	(8)	51.93%	62.28%	
Core capital / Common Equity	(9)	11.7%	11.7%	
Tier I	(10)	11.7%	11.7%	
BIS ratio	(11)	12.8%	12.5%	
Risk management	(D)			
Doubtful loans (€'000)	(12)	14,192,150	16,021,491	
Loan loss ratio (%)	(12)	12.17	13.63	
Loan loss and real estate impairment allowances (€'000)		17,441,989	18,341,298	
Loan loss coverage ratio (%)	(13)	50.3	52	
Loan loss and real estate coverage ratio (%)	(14)	13.14	13.61	
Share data (period end)	(E)			
No. of shareholders		231,481	262,589	
Number of shares		4,024,460,614	4,011,481,581	
Share price (€)		2.205	1.896	
Market capitalization (€'000)	(15)	8,873,936	7,605,769	
Earnings per share (EPS) (€)		0.09	0.04	
Book value per share (€)	(16)	2.54	2.50	
Price/Book value (times)		0.87	0.76	
Price/earnings ratio (P/E) (times)		23.88	52.12	
Adjusted for effect of mandatory convertible bonds:				
Total number of shares including shares resulting from conversion of bonds		4,289,732,386	4,298,634,476	
Earnings per share (EPS) (€)		0.09	0.03	
Book value per share (€)		2.38	2.34	
Price/Book value (times)		0.93	0.81	
Other data				
Branches		2,320	2,418	
Employees		17,529	18,077	

(A) This section of the table provides an overview of changes in the main items on the group's consolidated balance sheet, focusing especially on data related to customer loans and customer funds.

(B) This section sets out key components of the income statement for the last two years.

(C) The ratios in this section of the table have been included to give a meaningful indication of profitability, efficiency and capital adequacy in the last two years.
(D) This section gives some key numbers and ratios related to risk and risk management within the group.
(E) This section provides data on the share price and other stock market ratios and indicators.

(1) Includes customer deposits, debts represented by marketable securities, subordinated liabilities and liabilities under insurance contracts.
(2) Includes customer deposits (ex repos) and other liabilities placed via the branch network: mandatory convertible bonds, non-convertible bonds issued by Banco Sabadell, commercial paper and others.
(3) Includes on-balance sheet funds, mutual funds, pension funds, asset management and insurance contracts distributed by the Group..
(4) Consolidated profit (loss) for the year / average total assets.
(5) Income attributable to the group / average shareholders' equity (not treating income attributable to the group as part of shareholders' equity).
(6) Income attributable to the group / average shareholders' equity (not treating income attributable to the group as part of shareholders' equity, and deducting goodwill).
(7) Personnel and other general administrative expenses / gross income. To calculate these ratios, gross income was adjusted considering only net trading income and recurring exchange differences. The ratio for 2013 has been adjusted on this basis.
(8) Personnel and other general administrative expenses (less non-recurring expenses) / gross income. To calculate these ratios, gross income was adjusted considering only trading income and recurring exchange differences. The ratio for 2013 has been adjusted on this basis.
(9) Core capital / risk-weighted assets (RWA). The ratio for 2013 was calculated in accordance with Basel II. The December 2014 ratio was calculated according to Basel III with the modifications provided in Bank of Spain Circular 2/2014 (approved in July 2014).
(10) Tier 1 capital / risk-weighted assets (RWA). The ratio for 2013 was calculated in accordance with Basel II. The December 2014 ratio was calculated according to Basel III with the modifications provided in Bank of Spain Circular 2/2014 (approved in July 2014).
(11) Total capital / risk-weighted assets (RWA). The ratio for 2013 was calculated in accordance with Basel II. The December 2014 ratio was calculated according to Basel III criteria with the modifications provided in Bank of Spain Circular 2/2014 (approved in July 2014).
(12) The figures and percentages shown do not include assets covered by the Asset Protection Scheme (APS).
(13) The ratio of allowances to doubtful assets.
(14) Shows the allowances covering the group's overall credit risk and real estate exposure.
(15) The number of shares outstanding multiplied by the share price at year end.
(16) Shareholders' equity / Number of shares outstanding.

2.3. Financial review

Balance sheet and income statement

Notarial documents formalizing the merger of Banco Gallego and Sabadell Solbank into Banco Sabadell were registered with the Barcelona Mercantile Register on 14 March 2014. The IT integration of the business of both undertakings was completed during the first quarter of the year.

This was the culmination of a series of major changes in the structure of the Banco Sabadell group in the years 2013 and 2014 which can be summarized as follows:

- BMN-Penedès (acquisition of BMN's banking business in Catalonia and Aragón): included in the consolidated accounts as from 1 June 2013.
- Sabadell Solbank (acquisition from Lloyds TSB Bank of 100% of Lloyds Bank International and Lloyds Investment España): included in the consolidated accounts as from 30 June 2013.Sabadell Solbank was subsequently merged with Banco Sabadell in March 2014.
- Banco Gallego: included in the consolidated accounts as from 31 October 2013. Banco Gallego was subsequently merged into Banco Sabadell in March 2014.
- Acquisition of JGB Bank: on 11 July 2014, Banco Sabadell's subsidiary in Miami, Sabadell United Bank N.A., acquired and immediately absorbed JGB Bank, N.A.

Only the incorporation of JGB Bank into the group in 2014 had any effect on the inter-year differences in balance sheet items attributable to changes in the composition of the consolidated group, since all the other undertakings referred to above (BMN-Penedès, Sabadell Solbank and Banco Gallego) had already been integrated into the consolidated accounts by 31 December 2013. In the case of the income statement, however, inter-year comparisons of profit and loss data for 2014 with those of the preceding year were affected, albeit not to any significant degree, by the successive additions of the four undertakings, since the first of them was not incorporated into the consolidated accounts until 1 June 2013.

It should be noted that the balance sheet and income statement for 2013 as presented in this financial review section of the Report of the Directors have been restated to show the impact that the early adoption of IFRIC 21 would have had in that year.

The consolidated income statement of the Banco Sabadell Group for 2014 showed solid progress over the year, driven by increasing business volumes in the group's ordinary operations and rising ordinary margins from those operations. Particularly noteworthy were the good pace of inflows of customer funds, the strong growth in higher added-value products and, particularly in the second half of the year, the revival in the demand for credit, especially among small and medium-sized businesses.

Banco Sabadell's solvency was confirmed by the publication of the results of the European Central Bank's comprehensive assessment of the 130 largest banks in the Eurozone in October 2014. The ECB report made it clear that Banco Sabadell’s capital ratio does not need to be adjusted and that under the most adverse scenario it would have a CET1 capital ratio of 8.33%, well above the minimum of 5.5%. Under this adverse scenario, the Bank's CET1 ratio would be 9.38% if mandatory convertible bonds, which were not taken into account in the assessment (and most of which are due for conversion in 2015) were included; and 8.8% on a fully loaded basis.

Balance sheet

At the end of 2014, total assets for the Banco Sabadell Group amounted to €163,345.7 million, very similar to the figure at the end of 2013 (€163,522.5 million).

Thousand euro

	2014	2013	Change YoY (%)
Cash and balances with central banks	1,189,787	3,201,898	(62.8)
Assets held for trading, derivatives and other financial assets	3,253,356	2,623,485	24.0
Available-for-sale financial assets	21,095,619	19,277,672	9.4
Loans and receivables	117,895,179	118,989,126	(0.9)
Loans and advances to credit institutions	4,623,197	3,525,521	31.1
Loans and advances to customers (net)	110,835,723	112,928,890	(1.9)
Debt securities	2,436,259	2,534,715	(3.9)
Investments	513,227	640,842	(19.9)
Tangible assets	3,982,866	3,935,322	1.2
Intangible assets	1,591,296	1,501,737	6.0
Other assets	13,824,343	13,352,459	3.5
Total assets	**163,345,673**	**163,522,541**	**(0.1)**
Liabilities held for trading and derivatives	2,254,459	1,972,190	14.3
Financial liabilities at amortised cost	145,580,114	147,269,474	(1.1)
Deposits from central banks	7,201,546	9,227,492	(22.0)
Deposits from credit institutions	16,288,193	13,857,264	17.5
Customer deposits	98,208,370	99,362,908	(1.2)
Marketable debt securities	20,196,329	21,166,915	(4.6)
Subordinated liabilities	1,012,362	1,089,046	(7.0)
Other financial liabilities	2,673,314	2,565,849	4.2
Liabilities under insurance contracts	2,389,571	2,134,139	12.0
Provisions	395,215	664,246	(40.5)
Other liabilities	1,510,362	1,266,067	19.3
Total liabilities	**152,129,721**	**153,306,116**	**(0.8)**
Shareholders' funds	10,223,743	10,037,368	1.9
Valuation adjustments	937,416	120,814	--
Non-controlling interests	54,793	58,243	(5.9)
Total equity	**11,215,952**	**10,216,425**	**9.8**
Total liabilities and equity	**163,345,673**	**163,522,541**	**(0.1)**
Contingent risks	9,132,560	8,663,950	5.4
Contingent commitments	14,769,638	12,026,000	22.8
Total memorandum accounts	**23,902,198**	**20,689,950**	**15.5**

Gross loans and advances to customers (excluding repos) were 75% of the group's total consolidated assets and amounted to €121,140.8 million at year-end. This item declined by 2.8% year-on-year (mainly as a result of a reduction in doubtful balances), although demand for credit showed signs of recovering in the latter months of the year. In the fourth quarter, for example, gross loans and advances (excluding repos and doubtful loans) increased by €773.1 million.

Mortgage loans were the largest single component of gross lending (close to 45%), amounting to €54,260.2 million at 31 December 2014.

Thousand euro

	2014	2013	Change (%) YoY (%)
Mortgage loans & credit	54,260,230	57,580,035	(5.8)
Other secured loans & credit	2,155,279	2,358,314	(8.6)
Commercial loans	4,867,272	4,756,581	2.3
Other loans	24,194,643	21,852,593	10.7
Other credit	4,188,075	3,684,520	13.7
Finance leases	2,124,317	2,169,953	(2.1)
Overdrafts and sundry accounts	7,738,268	7,867,591	(1.6)
Doubtful loans	21,743,200	24,432,151	(11.0)
Accruals	(130,447)	(86,805)	50.3
Gross loans and advances to customers, excluding reverse repos	**121,140,837**	**124,614,933**	**(2.8)**
Reverse repos	587,597	688,010	(14.6)
Gross loans and advances to customers	**121,728,434**	**125,302,943**	**(2.9)**
Credit and country risk allowances	(10,892,711)	(12,374,053)	(12.0)
Loans and advances to customers (net)	**110,835,723**	**112,928,890**	**(1.9)**

The evolution of the Group's portfolio of problem assets improved in 2014. Quarter-on-quarter changes in these loans (doubtful assets plus real estate assets not covered by the Asset Protection Scheme) were as follows:

€ million

	2014				2013			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Net increase in ordinary doubtful exposure	(83)	(203)	(316)	(457)	388	760	365	(12) (*)
Change in real estate	64	148	202	263	394	1	218	400 (*)
Net increase in ordinary doubtful exposure and real estate	**(19)**	**(55)**	**(114)**	**(194)**	**782**	**761**	**583**	**388** (*)
Assets written off	265	97	224	298	247	305	105	51
Quarter-on-quarter movements in doubtful exposure and real estate	**(284)**	**(152)**	**(338)**	**(492)**	**535**	**456**	**478**	**337**

(*) These items relate to assets newly classified as doubtful/substandard, excluding businesses acquired in 2013.The net increase in ordinary exposure does not include exposure reclassified as doubtful during 2013 following the review of the criteria for reclassification of refinanced loans.

The decrease in doubtful assets was reflected in a loan loss ratio (not including assets covered by the Banco CAM Asset Protection Scheme) of 12.17% at the close of 2014, compared to 13.63% at the end of 2013 — a fall of 146 basis points. The provision coverage ratio for doubtful assets at 31 December 2014 was 50.3%, compared with 51.6% a year earlier.

The Bank's portfolio of fixed-income assets available for sale is held mainly to stabilise the net interest income at a stable level. The size of the portfolio was reduced in 2013 but remained largely stable in 2014. The composition of the portfolio according to asset class was as follows:

€million

Asset type	Fair value
Treasury bills	39
Government bonds	6,305
Bonds guaranteed by the State	975
Bonds issued by regional governments	1,492
Government securities of other countries	7,714
Securities issued by banks	702
Covered bonds	1,953
Asset-backed securities	31
Other debt instruments	1,183
Total	**20,393**

The breakdown of the available-for-sale portfolio by maturity was:

€million

Maturity	Fair value
1 year	843
5 years	3,642
10 years	10,017
Covered bonds	5,891
Total	**20,393**

The amortized cost of the portfolio was €18,853 million and it showed €1,259 million in net unrealized capital gains. Returns on the different types of asset ranged from 0.81% to 5.01% and the portfolio showed an average internal rate of return of 3.10%.

Customer funds increased overall by 4.1% year-on-year in 2014, mainly due to the steady rise in off-balance sheet funds, particularly in mutual funds managed and distributed by the group.

As of 31 December 2014, customer funds on the balance sheet amounted to €94,460.7 million, very similar to the figure at the end of 2013 (€94,497.2 million). Balances held in demand deposit accounts amounted to €43,275.0 million (up 17.4% year-on-year) while balances in time deposits amounted to €53,395.9 million, a 12.2% decline year-on-year that reflected the downward trend in interest rates in the financial markets, which drove investors to switch to more attractive investments in a search for better returns.

Total off-balance sheet customer funds amounted to €30,378.8 million, a 19.7% increase year-on-year. Within this item, the balance of assets in collective investment institutions rose steadily to reach €15,705.6 million at 31 December 2014, a 42.5% increase year-on-year, while the balance of assets under management amounted to €2,918.1 million (€1,927.6 million at 2013 year-end).

Debts represented by marketable securities amounted to €20,196.3 million at 2014 year-end, compared with €21,166.9 million as of 31 December 2013. This decline was due mainly to a net reduction in balances of asset-backed securities and mortgage covered bonds.

Total funds under management amounted to €152,185.4 million as of 31 December 2014, an increase of 2.1% with respect to the balance of €149,122.9 million as of 31 December 2013.

Thousand euro

	2014	2013	Change YoY (%)
On-balance sheet customer funds	**94,460,668**	**94,497,187**	**(0.0)**
Customer deposits	98,208,370	99,362,908	(1.2)
Current accounts	31,098,746	26,260,652	18.4
Savings accounts	12,176,217	10,601,835	14.9
Time deposits	53,395,928	60,798,681	(12.2)
Repurchase agreements	1,291,799	1,347,184	(4.1)
Accruals	447,697	611,168	(26.7)
Adjustments due to hedging derivatives	(202,017)	(256,612)	(21.3)
Debt represented by marketable securities	20,196,329	21,166,915	(4.6)
Subordinated liabilities	1,012,362	1,089,046	(7.0)
Liabilities under insurance contracts	2,389,571	2,134,139	12.0
On-balance sheet funds	**121,806,632**	**123,753,008**	**(1.6)**
Mutual funds	15,705,612	11,018,570	42.5
Equity funds	953,518	584,740	63.1
Balanced funds	1,695,488	866,585	95.7
Fixed-income funds	3,829,651	2,474,177	54.8
Guaranteed return funds	3,793,940	2,788,376	36.1
Real estate funds	9,225	44,364	(79.2)
Investment entities (SICAVs)	1,725,078	1,420,342	21.5
Mutual funds	3,698,712	2,839,986	30.2
Wealth management	2,918,071	1,927,634	51.4
Pension funds	4,334,615	4,356,291	(0.5)
Individual	2,861,552	2,857,495	0.1
Company	1,456,994	1,478,333	(1.4)
Group	16,069	20,463	(21.5)
Third-party insurance products	7,420,511	8,067,355	(8.0)
Funds under management	**152,185,441**	**149,122,858**	**2.1**

Income and profit performance

Thousand euro

	2014	2013 (***)	Change YoY (%)
Interest and similar income	4,513,497	4,863,170	(7.2)
Interest and similar charges	(2,253,791)	(3,048,476)	(26.1)
Net interest income	**2,259,706**	**1,814,694**	**24.5**
Returns on equity instruments	8,628	7,329	17.7
Share of profit/(loss) of equity-accounted entities	101	11,107	(99.1)
Net fees and commissions	860,891	759,670	13.3
Income from trading (net)	1,763,604	1,479,185	19.2
Exchange differences (net)	99,556	67,871	46.7
Other operating income/expense	(191,960)	(308,658)	(37.8)
Gross income	**4,800,526**	**3,831,198**	**25.3**
Personnel expenses	(1,202,604)	(1,135,175)	5.9
Recurring (*)	(1,169,295)	(1,090,620)	7.2
Non-recurring	(33,309)	(44,555)	(25.2)
Other general administrative expenses	(570,714)	(587,886)	(2.9)
Recurring (**)	(563,849)	(581,086)	(3.0)
Non-recurring	(6,865)	(6,800)	1.0
Depreciation and amortization	(278,104)	(228,447)	21.7
Profit before impairment and other provisions	**2,749,104**	**1,879,690**	**46.3**
Provisions for loan loss and other impairments	(2,499,659)	(1,768,998)	41.3
Profit on disposal of assets	236,948	43,893	439.8
Negative goodwill	0	30,295	(100.0)
Profit/(loss) from discontinued operations	0	0	--
Profit/(loss) before tax	**486,393**	**184,880**	**163.1**
Corporate income tax	(109,748)	(17,962)	--
Consolidated profit/(loss) for the year	**376,645**	**166,918**	**125.6**
Profit/(loss) attributed to non-controlling interests	4,968	21,003	(76.3)
Income attributed to the group	**371,677**	**145,915**	**154.7**
Memorandum item:			
Average total assets	163,372,812	166,571,462	(1.9)
Earnings per share (€)	0.09	0.04	153.9
Diluted earnings per share			

(*) Recurring personnel expenses, on a like-for-like basis, were 1.2% lower than in the previous year.

(**) Recurring administrative expenses, on a like-for-like basis, were down 10.5% on the previous year.

(***) Restated to show the impact of early adoption of IFRIC21. These adjusted data are presented solely for comparative purposes.

Banco Sabadell and its group ended 2014 with a net attributable profit of €371.7 million after booking €2,499.7 million in allowances for bad debts, securities and real estate assets.

Net interest income totalled €2,259.7 million in 2014, rising by 24.5% on the previous year's figure, with the ratio of net interest income to average total assets and the interest margin both increasing significantly. This upward trend was already observable in the second quarter of 2013 and resulted mainly from the reduction in funding costs.

In terms of overall annual averages, the net interest margin for the year was 1.38%, 29 basis points higher than the figure for the previous year (1.09%). The higher average return on average total assets was the result of several factors, including the rise in interest spreads (due mainly to the lower cost of customer deposits), lower capital market funding costs, the reduction in problem assets and the improved profitability of recent acquisitions.

Thousand euro

	2014			2013			Change		Effect	
	Average balance	Income/ (expense)	Rate (%)	Average balance	Income/ (expense)	Rate (%)	Average balance	Income/ (expense)	Volume	Rate
Cash. central banks and other credit institutions	4,259,117	40,099	0.94	4,529,883	40,794	0.90	(270,766)	(695)	(2,438)	1,743
Loans and advances to customers	106,441,489	3,640,970	3.42	105,997,323	3,859,745	3.64	444,166	(218,775)	16,174	(234,950)
Fixed-income portfolio	22,703,810	806,852	3.55	28,629,589	938,309	3.28	(5,925,779)	(131,457)	(194,212)	62,755
Subtotal	**133,404,416**	**4,487,921**	**3.36**	**139,156,795**	**4,838,849**	**3.48**	**(5,752,379)**	**(350,928)**	**(180,476)**	**(170,452)**
Equity portfolio	1,325,403	-	-	1,961,883	-	-	(636,480)	-	-	-
Tangible and intangible assets	3,761,914	-	-	3,246,609	-	-	515,305	-	-	-
Other assets	24,881,079	25,576	0.10	22,206,175	24,322	0.11	2,674,904	1,254	-	1,255
Total capital employed	**163,372,812**	**4,513,497**	**2.76**	**166,571,462**	**4,863,170**	**2.92**	**(3,198,650)**	**(349,673)**	**(180,476)**	**(169,197)**
Credit institutions	13,234,024	(194,307)	(1.47)	25,838,912	(298,066)	(1.15)	(12,604,888)	103,759	145,405	(41,645)
Deposits from other creditors	93,079,509	(1,107,189)	(1.19)	84,303,805	(1,627,350)	(1.93)	8,775,704	520,161	(169,401)	689,560
Capital markets	26,901,563	(908,505)	(3.38)	29,654,453	(1,038,410)	(3.50)	(2,752,890)	129,905	96,398	33,507
Repurchase agreements	8,597,642	(49,179)	(0.57)	6,732,891	(70,657)	(1.05)	1,864,751	21,478	(19,569)	41,047
Subtotal	**141,812,738**	**(2,259,180)**	**(1.59)**	**146,530,061**	**(3,034,483)**	**(2.07)**	**(4,717,323)**	**775,303**	**52,833**	**722,469**
Other liabilities	10,785,387	5,389	0.05	10,855,651	(13,993)	(0.13)	(70,264)	19,382	-	19,384
Shareholders' equity	10,774,687	-	-	9,185,750	-	-	1,588,937	-	-	-
Total funds	**163,372,812**	**(2,253,791)**	**(1.38)**	**166,571,462**	**(3,048,476)**	**(1.83)**	**(3,198,650)**	**794,685**	**52,833**	**741,853**
Average Total Assets	**163,372,812**	**2,259,706**	**1.38**	**166,571,462**	**1,814,694**	**1.09**	**(3,198,650)**	**445,012**	**(127,643)**	**572,656**

Net interest margins began to widen in the second quarter of 2013 and this rising trend continued to be seen in each of the following quarters, in both absolute and relative terms. Net interest income rose to 1.49% of average total assets in the fourth quarter of 2014 (compared with 1.17% in the fourth quarter of 2013).

Dividends received and income from equity-accounted undertakings together amounted to €8.7 million against €18.4 million in 2013, a decline of €9.7 million. The reduction was due to the fact that the number for 2013 included a €14.6 million contribution from Centro Financiero BHD which was sold in December 2013.

Net fees and commissions totalled €860.9 million, a 13.3% increase year-on-year. Increases were recorded across all categories of fee and commission income (generated on loan and guarantee risks, services, mutual funds, and the distribution of insurance and pension products) and were mainly attributable to a good performance by off-balance sheet funds, promotional actions to increase profitability and the incorporation into the group of businesses acquired in 2013.

Fees and commissions chargeable on loans and guarantees increased by €7.0 million overall, largely thanks to increased business volumes. Fees for services increased by €34.4 million, with a strong performance being shown in the securities, credit/debit card and current and demand deposit account categories, again driven by the growth in business volumes and the inclusion of new businesses in the consolidated group accounts. Fees and commissions related to mutual funds, insurance and pensions showed an increase of €66.8 million on the previous year, attributable primarily to the growth of assets held in collective investment schemes (CIS's) sold by the group or under its management.

Net income from trading totalled €1,763.6 million, including €1,860.7 million in capital gains on the sale of available-for-sale fixed-income assets. In 2013 net income from trading was €1,479.2 million, including gains of €927.8 million on the sale of available-for-sale fixed-income assets, €437.3 million on the sale of held-to-maturity investments, €58.8 million on the sale of equity securities, and €53.6 million in income from the trading portfolio.

Net gains due to foreign exchange differences totalled €99.6 million, a considerable increase with respect to 2013 (€67.9 million). This 46.7% year-on-year increase was due mainly to a higher volume of transactions in 2014 and to a number of currency deals that resulted in positive gains.

Other operating income and expenses showed a negative balance of €192.0 million. A major component of this item consisted of contributions to the bank deposit guarantee fund amounting to €158.4 million.

Operating expenses (personnel and general) for 2014 totalled €1,773.3 million, of which €40.2 million were non-recurring in character (consisting essentially of redundancy payments to employees); in 2013, operating expenses amounted to €1,723.1 million and included €51.4 million in non-recurring expenses (comprising mainly restructuring costs on the acquisition of Banco Gallego). On a strictly comparable basis, however, operating expenses for 2014 shrank by 4.4% overall compared with 2013 (personnel expenses fell by 1.2% and general expenses were reduced by 10.5%).

The increase in gross income in 2014 combined with the policies to hold down operating expenses resulted in an improved cost: income ratio which at the end of the year stood at 53.14%, down from 64.19% at the end of 2013 (the figures for both years excluded non-recurrent income from trading and net foreign exchange gains, in accordance with the revised procedure introduced in 2014 and applied also to 2013).

The profit and loss account explained before resulted in a profit before impairment and other allowances of €2,749.1 million. Allowances for impairment and other losses (on real estate and financial assets, for the most part) were €2,499.7 million. Capital gains on asset disposals amounted to €236.9 million and were made up largely of a €162 million gross capital gain on the sale of the group's debt management and recovery business and an exceptional payment of €80 million (net of formalization expenses) on the signature of a reinsurance treaty in respect of the Mediterráneo Vida portfolio of individual life and permanent disability policies. In 2013, capital gains on asset disposals amounted to €43.9 million, including net gains of €25.6 million in December 2013 from the sale of Banco Sabadell's stake in Centro Financiero BHD.

The group’s income statement for 2013 included a badwil of €30.3 million, mainly attributable to the acquisition of Banco Gallego.

After deducting income tax and the share of profit attributed to non-controlling interests, the year-end profit attributed to the group for 2014 was €371.7 million.

2.4.Business review

The main financial highlights associated with the group's main business units are set out below, in accordance with the segment reporting procedures described in note 36 to these consolidated annual accounts.

Commercial Banking

Thousand euro

	2014	2013	YoY change (%)
Net interest income	**1,778,469**	**1,353,679**	**31.4**
Net fees	636,270	576,411	10.4
Other income	(76,970)	(51,732)	48.8
Gross income	**2,337,769**	**1,878,358**	**24.5**
Operating expense	(1,345,734)	(1,258,142)	7.0
Net operating income	**992,035**	**620,216**	**59.9**
Impairment losses	(644,154)	(325,014)	98.2
Profit/(loss) before taxes	**347,881**	**295,202**	**17.8**
Ratios (%):			
ROE	8.0%	7.0%	
Cost/income ratio	57.6%	67.0%	
Loan loss ratio	10.3%	11.4%	
Coverage ratio	52.4%	52.5%	
Customer balances (million euro)			
Loans and receivables	79,853	81,956	(2.6)
Deposits	90,785	88,130	3.0
Securities deposited	8,678	8,424	3.0
Other data			
Employees	12,562	13,225	(5.0)
Domestic branches	2,253	2,356	(4.4)

The group's largest business line is Commercial Banking, which provides a range of financial products and services for large and medium-sized companies, SMEs, businesses and individuals (including private banking, personal banking and mass market customers), non-residents and professional groups, with a degree of specialization that provides customers with personalized attention depending on their needs, whether from experts throughout its multi-brand branch network or via other channels to support the customer relationship and give access to remote banking services.

The operating environment showed signs of recovery in 2014 and the Bank's sales initiatives helped to reduce loan defaults, drive up net interest income, build stronger customer relationships, give a major boost to the insurance business and achieve strong growth in mutual funds. From this perspective, business performance was positive in both the business and individual customer segments.

The integration of the Spanish branch networks of Banco Gallego and Lloyds International Bank was completed in the first quarter of 2014, significantly expanding Banco Sabadell's presence in Galicia and in the foreign resident customer segment.

Net interest income attributable to Commercial Banking amounted to €1,778.4 million in 2014, while profit before tax totalled €347.8 million. The ROE was 8.0% and the cost/income ratio was 57.6%. Loans and advances to customers amounted to €79,853 million and assets under management were €90,785 million.

Corporate Banking and Global Businesses

Corporate Banking and Global Businesses offers financial solutions and advisory services to large companies and financial institutions, both Spanish and foreign, with branches throughout Spain and in 14 other countries. Its activities encompass corporate banking, structured finance, corporate finance, development capital, international trade and consumer finance.

Corporate Banking

During 2014 the group completed a strengthening of its Corporate Banking organization that began in 2013.

Thousand euro

	2014	2013	YoY change (%)
Net interest income	**162,499**	**161,797**	**0.4**
Net fees	24,942	27,962	(10.8)
Other income	11,439	9,154	25.0
Gross income	**198,880**	**198,913**	**(0.0)**
Operating expense	(26,596)	(26,274)	1.2
Net operating income	**172,284**	**172,639**	**(0.2)**
Impairment losses	(102,236)	(90,784)	12.6
Other results			-
Profit/(loss) before taxes	**70,048**	**81,855**	**(14.4)**
Ratios (%):			
ROE	7.1%	8.0%	
Cost/income ratio	13.4%	13.2%	
Loan loss ratio	2.5%	2.5%	
Coverage ratio	58.0%	58.0%	
Customer balances (million euro)			
Loans and receivables	10,820	11,455	(5.5)
Deposits	5,177	4,366	18.6
Securities deposited	662	593	11.6
Other data			
Employees	113	110	2.7
Domestic branches	2	2	0.0
Foreign branches	3	3	0.0

A key feature of the new organizational model is the creation of teams of "global bankers" specializing in individual business sectors and establishing a direct presence in customers' target markets, thus ensuring that Corporate Banking's large corporate customers will benefit from the best possible banking experience. The model is based on a strategic relationship of closeness to its customers so as to offer comprehensive solutions tailored to the operational needs of each company and market. Standards of efficiency and service of the highest order and speedier day-to-day middle office processes are other key elements of the model.

From a strictly business standpoint, the focus remains on strengthening relations with customers in Spain and other countries and promoting fee-earning businesses that consume less capital, while maintaining a rigorous approach to the granting and renewing of loans.

Net interest income attributable to Corporate Banking in 2014 amounted to €162.5 million while profit before tax totalled €70 million. The ROE ratio was 7.1% and the cost/income ratio was 13.4%.

Private Banking

Thousand euro

	2014	2013	YoY change (%)
Net interest income	**16,601**	**10,549**	**57.4**
Net fees	45,456	37,971	19.7
Other income	3,248	3,318	(2.1)
Gross income	**65,305**	**51,838**	**26.0**
Operating expense	(36,626)	(36,034)	1.6
Net operating income	**28,679**	**15,804**	**81.5**
Provisions (net)	0	0	-
Impairment losses	995	(1,926)	(151.7)
Other results	0	0	-
Profit/(loss) before taxes	**29,674**	**13,878**	**113.8**
Ratios (%):			
ROE	59.3%	29.1%	
Cost/income ratio	56.1%	69.5%	
Loan loss ratio	3.4%	3.9%	
Coverage ratio	58.7%	56.7%	
Customer balances (million euro)			
Loans and receivables	1,029	1,053	(2.3)
Deposits	16,896	15,513	8.9
Securities deposited	7,326	7,007	4.6
Other data			
Employees	271	269	0.7
Domestic branches	12	12	0.0

In 2014 efforts continued to enhance recognition of SabadellUrquijo Private Banking as a leading banker to high net worth individuals, addressing the needs of customers who demand products and services to suit their risk profiles and ceaselessly striving to maximize their investment returns.

The sales team worked diligently to increase personal contact with customers by making more frequent visits and follow-up calls to ensure that customers felt well served. Even greater efforts were directed at new customers acquired as a result of recent acquisitions.

A significant change in the balance sheet was seen in the composition of customer funds under management, where mutual funds, discretionary portfolio management services and SICAVs gained prominence at the expense of more liquid assets with less attractive returns, such as term deposits and commercial papers, for which there was less demand from investors.

This change in the composition of clients' investment portfolios resulted in an increase in profitability for Private Banking.

Net interest income amounted to €65.3 million in 2014, while the profit before tax was €29.6 million. The ROE was 59.3%, and the cost/income ratio was 56.1%. Total customer funds under management amounted to €24,222 million.

Investment Management

Thousand euro

	2014	2013	YoY change (%)
Gross income	**42,448**	**29,015**	**46**
Operating expense	(20,546)	(20,191)	2
Net operating income	**21,902**	**8,824**	**148**
Other results	-	(13)	(100)
Profit/(loss) before taxes	**21,902**	**8,811**	**149**
Ratios (%):			
ROE	59.9%	29.0%	
Cost/income ratio	48.4%	69.6%	
Customer balances (million euro)			
Assets under management in CISs	12,007	8,070	48.8
Total assets including mutual funds sold but not managed	15,706	10,193	54.1
Other data			
Employees	145	147	(1.4)
Domestic branches	-	-	

Banco Sabadell's team of highly qualified experts specializes in financial market research and analysis and in drawing up asset allocation strategies to guide investment decisions; this includes the planning and development of investment products and a mandate to research any of the various types of asset in which customers might wish to invest.

The group's Investment Management business encompasses collective investment management companies, including investment management and the distribution and administration of collective investment vehicles (UCITS), as well as selecting, offering and recommending third-party funds and managing the investments of the Banco Sabadell group's other businesses.

Following the integration of Banco Gallego and Lloyds España in the first quarter of 2014, the Banco Sabadell group's investment management companies ended the year with €9,952.6 million of assets under management in Spanish-domiciled mutual funds, 59.1% more than at 2013 year-end, a growth rate far in excess of that registered by the industry as a whole. This volume of assets under management brought the group's share of the mutual fund market to over 5%, with its management company, Sabadell Inversión, being ranked fourth largest manager of Spanish-domiciled mutual funds.

Investors continued to prefer balanced funds in 2014 and assets in this category increased by a factor of 2.4 to €1,573.6 million. Guaranteed funds continued to be offered throughout the year, with return guarantees being issued for eight guaranteed funds amounting to €1,492.8 million at 31 December 2014. Assets in guaranteed funds totalled €3,765.7 million. Variable-yield guaranteed funds expanded to account for 23.0% of total Spanish-domiciled funds under management in 2014, compared with 17.8% in 2013. However, guaranteed funds declined as a proportion of the total, from 44.4% in 2013 to 37.8% in 2014.

Real Estate Asset Transformation

Thousand euro

	2014	2013	YoY change (%)
Net interest income	**(11,192)**	**42,085**	**(126.6)**
Net fees	(659)	(2,826)	(76.7)
Other income	15,228	(6,972)	(318.4)
Gross income	**3,377**	**32,287**	**(89.5)**
Operating expense	(135,824)	(193,726)	(29.9)
Net operating income	**(132,447)**	**(161,439)**	**(18.0)**
Provisions (net)	(1,469)	(301)	388.0
Impairment losses	(143,512)	(362,215)	(60.4)
Other results	(720,044)	(520,861)	38.2
Profit/(loss) before taxes	**(997,472)**	**(1,044,816)**	**(4.5)**
Ratios (%):			
ROE	(39.3)%	(39.9)%	
Cost/income ratio	--	--	
Loan loss ratio	61.9 %	56.0 %	
Coverage ratio	49.8 %	50.8 %	
Customer balances (million euro)			
Loans and receivables	14,989	18,894	(20.7)
Deposits	484	466	3.9
Real-estate assets (gross)	14,601	12,361	18.1
Other data			
Employees	668	807	(17.2)
Domestic branches	--	--	

The Asset Transformation Department manages the group's real estate exposure and non-performing exposures; specifically, it is charged with transforming and maximizing the value of these exposures. The department's structure and organization ensure that it has a broad view of management processes and can design and implement a transformation strategy to maximize the values of assets and/or remove them from the balance sheet as soon as possible.

With regard to non-performing exposures, early warning mechanisms have been established and business tools and solutions have been implemented to manage loan delinquency. Real estate exposures have been brought within a single comprehensive management process covering all stages from analysis and preventive action on loans secured on real estate through to direct action on foreclosed assets. This end-to-end approach has enabled us to work with our customers to find solutions that meet their real estate needs.

The Group's real estate unit Solvia, which was spun off in 2014, provides a range of real estate management services for the Group and third parties, from land and property development through to asset servicing and property sales, thus providing a unified service covering all aspects of the real estate business. In the provision of real estate services for portfolios of real estate assets (Bank's own-use or acquired through foreclosures, and third party-owned), personnel and processes were strengthened and Solvia now has one of the best real estate platforms in the marketplace, as was clearly seen when Sareb awarded it the contract for the management of a portfolio of 42,900 properties, citing Solvia's real estate expertise and management capabilities.

3. THE ENVIRONMENT

Environmental sustainability

We care about the future and about sustainability. This is why Banco Sabadell has an environmental policy in place, is a signatory to the main international covenants on the environment and promotes a commitment to the environment globally.

Environmental policy

- Minimize the potential environmental impacts of processes, facilities and services.
- Effectively manage the environmental risks and opportunities inherent in the business.
- Promote a global commitment to the environment

Global covenants and alliances

- A signatory of the United Nations Global Compact: in taking this step we are committing ourselves to adopting a preventive approach to environmental protection, promoting initiatives to foster environmental responsibility and supporting the development of technologies that do not harm the environment.
- A signatory of the Carbon Disclosure Project (CDP) and CDP Water Disclosure: a commitment to actively combat climate change and publish an annual inventory of corporate emissions.
- A signatory of the Equator Principles: to ensure that social and environmental risks are taken account of in the funding of large projects.
- A signatory of the United Nations Principles for Responsible Investment in the "investment manager" category: inclusion of environmental, social and governance criteria in investment policies and practices.
- A collaborating partner of the Spanish Association of Renewable Energy Producers and a member of the Spanish Wind Energy Association.
- Environmental management system certified to ISO 14001: 15% of our employees in Spain work in one of our six certified Central Service buildings. Our environmental management system has been adapted for the rest of the group.
- Certified to Gold level under LEED New Construction for sustainable buildings: certification was obtained for the service area of the group's main Central Service building in Sant Cugat del Vallès.
- A member of the European Commission's GreenBuilding Programme: Banco Sabadell is a partner in the GreenBuilding Programme for the sustainable construction of the group's logistics centre and general archive in Polinyà.

All departments of the organization have the financial resources they need to meet the group's aims and commitments on the environment. Due to the structure of the group and the nature of its business, these funds are not recognized under a specific line item to provide an overview of environment-related costs and investment.

No significant fines or other penalties were imposed on the group for non-compliance with environmental laws and regulations in 2014.

Key environmental action areas:

Renewable energy - finance and investment

Banco Sabadell promotes the development of sustainable energy through direct investment and as a provider of finance for renewable energy projects. As in previous years, the Bank shared its experience in the renewables sector and provided speakers at leading forums in Spain. These included events organized by the Spanish Wind Energy Association and the Association of Renewable Energy Producers.

In 2014 Banco Sabadell provided €141 million in finance for renewable energy generation projects, mainly in the US. Renewable energy installations financed by the Bank under project finance deals amount to a total attributable capacity of 161 MW, mostly wind farms.

In addition to finance, Banco Sabadell provides advisory and brokerage services for renewable energy projects.

The Bank makes direct investments in the equity capital of renewable energy generation projects. Most of this business is carried on through Sinia Renovables, a wholly-owned subsidiary.

The Equator Principles

Banco Sabadell adopted the Equator Principles in September 2011. Based on the policies, standards and guidelines of the International Finance Corporation (IFC), the Principles apply to structured finance projects and corporate loans. Under the latest version of the Equator Principles (EPIII), in 2014 the requirement to carry out environmental and social impact assessments was extended to decisions on corporate loans.

Environmental management and climate change

The Bank's Environment Committee is charged with overseeing compliance with group environmental policy and reviewing group performance in environmental matters. The group has an environmental management system which was set up in 2006 according to the ISO 14001:2004 standard. Currently 15% of the group's employees in Spain work in one of the six office buildings that have been certified to that standard. The environmental management system has been adapted for use at all other group facilities in Spain.

Year after year Banco Sabadell works to improve the eco-efficiency of its facilities and reduce the environmental impacts of the services it provides to customers. Some of the measures it has taken to reduce consumption and emissions are as follows:

- *Inventory of CO_2 emissions*: In 2009 the Bank compiled an independently verified inventory of corporate CO_2 emissions and set a reduction target of 3% for the period 2009-2013. During this period a reduction in emissions of 77% has been achieved, mainly by purchasing electrical power generated from renewable sources.

- Power consumption: overall consumption of electrical power in Spain in 2014 increased to 104,419 MWh from 102,991 MWh in 2013. Despite new undertakings being integrated into the group during the year 2014, the increase in power consumption was not significant (1%) owing to the energy efficiency measures being implemented. These measures to reduce power consumption included the following:

    - 79% of group branches are equipped with centralized lighting and climate control systems. Lighting systems fitted with LED lamps and presence detectors in some areas of Central Service buildings.
    - Widespread use of low-energy lamps and billboard lighting systems fitted with daylight switching systems.
    - Energy recovery climate control systems are installed in Central Service buildings and larger branches.
    - Branches are using Thin Client hardware which consumes 90% less energy than conventional PCs. In 2014 a pilot programme was launched to install Thin Client technology at Central Service buildings.

- Paper consumption: Reduce, reuse and recycle. Paper consumption by the group in Spain in 2014 was 1,039 tons (up from 939 tons in 2013). The increase was due to the addition of new businesses to the group and the rise in customer numbers. At the same time, the main actions put in hand to reduce paper consumption were as follows:
    - Banking services are available to customers 24 hours a day via remote access channels, ATMs, telephone banking, email or social media. Customers can access 100% of their correspondence with the Bank electronically.
    - Branches are equipped with digital tablets for customers' signatures. In 2014 this made it possible for 29 million printed forms to be eliminated. There are plans to process more transactions via tablets in the future and progressively eliminate the use of paper.
    - Conventional paper is chlorine-free, certified by the FSC and produced to ISO 9001 and ISO 14001 standards; all of the group's printers are configured for duplex printing by default.

- Water usage: Water consumption is limited to sanitary uses and to some watering of gardens. In

2014 the group's water consumption resulted in costs of €1.1 million (€0.9 million in 2013). With regard to waste water management, all our facilities and offices are connected to the public sewage network. Toilet cisterns and taps are fitted with water-saving mechanisms. The main group Central Service building has a cistern for collecting rainwater and greywater for watering plants. Landscaped areas have been planted with autochthonous drought-resistant plants.

- Waste management: In 2014 the group generated 883 tons of waste paper and card, up from 594 tons in 2013. In all group premises, used paper is treated as confidential waste for shredding and 100% is recycled through authorized waste managers. All Central Service buildings have facilities for the separation and collection of packaging, organic matter and batteries). Banco Sabadell works with Ricoh and the HP Planet Partners programme to manage the collection and reuse of toner cartridges and disposes of computer waste through authorized waste managers. There are specific oversight mechanisms for managing waste at branches that are in the process of closing or being merged.

Environmental training and awareness

All group employees have access to an on-line training course which is obligatory for staff at Central Service facilities. Additionally, an on-line guide, “Connect with the Environment”, gives employees ready access to information about the corporate environmental footprint, resource consumption and waste management at their branch or Central Services facility. The Bank's employees have the use of a car sharing platform, "BS Carpooling", which gives them the option of sharing a car to get to and from work. Employees at the main group Central Service building who make use of the platform are entitled to a reserved parking space. Features and articles about the environment are published in the staff newsletter, which is now available in digital format.

Banco Sabadell also keeps all its suppliers informed on the group’s environmental policy and incorporates environmental and social responsibility into its supply chain in a number of ways. In the group-level procurement process, tenders or offers from suppliers with ISO 9001, ISO 14001/EMAS or EFQM certification are looked on favourably. Consideration is given to the environmental qualities (recycled, ecological, good for the environment, etc.) of the products offered. Banco Sabadell's basic contract with suppliers includes specific clauses on compliance with environmental criteria, human rights and the Ten Principles of the United Nations Global Compact, as well as acceptance of the Supplier Code of Conduct. In particular, environmental requirements are included in specifications for products and services that have significant environmental impacts.

4. HUMAN RESOURCES

Human Resources aims to support the transformation of the organization through a people agenda that is an integral part of its day-to-day business operations and its growth. Its key objective is to maximize the value-creating potential of Banco Sabadell’s highly skilled workforce by developing their talent, managing their expectations and fully leveraging their capabilities.

Talent management and human capital form an essential component of the new “Triple” strategic business plan along with other key action areas of the plan.

The people agenda developed as part of the Triple plan includes drivers of organizational change and development as well as a wide-ranging and completely updated view of the Human Resources function.

In the area of organizational change and development, three strategic priorities have been identified: comprehensive talent management (strengthening leadership and fostering a culture in which talent is planned for and nurtured) to meet the needs generated by growth; raising the bar on employee performance (a universal model for today’s businesses that allows people performance to be actively managed); and involving and engaging all employees in the Group's development.

Key human resources data

No. of employees

	2014	2013
Equivalent average workforce	17,760	16,427
Domestic workforce at year-end	16,593	17,171
Workforce at year-end	17,529	18,077
Turnover (%) (*)	0.60%	0.27%
Absenteeism (%) (**)	2.17%	2.11%
Employee satisfaction index (%) (***)	--	66%
Hours of training per employee	33.62	25.55

The average number of employees has been calculated from the average number of employees at the end of each month.

(*) Undesired turnover: number of cases of sick leave and voluntary leaves of absence/total workforce x 100.

(**) Seriousness index (days lost/total working days x 100).

(***) 66% of employees responded to the final question in the 2013 employee satisfaction survey that "All things considerd, I would say it is an excellent place to work". No employee satisfaction survey was conducted in 2014. A survey will be conducted in 2015.

No. of employees

	Men	Women	Total
Spanish workforce	8,373	8,220	16,593
International workforce	375	561	936
Breakdown by gender (%) (*)	49.9%	50.1%	100%
Average age (*)	44.88	41.26	43.1
Average length of service (*)	19.22	15.21	17.21

(*) Figures calculated for the group's total workforce.

No. of employees

	Men	Women	Total
Clerical staff	971	1,694	2,665
Technical staff	7,390	7,009	14,399
Management	387	78	465
Total	**8,748**	**8,781**	**17,529**

Figures calculated for the group's total workforce.

At 2014 year-end, the categories have been changed to Clerical staff, Technical staff and Management.

Human resources management - policies and principles

- Human resources policy is grounded in respect for human dignity, fair and competitive remuneration, transparency and truthfulness in reporting, and lasting cooperation.

Recruitment policy

In line with its human resources policy, Banco Sabadell has a personnel selection process which ensures that objective criteria are applied in finding the right person for each job and career path. The group seeks to ensure optimal professional development for its employees by encouraging them to excel and rewarding hard work. This mutual commitment is set out in the Banco Sabadell Group Code of Conduct.

In 2014 the Bank worked on a number of initiatives to strengthen and adapt its procedures for recruiting and attracting talent.

Banco Sabadell is not only competing in an ever more global, dynamic and competitive environment, but is also currently undergoing a major programme of transformation, expansion and internationalization, for whose success having the best talent is critical.

Attracting, selecting and recruiting staff are a part of this new environment: a higher intake of new employees, new job profiles, and geographic dispersion are making it necessary to redesign and update the procedures, skills, technologies and capabilities used to attract the best candidates and provide them with a professionally rewarding experience.

To meet this need the Group launched its Talent Graduate Programme, a scheme designed for recent graduates to give employment to well-qualified young people with high potential, both locally and internationally, and prepare them to perform roles in the Bank's functional and business areas.

The Programme, in alignment with the Group's corporate social responsibility policy, aims to create jobs in an age bracket that has suffered particularly severely from unemployment in Spain, and many of whose members are still searching for their first job.

Equality, work-life balance and integration

Banco Sabadell guarantees equal opportunities in all aspects of its relations with employees — recruitment, training, promotion, working conditions, remuneration, etc. These principles are also set out in the Group's Equality Plan, human resources policy and Code of Conduct.

Equality

In 2010, Banco Sabadell adopted an Equality Plan aimed at avoiding all types of employment discrimination between women and men in the company, as required by Organic Law 3/2007. Certain lines of action were established for this purpose, including effective tracking and goal evaluation systems covering training, promotion and career development, remuneration, work-life balance, gender violence and sexual harassment. The Equality Plan's steering committee, which consists of employee and Bank representatives, meets twice per year to monitor progress and compliance with the Plan.

	2014	2013
% of promoted employees who are women	56%	55%
% of managerial positions held by women (*)	17%	15%

Figures calculated for the group's total workforce.

(*) At 2014 year-end, the categories have been changed to Clerical staff, Technical staff and Management.

Diversity and integration

Banco Sabadell promotes employee diversity and integration in the workplace and non-discriminatory recruitment processes. The Group takes action to adapt workplaces wherever necessary according to special sensitivity protocols established by the industrial medicine unit. The Bank also assists employees with paperwork in their dealings with municipal, regional and national governments, thus helping to improve employees' well-being outside the strictly professional sphere. In compliance with Spain's Integration of People with Disabilities Act ("LISMI"), the Bank pursues other measures such as buying services and supplies from special employment centres. In 2014 the Group had 156 employees with some form of disability (170 at the end of 2013).

Disability is not the only diversity issue that the Bank handles in a special way. Talent in women employees receives special attention given the important contribution it can make to the Bank's current and future development. In recognition of this, Banco Sabadell signed an agreement with the Ministry of Health, Social Services and Equality in 2014 to actively ensure equality and to recognize and value women's merits and capabilities in its internal training, hiring and promotion processes.

The Group's aim of making the best use of multigenerational talent is an increasingly important policy area, given the changing age structure of its workforce.

Work-life balance

Group employees enjoy a series of benefits thanks to an agreement between the Bank and union representatives on ways of striking the right balance between work and personal and family life. All employees have been properly informed of these benefits and full details are available on the intranet and on the Bank's website.

Benefits include time off from work, paid or unpaid (e.g. to nurse an infant); unpaid leave (for maternity or to care for a relative); leave in special circumstances; paternity leave; and flexitime arrangements.

Compensation policy

Banco Sabadell's compensation policy is based on the principles of internal fairness, external competitiveness, transparency, differentiation, flexibility, simplicity, confidentiality and communication, as prescribed by the Group's human resources policy.

Compensation policy is based on the degree of responsibility attaching to the position and on each employee's professional development. This determines Group practice with regard to increases in both fixed and variable remuneration. In total, 74.2% of the workforce in Spain qualified for variable remuneration in 2014 (75.3% in 2013).

Other types of benefit are available to employees, including interest-free loans and grants to help with training or children's schooling.

Workplace hazards

Banco Sabadell has a policy of constantly striving to improve employees' health and working conditions.

As required by law, the Bank has a health and safety plan setting out policy measures in this area. Each year it publishes a report on health and safety initiatives which is available on the employee portal and the Group website.

An initial risk assessment is performed on each new workplace and also on workplaces that have undergone refurbishment or alterations. A follow-up assessment is performed at a later date to evaluate both individual workstations and common areas, as well as aspects such as temperature, relative humidity, lighting, etc. In 2014, 1,624 questionnaires on psycho-social risk were sent out, producing a 70% response rate.

All Banco Sabadell personnel and new employees receive information on workplace hazard prevention and are required to take an online course in health and safety at work. The training is supplemented by publications, such as ergonomics factsheets and equipment manuals, related to the specific hazards affecting bank employees.

Employee development

Training

Banco Sabadell provides employees with function-based training: continuous, progressive training adapted to each individual's position.

	2014	2013
Employees who received training (%)	98%	88%
Investment in training per employee (euro)	365.7	247.3

Figures for Spain.

The "Laude" programme, initiated in 2009, allows employees who undertake Bank in-house training schemes to be awarded academic qualifications by the University of Barcelona's Institute of Lifelong Learning (IL3), under the framework of the new European Educational Space. Four different qualifications may be obtained, depending on the employee's role. Qualifications awarded under the programme in 2014 were as follows: 145 Higher Diplomas in Banking Products and Services, 25 "Expert in Commercial Banking", 7 "Expert in Investment Advisory Services" and 7 "Expert in Bank Branch Management" qualifications. A total of 531 people have gained qualifications under the programme since its inception in 2009. The Bank has also reached agreements with a number of universities to provide places for student interns.

Leadership development

The Bank has a special Executive Management unit focused on developing senior management's leadership skills. Bank executives participating in the corporate development program underwent a psychometric evaluation and a 360° assessment which collected feedback from direct superiors, colleagues and subordinates. They also received specific strategic leadership training designed to enhance their leadership and team management skills.

In 2014, management appraisals were performed for all Group Central Services managers, the goal being to support them in their development in managerial roles and to have a better understanding of the aspirations, strengths and areas for improvement of each and every Central Services manager. A total of 1,275 interviews were conducted as part of the appraisal.

One of the main outcomes of this exercise has been the Corporate Management Programme, which is designed for new department heads and Central Services directors with subordinates working under them. The Programme is based on developing management and team-building skills, promoting joined-up management at Central Services divisions and improving familiarity with human resources policies as a way of managing professional development and promoting success-driven behaviours appropriate to each role. A total of 131 employees took this training in 2014, its fourth year.

One of the organization's main tools in managing people and focusing on results is the annual performance review and interview, where managers hold a mandatory one-to-one meeting with their direct reports, the goal being also to foster professional growth and build trust. During the interview the employee's performance during the year and their performance assessment, occupational goals and geographic mobility are discussed. To provide managers with leadership and coaching skills and tools, two key initiatives were launched last year by the professional development unit: workshops to develop the skills required to carry out these interviews, and online knowledge pills on the performance management process for employees joining the Bank as a result of recent mergers.

The Human Resources department also conducts development interviews to assess employees whose performance is outstanding or who may be underperforming and ascertain their motivations, concerns and interests in relation to professional development.

Communication, participation and the volunteer programme

Communication

Banco Sabadell has numerous channels of communication between the different levels of the organization to enhance internal communication and involve employees in the Bank's goals.

The "BS Idea" platform allows employees to propose improvements in any area of the organization. The platform is also an excellent communication channel by which employees can make queries and share experiences on products and processes. The ideas with the most votes and those which add the greatest value to the Bank are considered by the persons in charge of the processes concerned and by members of a Decision Committee, who together reach a decision on their implementation. The ideas with the most votes also receive a cash prize.

Participation

Banco Sabadell respects and guarantees employees' basic rights, including freedom of association and collective bargaining, enshrined in Spanish law. These principles are set out in its Code of Conduct and human resources policy.

Union representatives represent the entire workforce, not just union members; accordingly, labour agreements apply to all employees at the level at which the negotiation was conducted (industry, group, company, etc.). All employees are given one month's notice of significant changes. Union elections are held every four years. Banco Sabadell management meets periodically with the general secretaries of the various trade unions and the latter participate regularly in committees (National Health and Safety Committee, Equal Opportunities Committee, Training Committee and the Pension Plan Oversight Committee). Workplaces with more than 50 workers have a works council. Workplaces with between 6 and 10 workers may elect a union representative.

Since 2012 Banco Sabadell has been working on an assistance plan to offset redundancies resulting from the workforce restructuring that followed the integration of Banco CAM. The assistance plan concluded in 2014; it was based on two main programmes: helping the 1,250 employees who were made redundant to find other jobs, and revitalizing business activity in the areas most severely affected by the Banco CAM lay-offs.

The re-employment plan includes career counselling for affected employees and their spouses with a view to enhancing their employability. At the end of the plan, 70% of participants (317) had found a new employment opportunity.

The aim of the business revitalization plan was to restore employment levels, as far as possible, by supporting entrepreneurship and job creation in the areas most affected by restructuring. It includes an aid programme based on monetary contributions for newly-created jobs, finance on preferential terms, one year's rent-free use of office accommodation or business premises, and professional advice.

At the end of the revitalization plan, 705 new jobs had been created in the Levante region.

The outplacement programme organized by Banco Gallego (acquired by the Group in 2013), which was taken up by 37 former employees, resulted in a solution in 20 cases and continues to work on the other 17.

Volunteer programme

Social action and corporate volunteer programme initiatives are publicized on the employee portal under the Solidaris label. The successes achieved year after year led to a substantial increase in the number of volunteers and in the activities organized in 2014, all of which were aligned with Banco Sabadell's corporate social responsibility policy and many of which were proposed by the employees themselves.

The participation of 26 teams from the Bank in Oxfam Intermon's Trailwalker event is a perfect example. A total of 144 people represented Banco Sabadell in the 2014 event, making us the company with the largest number of employees taking part and raising more than €40,000 to be used for Oxfam's water management projects in the Sahara.

For the second year in a row, 105 volunteers from the Bank participated in workshops for fourth grade pupils as part of the Schools Financial Education Programme in Catalonia (EFEC). The collaboration agreement with Catalonia's regional government and the *Instituto de Estudios Financieros* covered 20% of schools in Catalonia in 2014.

Surveys

The Bank participates in the "Best workplaces" survey conducted by the Great Place to Work Institute, which covers over 5,000 employers and 1,500,000 employees in 32 countries around the globe. It is considered the leading survey for measuring employee satisfaction, and will be conducted again in 2015. In 2014 new initiatives were launched to listen to employees and enable them make their voices heard. A survey to measure the degree of employee commitment to the Bank's current and future business goals was conducted for the first time. This new form of participation was implemented in view of the high correlation between employee engagement and business performance.

International expansion

One of the key objectives of the “Triple” business plan is to prepare the Group’s organizational structures for future international expansion. In 2014 Human Resources completed its proposed arrangements for International HR management, including functional and governance requirements and roles and responsibilities for HR at corporate, regional and local level.

New international mobility policies were also defined, based on market benchmarks, with six distinct programmes being identified according to the purpose and duration of the secondment and the value provided by the employee.

A talent map of employees with potential for secondment abroad was completed and a roster of 347 employees willing to change locations was compiled.

5. LIQUIDITY AND CAPITAL RESOURCES

5.1 Liquidity

Banco Sabadell's liquidity management policy seeks to ensure that its lending can be financed at a reasonable cost and within a reasonable time so that liquidity risk is kept to a minimum. In recent years the Bank's funding policy has focused on generating a positive liquidity gap in the commercial business, reducing the total amount of funding obtained from the wholesale markets (€23,106 million at 2014 year-end) and increasing the Bank's liquidity position.

Principal sources of funding:

The Group's main source of funding is the customer deposit base (mainly demand deposits and time deposits captured through the branch network), together with funding from the interbank and capital markets, where the Bank has a number of short- and long-term funding programmes in place to assure a suitable diversity of products, maturities and investors. The Bank also holds a diversified portfolio of liquid assets, most of which are eligible as collateral in funding operations with the European Central Bank (ECB). At 31 December 2014, the effective value of the Group’s liquid assets stood at €18,827 million (€18,468 million at 31 December 2013). Banco Sabadell participated in the ECB's 3-year liquidity auctions on 22 December 2011 and 1 March 2012, receiving an overall total of €23,650 million. These borrowings were gradually repaid in 2013 and the balance stood at €8,800 million at 31 December 2013; this was repaid in full in July 2014. The Bank also participated in the ECB's 4-year TLTRO liquidity auction on 17 December 2014, obtaining €5,500 million, close to the maximum amount permitted by the Bank’s balance sheet position. At 31 December 2014, Banco Sabadell held €7,200 million in borrowings from the ECB.

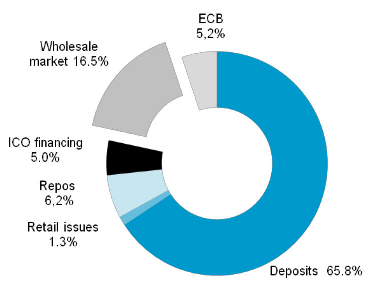
The Group's principal sources of funding at the end of the years 2014 and 2013 are shown in the following table according to the accounting item under which they are recorded:

€million

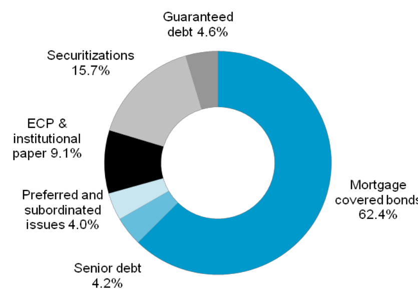
	2014	2013
Deposits from other creditors	98,208	99,363
Deposits with central banks and credit institutions	23,490	23,085
Marketable debt securities and subordinated liabilities	21,209	22,256
Total	**142,907**	**144,704**

The composition of the Group's funding in 2014 according to the type of instrument and counterparty, is further analysed below:

Funding structure



Wholesale market



On-balance sheet customer funds

At 31 December 2014 customer funds on the balance sheet amounted to €94,461 million, compared with €94,497 million at 2013 year-end and €80,179 million at 2012 year-end. There was a sharp 17.9% increase in 2013 over 2012, due mainly to acquisitions: that of Banco Gallego in October 2013, and those of Lloyds Bank's Spanish subsidiary and Banco Mare Nostrum's branch network in Catalonia and Aragón in June. There was a shift from time deposits to demand deposits in 2014 due to lower interest rates. At 31 December 2014 demand deposits (which includes current and savings accounts) had increased to €43,275 million (up 17.4%) at the expense of time deposits, which shrank by 12.2%.

Customer funds by maturity:

€million

	2014	3 months	6 months	12 months	More than 12	No fixed maturity
Total customer funds	**94,461**	**10.7%**	**11.6%**	**19.0%**	**12.7%**	**46.0%**
Time deposits	48,639	20.0%	22.3%	34.5%	23.2%	
Demand deposits	43,275					100.0%
Issues for retail investors	2,547	16.6%	6.0%	46.3%	28.1%	3.0%

The Group's deposit products are distributed through its Commercial Banking and Corporate Banking and Global Businesses units and its private banking arm, Sabadell Urquijo Banca Privada. Key financial data for these business units can be found in section 2.4 above.

The upward trend in the Group's deposit base in recent years has made it possible to replace capital market funding with customer deposits. This has not only helped to boost the Group's earnings but has also driven down its loan-to-deposit (LTD) ratio from 147% at the end of 2010 to 104% at the close of 2014. The loan-to-deposit ratio is obtained by dividing net lending (adjusted for subsidized finance) by retail deposits.

Capital market

As a result of deleveraging by the Group and its successful campaign to attract deposits, the proportion of funding raised on the wholesale markets has declined steadily in recent years. At the end of 2014 the outstanding balance of capital market funding was €23,106 million, compared with €26.063 million at the end of 2013. In terms of product type, €14,406 million of the total sourced from capital markets was raised from mortgage covered bonds, €1.941 million from senior debt (of which €1,059 million consisted of Spanish government-backed bond issues resulting from the takeover of Banco CAM), €917 million from subordinated debt issues (including Mandatory Convertible Subordinated Debentures IV/2013 issued as part of the buyback arrangements for Banco Gallego hybrids) and preference shares, and €4,062 million from preference shares and asset-backed securities sold on the open market. The maturities of institutional issues by product type at 2014 year-end are shown in note 37 to the financial statements.

Short-term funding arrangements included a Spanish commercial paper programme whose outstanding amount cannot exceed €5,000 million and a Euro Commercial Paper (ECP) programme for a nominal value of up to €3,500 million. The amount of outstanding commercial paper issues directed mainly at the domestic market remained stable over the year, with a slight reduction in the outstanding amount of commercial paper placements with non-qualified investors, which was offset by an increase in the amount placed with institutional investors. At 31 December, the outstanding balance was €2,745 million (net of commercial paper purchased by Group companies). The balance of the ECP programme, aimed at qualified international investors, expanded slightly from €98.6 million at the end of 2013 to €165.2 million at 31 December 2014.

As part of the Group's longer-term funding, on 29 April 2014 an issuance programme of non-equity fixed-income securities with an upper limit of €10,000 million was registered with the CNMV. During 2014, Banco Sabadell issued bonds totalling €4,087 million under the programme, both for placement on the market and for retention by the Group. During the year the Group tapped the bond market on a number of occasions. Banco Sabadell made a public offering of 7-year mortgage covered bonds totalling €1,250 million; three issues of 8- and 9-year mortgage covered bonds totalling €388 million, underwritten in their entirety by the European Investment Bank (EIB); six issues of senior debt between 1.5 and 5 years totalling €916.5 million; and 13 issues of structured bonds amounting to €68 million with maturities of between one and 10 years. Additionally, as part of funding arrangements agreed between the ICO and Banco Sabadell, the Bank carried out 71 issues of straight bonds with maturities of between two and six years, all of which were fully subscribed by the ICO for a total of €588.9 million. In current market conditions the Group would have the ability to carry out debt issues in a variety of formats and maturities.

Historically the Group has been very active in originating asset-backed securities. It currently has 40 such issues outstanding (including issues by Banco Guipuzcoano, Banco CAM, BMN and Banco Gallego); a portion was retained by the Group as liquid assets available for use as eligible collateral in funding arrangements with the European Central Bank, and the remaining bonds were sold on the capital markets. At the end of 2014 the Group had €4,062.3 million outstanding in asset-backed securities. For reasons of efficiency six asset-backed issues with relatively small outstanding balances were redeemed early in 2014.

The capital markets remained upbeat in 2014 and in the market as a whole there was no large-scale refinancing of maturing debt. This, together with the ECB's economic stimulus measures in the fourth quarter, resulted in a surplus of liquidity. This situation, together with low interest rates, boosted the repo market, where counterparty risk-related concerns abated considerably. The net amount of repo funding at 31 December 2014 was €1,730 million higher in nominal terms than at 2013 year-end.

In addition to these funding sources, Banco Sabadell has a liquidity buffer consisting of liquid assets to cover possible liquidity needs. Since the start of the crisis, Banco Sabadell has accelerated the process of building up this liquidity buffer as a first line of defence. At the end of 2011 the size of the Group's "first-line" liquidity buffer was €11,399 million (that is, market value less the haircut applied by the ECB in its monetary policy operations to assets with ECB eligibility, and with the reduction in the Liquidity Coverage Ratio (LCR) in other cases). During 2012 Banco Sabadell continued to strengthen its liquid asset base by generating a positive funding gap through the branch network, bringing its first-line liquidity buffer up to €17,396 million by the end of that year. The amount of first-line liquid assets increased to €19,009 million by the close of 2013. The liquidity buffer was maintained throughout 2014, at the end of which the Group's first-line reserve amounted to €18,758 million. At the close of 2014, 93% of the Group's liquidity buffer consisted of eligible assets available for discounting in ECB funding operations. The rest was made up of such assets as the balance of liquid assets classified as of very high liquidity for LCR purposes but not eligible for discounting with the ECB; the Group's portfolio of listed equities; and investments in mutual funds and open-end investment companies (SIMCAVs), plus its net position in the interbank market.

The Group's holdings of assets eligible as collateral to the ECB are shown below, classified by rating and liquidity class as defined by the Bank of Spain in its Technical Application 1/2013:

	LIQUIDITY CATEGORY *(In €Mn. at effective value (market value + BCE haircut))*					
RATING (*) (DBRS/ Fitch/Moody's/ S&P's)	**I**	**II**	**III**	**IV**	**V**	**Non-negotiable securities**
Up to AAL/ AA-/ Aa3/ AA- or R-1H/ F1+/ A-1+	52	0	6,369	0	210	
Up to AL/ A-/ A3/ A- or R-2H/ F1/ P-1/ A-1	7,450	455	2,304	18	2,219	3,239
Up to BBB/ BBB-/ Baa3/ BBB- or R-2M/ F2/ P-2/ A-2	573	933	437	66	341	
TOTAL	**8,075**	**1,388**	**9,110**	**84**	**2,770**	**3,239**

(*) Where more than one rating has been assigned the highest rating has been shown except in the case of category V, where the second highest rating is shown.

In addition to its first-line liquidity buffer, the Group maintains a buffer of mortgage assets and public sector loans that are eligible as collateral for mortgage and public sector covered bonds, respectively. At the end of 2014, these provided an additional capability for the issuance of covered bonds — eligible to be discounted as collateral with the ECB — in an amount of €9,941 million. By the close of the year, the Group's available liquidity reserve had reached an effective amount of €28,699 million, composed of the Group's "first line" liquidity reserve plus its year-end capacity to issue mortgage and public sector covered bonds.

5.2. Capital resources

The way in which the Group's capital resources are managed is the result of an ongoing capital planning process. This planning takes account of expected future changes in the economic, regulatory and business environment, as well as more adverse scenarios. It considers the likely capital consumption of different areas of activity under different scenarios, and market conditions that are likely to have a bearing on any actions that are proposed. Capital management is framed within the context of the Bank's strategic objectives and the search for attractive shareholder returns, subject always to ensuring a level of own funds sufficient to cover the risks inherent in the business.

The new regulatory framework on the minimum own funds that Spanish credit institutions must hold, both individually and on a consolidated basis, the way in which those resources are determined, the various capital self-assessment processes they must perform and the information they must disclose to the market entered into force on 1 January 2014. The regulatory framework comprises:

- Directive 2013/36/EU, of the European Parliament and of the Council, of 26 June 2013, on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (generally referred to as CRD IV).
- Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012) (generally referred to as CRR).

As a Spanish credit institution, the Group is subject to CRD IV, through which the European Union is implementing the Basel III capital rules issued by the Basel Committee on Banking Supervision (BCBS) under phase-in allowances until 1 January 2019. CRD IV has been partially implemented in Spain through (i) Royal Decree-Law 14/2013, of 29 November, on urgent measures to adapt Spanish legislation to European Union regulations on bank supervision and solvency, and (ii) Law 10/2014 of 26 June on the organization, supervision and solvency of credit institutions.

The CRR, which is directly applicable to Spanish credit institutions, implements the CRD IV requirements while leaving certain options to national authorities. Under the authorization granted by Royal Decree-Law 14/2013, the Bank of Spain issued Circulars 2/2014 and 3/2014 on 31 January and 30 July respectively, using certain permanent regulatory options envisaged in the CRR, including those applicable to the transitory regime on capital requirements and to the treatment of deductions.

According to the requirements established in the CRR, credit institutions must have a total capital ratio of 8% at all times. However, regulators may exercise their powers under the new regulatory framework and require that banks maintain additional capital levels.

As required by this new regulatory framework, all allowances of the Bank of Spain's Circular 3/2008 that would be in conflict with the above-mentioned European regulation were repealed as of 1 January 2014.

Capital resources are grouped into categories according to their capacity to absorb losses, their long- or short-term nature, and their seniority. The categories of capital, ranked in descending order of permanence, loss absorption capacity and seniority, are common equity and other first-level capital instruments, which together form primary (Tier 1) and secondary (Tier 2) capital instruments. The overall capital base is obtained by adding Tier 1 capital to Tier 2 capital.

In the last four years the Bank has increased its capital base by issuing securities qualifying as primary capital, which have enabled it to increase its capital by more than €5,000 million.

Mandatory Convertible Subordinated Bonds were converted to shares for €31.35 million in 2014.

All these transactions and events enabled Banco Sabadell to increase its core capital/common equity to 11.7% in December 2014.

With regard to risk-weighted assets, in 2008 Banco Sabadell was one of the seven Spanish financial institutions to obtain Bank of Spain approval to use internal credit risk models for the calculation of regulatory capital under the (then) new capital framework known as Basel II.

Central bank approval meant recognition and endorsement of the risk management and control systems that Banco Sabadell had begun to develop in the mid-1990s and which have since enabled it to maintain an excellent credit quality.

Since then, through constant attention to its balance sheet and its capital, and thanks to Regulator-approved changes in the development of its internal risk models, Banco Sabadell has been able, by a process that is still ongoing, to respond to increases in capital requirements arising from its acquisitions: Banco Guipuzcoano, Banco CAM, Banco Gallego, BMN-Penedès, and Sabadell Solbank (formerly Lloyds Bank).

Even so, risk-weighted assets (RWA) increased by 2.12% in 2014. This was due to the effect of applying the new rules described above, which introduced new areas of capital consumption connected with deferred tax assets and significant holdings in financial sector entities, among other aspects.

A reconciliation between net worth and regulatory capital is shown in the following table:

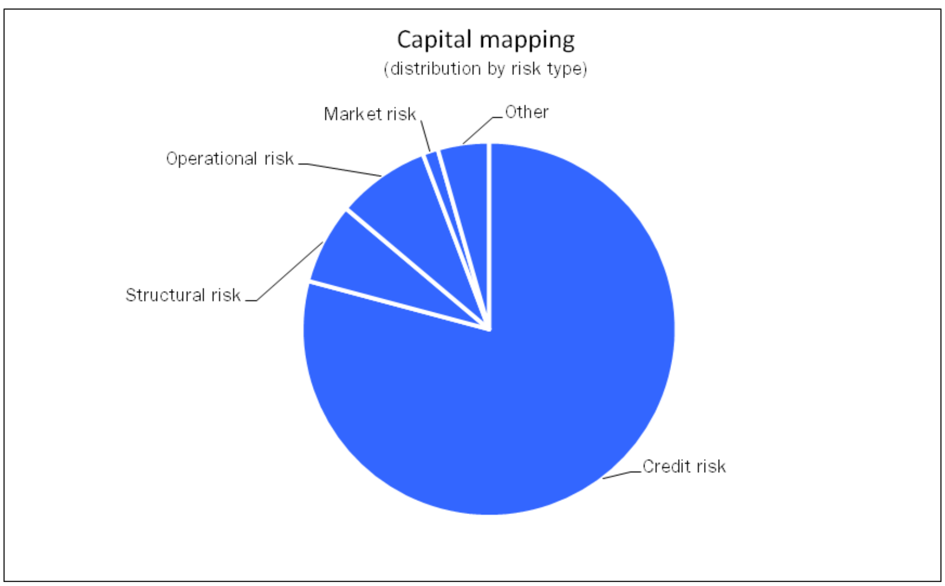
€million	2014	2013
Shareholders' equity	10,224	10,227
Measurement adjustments	937	121
Non-controlling interests	55	58
Total equity	**11,216**	**10,406**
Goodwill and other intangible assets	(684)	(1,539)
Other adjustments	(1,829)	(150)
Regulatory accounting adjustments	**(2,513)**	**(1,689)**
Common equity Tier I capital	**8,703**	**8,717**
Additional Tier I capital	**0**	**(4)**
Tier II capital	**839**	**588**
Total regulatory capital	**9,542**	**9,301**

Considering that risk-weighted assets amounted to €74,417,813,000 in 2014 and €72,876,287,000 in 2013, the Bank's year-end capital ratios were as follows:

%	2014	2013	requirement (*)
Core capital	11.7	12.0	
Principal capital (Bank of Spain Circular 7/2012)	n/a	11.7	9
Tier I	11.7	12.0	
Tier II	1.1	0.8	
BIS ratio	12.8	12.8	8

(*) When the 2013 ratios were calculated the Basel II rules were applicable, whereas the 2014 ratios were arrived at in accordance with Basel III.

The breakdown of capital requirements by type of risk is as follows:



Results of the comprehensive assessment

In October 2014, the European Central Bank (ECB) conducted a comprehensive assessment of the 128 largest banks in the euro area in cooperation with the national authorities and, for the stress test, in close collaboration with the European Banking Authority (EBA). The published results concluded that the values of Banco Sabadell's assets, collateral and reserves were appropriate and that the Bank would not require additional capital in any of the scenarios considered.

The Comprehensive Assessment (CA) began in November 2013 and was a prerequisite for the ECB to undertake its new supervisory functions, which it assumed one year later. The CA covered a very significant part of the processes and procedures of the banks that were analysed.

The CA comprised the following phases:

1. Asset Quality Review (AQR)

The objective of the first phase was to perform a detailed review of bank balance sheets to determine, inter alia, whether their loan classifications (performing/doubtful), allowances and valuations of specific assets were appropriate.

The ECB started by reviewing the Bank's main accounting policies, processes and criteria, covering areas related to funding activities (treatment of refinanced loans, the accounting system for allowances, and the definition of "doubtful"), and other areas such as consolidation and measurement of financial instruments, including derivatives.

Next, after selecting the portfolios that represented the highest levels of risk and exposure, the ECB reviewed a sample of borrowers (based mainly on loan applications). In the case of Banco Sabadell, the entire loan book was considered, which involved a review of 905 borrowers (including the 210 largest customers) and re-measurement of more than 1,500 property appraisals.

This phase, which was assisted by leading audit firms and was subject to quality control by the ECB and the Bank of Spain, had the potential to trigger adjustments to the level of CET1 to be used as the starting level for the stress test.

2. Stress test

This second phase sought to analyse the ability of banks' balance sheets to withstand two hypothetical scenarios: a baseline, or more probable, scenario (macroeconomic scenario approved by the European Commission) and an adverse or more severe one (established by the European Systemic Risk Board) for 2014-2016.

The test was based on consolidated balance sheets at 2013 year-end and used a bottom-up approach, applying the methodology defined by the EBA at the lowest level of granularity in the Bank's portfolio, including in this case all of its lending and all of its exposure to sovereign and corporate debt, investees and real estate. As a result, all the main credit, market, counterparty and real estate risks were analysed.

Detailed templates were used to ensure that the exercise was unbiased; as with the previous phase, the ECB and the Bank of Spain oversaw quality.

The minimum capital threshold was fixed at 8% in the baseline scenario and 5.5% in the adverse scenario.

Results of the Comprehensive Assessment

According to the published results of the Comprehensive Assessment for each of Europe's 128 largest banks, 25 institutions failed the test with a capital shortfall totalling €25,000 million. However, corrective actions implemented in 2014 had reduced the shortfall to €9,500 million, distributed among 13 banks. All Spanish banks passed the stress test and the AQR, with the exception of one minor institution (as defined by the ECB), whose capital shortfall was duly covered as a result of actions implemented in the first half of 2014.

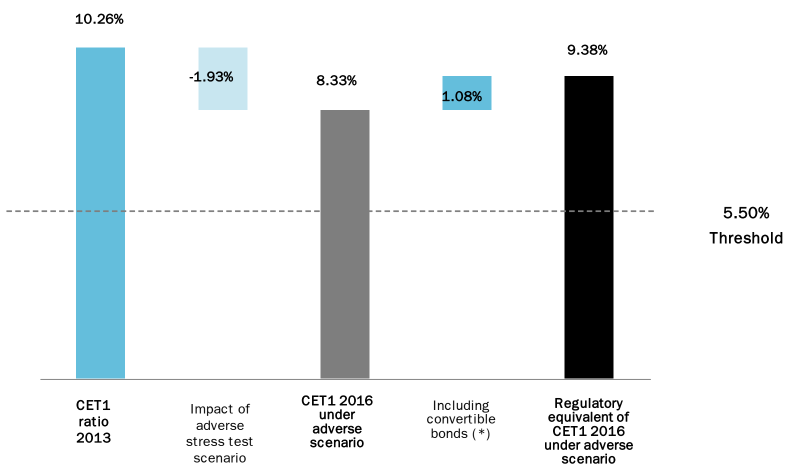
Banco Sabadell was the only Spanish bank whose initial capital ratio was not adjusted as a result of the Asset Quality Review (AQR). Only 15 European banks were not required to make any adjustments.

The stress test concluded that Banco Sabadell had a common equity Tier 1 (CET1) ratio of 10.26% and that in the most adverse scenario considered the ratio would be 8.33%, well above the required minimum of 5.5%. With these ratios, it was estimated that Banco Sabadell had surplus capital amounting to over €1,700 million in the baseline scenario and over €2,200 million in the adverse scenario.

These results did not take account of the effect of mandatory convertible bonds (not included in the stress test even though they mature in 2015); neither did they include all of the deductions envisaged under Basel III. If those items had been considered, the CET1 ratio would have been 9.38% (including convertibles) and 8.8% (fully loaded) in the adverse scenario.

The Group's directors believe that these results vindicate the capital-raising actions performed by Banco Sabadell in the last three years, while also strengthening its competitive position in Spain, and that they reflect the quality of its financial asset management.

Banco Sabadell. Stress test – adjusting factors
Common Equity Tier 1 ratio 2016 in the adverse scenario
In percentage



(*) Given that mandatory convertible bonds are not included in the scope of the stress test, they have been added back for illustrative purposes.
Total mandatory convertible bonds of €860M (105bps) as of December 2013, of which the maturity calendar is: €17.6M in 2014, €755.6M in 2015, €68.6M in 2016 and €17.6M in 2017.

6. RISKS

In 2014, Banco Sabadell Group continued to strengthen its risk management framework and to make improvements in line with financial sector best practice.

The main challenges this year were developing a new Risk Appetite Framework that ensures control and proactive management of all the Group's risks, and strengthening the governance framework for risks.

In 2014, the Group also integrated the business from the Banco Gallego and Lloyds Banking Group Spain acquisitions into its systems by standardizing risk management and control.

Below are the main aspects, which are detailed later in this report.

Risk Appetite Framework

The Banco Sabadell Group has a new Risk Appetite Framework, which aims to ensure control and proactive management of all Group risks. This new framework includes a Risk Appetite Statement, which establishes the amount and diversity of risks that the Group seeks and tolerates in order to achieve its business goals while maintaining a balance between risk and return.

The Risk Appetite Statement comprises quantitative metrics which allow for objective monitoring of risk management, as well as complementary qualitative aspects. It is implemented throughout the organization by means of the Risk Appetite Framework, using various instruments, including:

- Risk management policies
- Models
- Tools
- Regulations
- Strategic planning
- Incentives
- Monitoring and reporting
- Pricing
- Communication
- Adequacy protocol

Strengthening risk function governance

The Risk Appetite Framework is covered by an updated risk governance framework in accordance with European and national regulations (specifically, CRR and CRD IV and their transposition to Spanish law through Law 10/2014 on the organization, supervision and solvency of credit institutions).

Accordingly, the Bank has strengthened the supervisory role of the Risk Committee, made up of non-executive Board members, whose main function is to ensure that the risks undertaken by the Group conform to the Risk Appetite Statement approved by the Board of Directors.

The Group has state-of-the-art risk control systems that is well suited to the activities of its business units and to the risk profile it pursues. These control systems are built into the Bank's principal risk acceptance, monitoring, mitigation and recovery procedures.

The Bank's risk control function is responsible for monitoring and evaluating the main risks, ensuring that all risks identified are supervised effectively by the various business units and always ensuring that the Bank's risk profile is attuned to the Risk Appetite Statement.

Reviewing compliance with the established control framework and its application to management is the responsibility of the Internal Audit Department, which advises the Board of Directors and Senior Management on the effectiveness and adequacy of established processes and controls.

Technological and functional integration of Banco Gallego and Lloyds Banking Group Spain

The integration, in terms of technology and risk management, of the two absorbed banks (Banco Gallego and Lloyds Banking Group Spain) was concluded in 2014. The loan portfolio acquired from these banks, and also their branches, are now covered by the Group's risk management framework, in terms of both acceptance and monitoring.

6.1. General risk management principles

6.1.1 Corporate risk culture

Banco Sabadell's risk culture is one of its distinguishing features and is well established throughout the organization as a result of continuous development over the decades. Aspects of this strong risk culture include:

- A high level of involvement by the Board of Directors in risk management and control. The Bank has had a Risk Control Committee since before 1994, whose main function is to supervise the management of all significant risks and ensure that they are in alignment with the profile defined by the Bank.

- The Basic Management Team, a key part of the risk acceptance and monitoring process. The team structure, which has been in place for more than 20 years, comprises an account manager and a risk analyst. Each of them contributes their individual view to the management process; decisions must always be discussed and agreed upon by the parties. This involves the team in the decision and results in a fuller discussion and a more reliable outcome.

- A high degree of specialization: specific management teams for each segment (Real Estate, Corporate, Companies, SMEs, Retail Investors, Banks and Countries, etc.), allowing for specialized risk management in each area.

- Advanced internal credit rating models, which have been a basic component of decision-making for more than 15 years (since 1999 for individuals and 2000 for companies). The Bank, in accordance with best practice, relies on these models to improve the general efficiency of the risk management process.

- The delegation of loan approval authority at various levels, based on expected losses.

- Rigorous monitoring of credit risk supported by an advanced system of early alerts for companies and individuals. Risk monitoring at customer or risk group level can be organized into three types: operational, systematic and integral. One of the basic tools for monitoring is an early alert system for companies and individuals (implemented in 2008 and 2011, respectively) which provides advance warning of credit risk. These alerts are based on both internal data (e.g. the number of days an instalment is past-due, limits exceeded on discounted bills, guarantees or international credit lines), and external data (e.g. customers classified as delinquent elsewhere in the financial system, and credit bureau reports).

- An advanced model for managing non-performing exposures which enhances early detection and specialized management. An end-to-end model for managing non-performing exposures which enables risk management to focus those situations closer to default (early warnings, refinancing, collection). This comprehensive system has specific tools (simulators to seek the best solution in each case) and dedicated managers who specialize in specific customer segments.

- Risk-adjusted pricing. Commercial pricing policy is dynamic, adapting constantly to changing business and financial market conditions (liquidity premium, difficulty in accessing credit, interest rate volatility, etc.). Funding and risk costs are taken into consideration (expected loss and cost of capital). Risk models play a vital role in determining prices and profitability targets.

- The risk management model is fully integrated into the Bank's technology platform, with the result that policies are applied immediately in everyday processes: the policies, procedures, methodologies and models that make up Banco Sabadell's risk management approach are built into the Bank's operating platform. This means that policies are applied immediately in everyday processes. This proved particularly important when integrating the Bank's recent acquisitions.

- Use of stress testing as a management tool: Banco Sabadell has for some years been using a powerful calculation tool to perform stress tests, supported by in-house teams with extensive experience in its development. Considerable progress has also been made in the last year, including: upgrading the tool (greater granularity, calculation power, etc.), defining potential uses of the tool and establishing a governance framework.

6.1.2 Risk Appetite Framework

In 2014, the Banco Sabadell Group developed a new Risk Appetite Framework which broadens and reinforces the existing management framework.

This Framework includes the Risk Appetite Statement, defined as the amount and range of risk that Banco Sabadell Group seeks and tolerates in order to achieve its business goals while maintaining a balance between risk and return.

The Risk Appetite Statement (RAS) comprises quantitative metrics, which allow for objective monitoring of compliance with established targets and limits, and qualitative elements, which complement the metrics and guide the Group's risk management and control policy.

Quantitative elements

The quantitative metrics in the RAS are organized into six broad sections:

- Capital and Solvency: amount and quality of capital
- Liquidity: liquidity buffers and funding structure
- Profitability: the right balance of risk and return
- Asset Quality: for the various types of relevant risk, and in stressed scenarios
- Losses: for the various key risks and in stressed scenarios
- Credit and Concentration: individual and sector

Qualitative aspects

In addition to quantitative metrics, the Risk Appetite Framework includes the following qualitative elements:

- The Institution's general position with regard to risk-taking seeks a medium-low risk profile through a prudent, balanced risk policy that ensures steadily rising profitability and is aligned with the Group's strategic objectives so as to maximize value creation while guaranteeing an appropriate level of capital.
- The Banco Sabadell Group's risk management and control approach consists of a broad framework of advanced measurement principles, policies, procedures and methodologies integrated into an efficient decision-making structure. The risk variable is factored into decisions in all areas and quantified using a common metric in terms of allocated capital.
- Risk management is underpinned by solid, ongoing procedures for checking that risks conform to pre-set limits, with clearly defined responsibilities for identifying and tracking indicators and early warnings, and an advanced risk measurement methodology.
- Capital and liquidity levels must enable the Bank to cover the risks it has assumed, even in adverse economic situations.
- Risks should not be concentrated in such a way as to significantly compromise own funds.
- The assumption of market trading risk seeks to cover the flow of transactions arising from customer business and to seize market opportunities while maintaining a position that is commensurate with the Bank's market share, risk appetite, capacity and profile.
- The risk function is independent and has strong senior management involvement, ensuring a strong risk culture focused on protecting capital and ensuring an adequate return on same.
- The Board of Directors is committed to the risk management and control processes: approval of policies, limits, management model and procedures, and the measurement, tracking and control methodology.
- The Group has a risk culture that pervades the entire organization and has units specialized in managing specific types of risk. The Risk Department transmits this culture by setting policies and implementing internal models and ensuring that they conform to the risk management processes.
- Risk Management policies and procedures should be oriented to adapting the risk profile to the Risk Appetite Framework while maintaining and pursuing a balance between expected returns and risk.
- The institution will have sufficient human and technological resources to track, control and manage all the risks that may materialize in the course of its business.
- The Group's compensation systems should align individual interests with compliance with the Risk Appetite Framework.

6.1.3. Overall organization of the risk function

The Board of Directors is the body responsible for setting general guidelines as to the organizational distribution of risk management and control functions and for determining the main lines of strategy in this respect. It is the body responsible for approving the Risk Appetite Framework (developed in cooperation with the Managing Director, the Director of Risk and the Chief Financial Officer) and ensuring that it is aligned with the Bank's short- and long-term objectives, as well as with the business plan, capital planning, risk capacity and compensation programmes.

The Board of Directors has four committees which play a role in the management and control of risk. The Bank also has several other Committees which participate in this function.

6.2. Managing and monitoring the main risks

6.2.1. Credit risk

Credit risk is the possibility that losses may be incurred as a result of borrowers failing to meet their obligations or through losses in value due simply to deterioration in borrower quality.

Credit risk management framework

Acceptance and monitoring

To maximize the business opportunities provided by each customer and to guarantee an appropriate degree of security, responsibility for risk acceptance is shared between the relationship manager and the risk analyst, who are thus able to obtain a comprehensive view of each customer's individual circumstances.

The Board of Directors delegates powers to the Executive Committee, which then sub-delegates authority at each level. The implementation of authority thresholds in the credit acceptance systems ensures that powers delegated at each level are linked to the expected loss calculated for each loan.

The analysis of indicators and advanced alerts as well as rating reviews allow for risk quality to be continuously measured in an integrated way. The establishment of effective processes for managing existing risk exposures also benefits the process of managing past-due accounts, since the early identification of probable default cases ensures that measures can be taken proactively.

The Bank's early warning alert system means that the quality of a risk can be assessed in an integrated way and ensures a timely referral of the risk to recovery specialists, who determine the most appropriate approach. When risks exceed a certain limit or loss ratio, groups or categories are established to address them.

These alerts are managed jointly by the relationship manager and the risk analyst, helped by the feedback obtained as a result of direct contact with the customer.

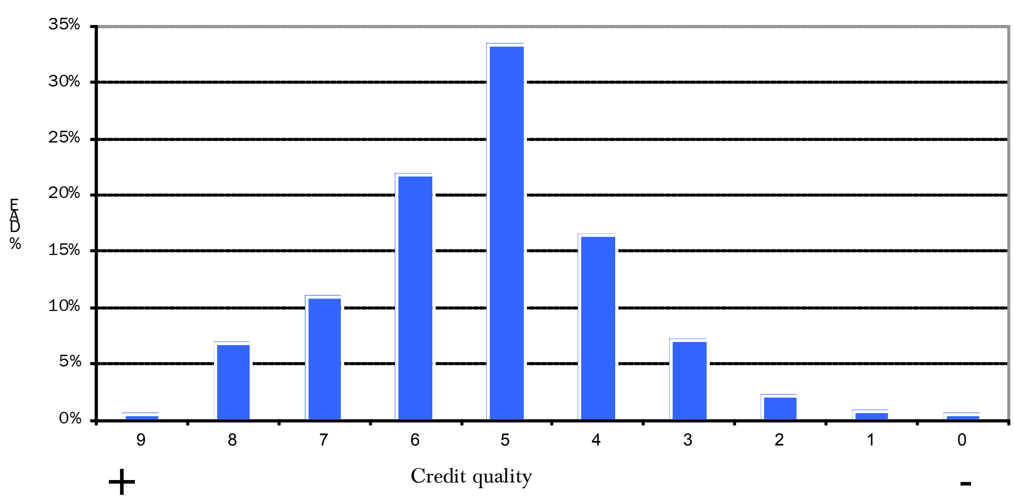
Risk management models

Credit rating

Credit risk exposures to corporate customers, real estate developers, specialized financing projects, retailers and sole proprietors, financial institutions and countries are assessed according to a system of credit ratings based on predictive factors and internal estimates of the probability of default.

The rating model is reviewed each year on the basis of an analysis of actual default data. Each internal rating score is assigned an anticipated default rate which allows consistent comparisons to be made across segments and with the ratings produced by independent rating agencies, according to a master scale.

BS business loan portfolio - credit rating profile



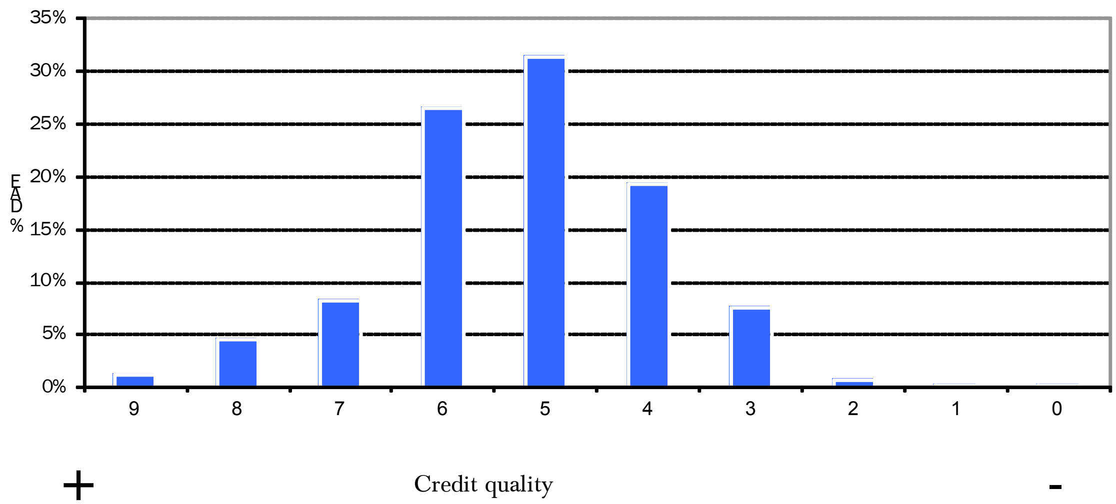
Scoring

Credit risk exposures to individual customers are classified by means of scoring systems which make use of quantitative modelling based on historical data to identify key predictive factors. Two types of scoring are used:

Behavioural scoring: The system in which all customers are automatically classified according to their transaction histories and data for each product acquired. It is used primarily for such purposes as granting loans, setting overdraft limits, targeting sales campaigns, and for tracking and segmenting in claim and/or recovery procedures.

Reactive scoring: This is used to evaluate applications for personal loans, mortgage loans and credit cards. When full details of the application have been entered, the system generates a result based on the estimated borrowing capacity and financial position of the applicant and the quality of any security or collateral.

Individual customer loan portfolio - credit rating profile



Early alert tool

For both Companies and Individuals, Banco Sabadell has a system of early alerts which, based on available information sources (rating or scoring, customer file, balance sheets, the Bank of Spain's CIRBE risk information system, industry information, transaction data, etc.), models the customer's short-term risk (anticipating delinquency) and achieves a high level of predictability in detecting potential non-performing exposures. The score, which is produced automatically, is included in the monitoring process as one of the basic inputs in tracking the risk posed by individuals and companies.

This alert system allows for

- Improvements in efficiency by focusing attention on customers with lower credit scores (different groups are assigned different thresholds).
- Early action in view of a customer's worsening situation (change of score, new serious alerts, etc.).
- Periodic oversight of customers who remain in the same situation and have been analysed by the Basic Management Team.

Non-performing risks

Banco Sabadell has an advanced non-performing risk management model for impaired asset portfolios.

The objective of managing non-performing exposures is to find the best solution for the customer at the first sign of impairment so as to reduce the number of customers in difficulties who enter default. This should be done through intensive management with no dead times between the various phases of the process.

Country risk

This is the risk of incurring loss from exposures to sovereign borrowers or to persons domiciled in a particular country for reasons connected with national sovereignty or the economic situation of the country, i.e. for reasons other than the usual commercial risk. Country risk includes sovereign risk, transfer risk and other risks inherent in global financial operations (war, expropriation, nationalization, etc.).

An overall exposure limit is set for each country and this applies across the whole Banco Sabadell group. These limits are approved by the Executive Committee and the corresponding decision-making organ, depending on the level of delegation, and are constantly monitored to ensure that any deterioration in the political, economic or social situation in a country can be detected in good time.

A range of different tools and indicators are used to manage country risk. credit ratings, CDS, macroeconomic indicators, etc.

Counterparty risk

The counterparty risk management philosophy is aligned with the business strategy, which pursues value creation through the efficient use of capital allocated to the business units. Strict criteria have been established for managing counterparty risk deriving from the financial markets, to guarantee the integrity of Banco Sabadell Group's capital.

Banco Sabadell has a system for evaluating and managing those risks, which allows it to monitor and control compliance with approved limits on a daily basis.

Additionally, to mitigate exposure to counterparty risk, Banco Sabadell has Credit Support Annexes (CSA) and Global Master Repurchase Agreements (GMRA) with most counterparties, which notably reduces the risks incurred through the provision of collateral.

Concentration risk

Concentration risk refers to exposures that can potentially generate enough losses to threaten the financial health of an institution or the viability of its ordinary business activity. This type of risk is divided into two basic subtypes:

- Individual concentration risk: imperfect diversification of idiosyncratic risk in the portfolio, due either to its small size or to very large exposures to specific customers.

- Sectorial concentration risk: imperfect diversification of systematic risk components in the portfolio. Such concentrations may occur in particular sectors or geographical regions, for example.

In order to ensure on efficient management of concentration risk, Banco Sabadell has a series of specific tools and policies:

- Quantitative metrics in the Risk Appetite Statement and their subsequent monitoring as top-level metrics

- Individual limits for risks and customers considered to be significant, which are established by the Executive Committee

- A structure of delegation which require that relevant customer transactions be approved by the Credit Operations Committee, or even by the Executive Committee

Greater information on credit risk, both qualitative and quantitative, can be found in the Notes to the Accounts (especially Notes 8, 9, 18, and 37).

6.2.2. Liquidity Risk

Liquidity risk can be defined as the possibility of losses being incurred as a result of the Bank’s being unable, even if only temporarily, to attend payment commitments due to a lack of liquid assets, or of its being unable to access the markets to refinance debts at a reasonable cost. This may be associated with factors of a systemic nature or specific to the Bank itself.

Liquidity risk management is established around the basic requirement that the Group have, at all times, enough liquidity to achieve with the levels established by regulation and by the Bank's internal risk management policies.

As an additional policy, the Bank requires a reserve margin to cover liquidity needs arising from maintaining liquid assets classified as eligible collateral by the European Central Bank that is sufficient to fund debt issued on the capital markets that matures in the next 12 months.

A number of methodologies and information systems are used to evaluate this risk:

- Information related to the daily balance of assets and liabilities and the financial market situation.
- Information on liquid assets and second-line liquidity reserves based on assets eligible for discounting with the ECB.
- Liquidity gap using the tool's measurement framework to measure out interest rate risk, with the ability to perform simulations.
- Information on the maturities of funding obtained in the wholesale markets.
- Periodic stress tests.
- General market information: issues, spreads, external rating agency reports, etc.

The Bank periodically carries out a stress test exercise focused on its position in the institutional market. The stress test measures the effects of a prolonged shutdown of the capital and interbank markets combined with a one level fall in the Bank's credit rating and a flight of deposits held by institutions and companies with professional treasury management functions. The result of this exercise is to ensure that the Bank continues to hold a cushion of liquid assets sufficient to cover the net balance of inflows and outflows in a stress situation lasting for up to a year.

In addition, the Bank carries out a further stress exercise which, unlike the one described above, assumes the complete drawdown of all available funds from the Bank within a period of one month, the withdrawal of 7.5% of its retail customer deposit base (households and SMEs) and of 15% of its corporate and public sector deposit base within one month, and the non-renewal of all securities sold to retail customers.

The Bank also analyses the robustness of its holdings of liquid assets such as ECB-discountable assets by conducting a study of the sensitivity of its eligible asset base to different scenarios combining credit rating downgrades and impacts on the market prices of the assets. The purpose of this exercise is to establish that the Bank's eligible asset base is sufficiently robust to ensure that it is holding available eligible assets that are sufficient in terms of its current position *vis-à-vis* the ECB.

As part of its stress test exercises, each month Banco Sabadell draws up a contingency plan for responding to two different stress liquidity situations: a systemic crisis and a crisis specifically affecting Banco Sabadell. The contingency plan examines the Group's ability to issue securities on the capital market under each of the scenarios and all balance sheet assets that would be capable of generating liquidity. It determines, for each asset class and under each crisis scenario, the proportion that could be made liquid within one week and one month. This establishes the Group's contingent liquidity in a liquidity crisis situation.

As regards the new Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR), Banco Sabadell is providing the Regulator with the information required under the EBA's new liquidity templates on a monthly and quarterly basis, respectively. The Group amply exceeds the LCR requirement. At the end of 2014, its LCR was over 100%, compared with the minimum requirement of 60% in 2015. The NSFR is still in the final phases of being analysed and defined. The NSFR is expected to be implemented in January 2018, with a phase-in period, like the LCR.

6.2.3. Market risk

Market risk arises from possible fluctuations in the fair value or future cash flows of a financial instrument as a result of changes in market risk factors. Several types of market risk factors can be distinguished, the main types being interest rate risk, exchange rate risk, stock price risk and credit spread risk.

Different approaches are taken to manage this risk, depending on which of the Group's main business lines has given rise to it:

Risk arising from proprietary trading as part of the strategy of focusing on customer business. Risk that is primarily attributable to Treasury and Capital Market positions using currency instruments, equities and fixed-income, in both the treasury and derivatives markets.

Risks arising from the Group's commercial banking with customers and its corporate banking businesses, known as structural balance sheet risk. These risks can be sub-classified into interest rate risk and currency risk.

The system for acceptance, management and control of market risk is based on establishing limits for expressly assigned positions and approval of transactions for each business unit, with the result that the various management units must always keep their positions within the established limits and obtain approval for transactions from the risk management function.

Trading

The main indicator used to measure market risk is VaR (Value at Risk), which allows the risks on different types of financial market transaction to be analysed as a single class. The VaR method provides an estimate of the potential maximum loss on a position that would result from an adverse, but possible, movement in any of the market risk factors. This estimate is expressed in money terms and is calculated at a specified date, to a specified confidence level and over a specified time horizon. The estimate takes account of the different levels of market risk factors (interest rate, currency rate, equities and credit spread) to which the transaction is exposed.

Market risk is monitored on a daily basis and reports on current risk levels and on compliance with the limits assigned to each unit are referred to the risk control functions. Limits are assigned by the Risk Control Committee for each management unit (based on nominal values, VaR or sensitivity, as applicable). This makes it possible to track changes in exposure levels and measure the contribution of each risk factor.

Risk control of this kind is supplemented by special simulation exercises and extreme market scenarios (stress testing), which provide the positions' risk profile. However, the VaR methodology does not rule out the possibility that losses will exceed the set limits, as significant market movements may occur that exceed the confidence levels being applied. The reliability of the VaR methodology is validated by back-testing techniques which are used to verify that VaR estimates are consistent with the specified confidence level.

Structural interest and exchange rate risk

Structural interest rate risk:

Interest rate risk is caused by changes in interest rates or in the levels or slope of the yield curve to which asset, liability and off-balance sheet positions are fixed. Gaps arise between these items because of differences in repricing and maturity schedules may affect the robustness and stability of results.

The management of interest rate risk focuses on overall financial exposure for the Group as a whole and involves proposing alternative commercial or hedging strategies that will meet business objectives and are appropriate to market conditions within the exposure limits established for the Group. A number of methodologies are used to measure interest rate risk. These include measuring the sensitivity of net interest income to changes in interest rates over a one-year horizon. This is done by means of static (gap analysis) and dynamic (simulation) techniques based, in the latter case, on different assumptions of balance sheet growth and changes in the slope of the yield curve.

Another technique is to measure the sensitivity of equity to changes in interest rates using duration gap analysis. This measures the effect of interest rate changes over a longer time horizon.

Structural exchange rate risk

Structural exchange rate risk arises as a result of changes in the exchange rates between different currencies and the possibility that these movements may result in losses on financial investments and on permanent investments in foreign branches and subsidiaries.

Exchange rate risk is monitored on a daily basis and reports on current risk levels and on compliance with the limits assigned to each unit are sent to the decision-making authority.

6.2.4 Operational risk

Operational Risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, and systems or from unforeseen external events. This definition includes reputational risk (which includes behavioural risk), technology risk and model risk.

Management of operational risk is decentralized and devolved to the people in charge of organization-wide processes. All of those processes are identified on a corporate process map, thus facilitating the compilation of information in a way that reflects the structure of the organization. The group has a specialized central unit to manage operational risk, whose main functions are to coordinate, supervise and promote the identification, assessment and management of risks by process managers in line with Banco Sabadell's process-based approach.

Senior management and the Board of Directors play a direct, hands-on role in managing operational risk by approving the risk management framework and its implementation as proposed by an Operational Risk Committee, made up of senior managers from different functional areas of the company; they also ensure that regular audits are carried out on the management strategy being applied, the reliability of the information being reported, and the internal validation tests required by the operational risk model. Management of operational risk is divided into two action areas:

- The first action area is based on an analysis in which all processes and any associated risks that involve potential losses are identified, leading to a qualitative evaluation of the risks and their associated control mechanisms. This is done by process managers in conjunction with the central operational risk unit. The result is an assessment that allows future exposures to be recognized as expected and unexpected losses, tendencies to be anticipated and mitigating action to be taken.

  This is supplemented by a system for identifying, monitoring and actively managing risk through the use of key risk indicators. These can be used to trigger alerts in response to increases in exposure, identify the causes of that exposure and measure the effectiveness of the controls put in place and of any improvements made.

  Care is taken to ensure that all processes identified as critical are protected by specific business continuity plans for the event of a service failure. The operational risks identified are also assessed qualitatively from the point of view of their reputational implications should the risk materialize.

- The second action area is based on experience. It consists of maintaining a database of all losses that occur in the organization, which provides a store of information of actual operational risk events for each business line and the causes of those events, so that risks can be acted upon and their causes minimized.
  This loss information is also of use in measuring the extent to which estimates of potential loss are consistent with reality, in terms of both severity and frequency, so that loss exposure estimates are constantly being updated and improved in this way.

  The database contains historical records of actual losses resulting from operational risk going back to 2002. It is constantly being updated as information is received on losses and recoveries, whether resulting from the Bank's own efforts or from insurance provision.

  Operational risk includes management and control of the following main risks:

  - Reputational risk: the possibility of losses arising from negative publicity related to the Bank's practices and activities, potentially leading to a loss of trust in the institution, with an impact on its solvency.
  - Technology risk: possibility of losses due to the inability of the systems infrastructure to fully support the continuation of ordinary business activity.
  - Model risk: possibility of losses due to decision-making based on the use of inadequate models.

6.2.5 Tax risk

Tax risk reflects the possibility of a breach, or of uncertainty over the interpretation, of tax legislation in any of the jurisdictions where the Bank operates.

Banco Sabadell Group's objective in this area is to ensure compliance with tax obligations while guaranteeing adequate returns for our shareholders.

The Board of Directors determines the tax risk control and management policies, as well as the tax strategy, with the double objective of ensuring that legal obligations are met and ensuring greater returns for shareholders.

The Tax Advisory Area provides an independent review of the Bank's operations to ensure that they conform to the tax legislation in force. Its functions can be divided into two areas, depending on Banco Sabadell's purpose in each case:

- As a taxpayer: with a view to ensuring that Banco Sabadell meets its tax obligations accurately and on time, the Tax Advisory Area performs regular checks that the Bank's general situation complies with the tax legislation, and sporadic checks, as required, that specific operations are compliant.

- As a developer of new products: the Bank's ordinary activity involves creating new products to be offered to our customers. The development of these products must include an analysis of their tax situation with a view to describing their characteristics in a transparent way.

6.2.6 Compliance risk

Compliance risk is defined as the risk of incurring legal or administrative penalties, significant financial loss or an impairment of reputation due to a breach of laws, regulations, internal rules and codes of conduct applicable to the banking industry.

One of the essential aspects of Banco Sabadell Group policy, and the basis of its organizational culture, is rigorous compliance with all legal provisions. The pursuit of our business objectives must be compliant at all times with the current legislation and with best practice.

The Group has a Compliance Department with the mission to promote and attain the highest levels of compliance with regulations and ethical standards within the Group, manage compliance risk so as to minimize the possibility of non-compliance, and ensure that any non-compliance that occurs is identified, reported and resolved diligently and that appropriate preventive measures are implemented, where they do not already exist.

The compliance model centralizes the definition of policies, procedures and controls on the parent company, together with the execution of Banco Sabadell control programmes, and decentralizes the execution of programmes to subsidiaries and branches outside Spain, while maintaining functional responsibility.

It is a flexible risk-focused model which can be adapted to the Group's strategy at all times and leverages synergies, maintaining an overall approach to those aspects that are general in scope and/or which require major technological developments, but also adapting to the specific features and legislation affecting each business or country.

The main challenge is standardizing the levels of compliance oversight across the Group and establishing minimum standards for mandatory compliance, regardless of the activity or country.

This model is based on two pillars:

(i) A central unit which serves the entire Group and is focused on overall management of Compliance Risk. Its main activity is the analysis, distribution and oversight of the implementation of all new regulations with an impact on the Group, as well as risk-focused control of proper compliance with pre-existing regulations.

It is directly responsible for executing processes considered to be high risk as they require direct, comprehensive oversight: prevention of money laundering and terrorist financing; controlling market abuse; controlling compliance with internal codes of conduct; and monitoring investor protection (MiFID).

(ii) A network of compliance officers in each subsidiary and foreign branch (functionally dependent on the Central Compliance Unit and hierarchically dependent on the head of the subsidiary/foreign branch) who execute their own control programmes and report periodically to the Central Unit, ensuring compliance with the internal rules and the legislation in force in all countries and activities in which the Group operates.

For greater efficiency, this model is implemented and enhanced through six catalysts (technology, training, procedures, communication channels, control and monitoring programmes, and a process for approving products and rules).

7 – POST-BALANCE SHEET EVENTS

Since 31 December 2014, there have been no significant events worthy of mention.

8- EXPECTED FUTURE DEVELOPMENTS

Banco Sabadell adopts three-year strategic plans designed in accordance with macroeconomic and regulatory conditions. The success it has had in implementing each of its previous strategic plans allowed Banco Sabadell to be ready for the new one and to have a high level of confidence in its successful outcome.

The "Óptima 2010" plan had the aim of preparing the Bank to become an efficient platform for growth. Once that had been achieved, the CREA plan focused on organic and inorganic growth, which enabled the Bank to reach critical mass so as to compete effectively in the Spanish financial system while the whole sector was undergoing a process of concentration.

During the implementation phase of the "CREA" plan, Banco Sabadell was able to transform itself commercially, growing its customer base by a factor of three, increasing market shares and optimizing its resources.

In the current macroeconomic context, having completed the restructuring and integration of Banco CAM and several acquisitions in 2013 in order to continue strengthening its franchise, Banco Sabadell started a new business plan that aims to extract value from the customer base by leveraging its new size and margin-generating capability. The main goal of the 2014-2016 Triple Plan is profitability. Key themes of the new plan are transformation (transformation of the business, transformation of the production process and transformation of the balance sheet) and internationalization (laying the foundations for becoming more international in terms of structure, resources, etc. and entering new markets).

The Triple plan proposes a series of financial objectives for the medium term. These include (i) bringing the cost/income or efficiency ratio (personnel and other administrative expenses as a proportion of gross income) down to 40%; (ii) a double digit return on capital (consolidated profit attributable to the Bank divided by average monthly own funds over the 3-year period); (iii) a loan-to-deposit ratio of over 100%; and, finally (iv) a core Tier 1 ratio of more than 10% (with full application of the standards laid down in the Basel III accords and CRD IV/CRR IV).

The Group met the intermediate objectives set in the Triple plan for the first year, and is therefore on track to achieve the plan's goals.

9 –RESEARCH, DEVELOPMENT AND INNOVATION

The Bank completed the integration of Banco Gallego and Lloyds Bank International in 2014, a process which began at the end of 2013.

Meanwhile, a Systems Plan was being put into effect that was more intensive than the previous year's plan and was aligned with the key aims of the 2014-2016 Triple Business Plan.

Initiatives were launched to strengthen multi-channel commercial management and marketing campaigns by implementing new tools. Projects for further improvements to branch operations and performance continued to be put in place, with initiatives such as the implementation of biometric signature input and a multi-channel document signing system. A document scanner and manager has been incorporated into the new Proteo front-end application, and the previous distributed OCR system has been replaced by a centralized OCR system that can be used from any kind of front-end application, including mobile devices.

As regards corporate mobility, the first functional versions of Proteo Mobile (the front-end application for mobile devices) have been developed.

In the field of active risk management, further work was done to develop the risk model for individual customers, and work on process automation continued.

In the Treasury, Markets and Asset Management area, efforts were made in 2014 to adapt the systems to handle negative rates and to implement a new customer risk control system for Treasury operations involving foreign exchange (TGR).

As regards Corporate Administration Systems, the main actions in the year were focused on improving processes to comply with new regulatory requirements (e.g. those related to the new CIRBE 2 statements). In the area of human resources, the Bank began implementing solutions for internal talent management.

10 –TREASURY SHARE SALES AND BUYBACKS

For information on treasury share sales and buybacks see Note 28 to the Annual Accounts.

11 – ADDITIONAL INFORMATION

a) Shares and share price information

Some indicators of the Bank's share performance are shown in the following table:

	2014	2013	YoY change (%)
Shareholders and trading			
No. of shareholders	231,481	262,589	(11.8)
Number of shares	4,024,460,614	4,011,481,581	0.3
Average daily trading volume (number of shares)	27,272,221	15,512,282	75.8
Share price (€)			
Opening session	1.896	1.975	
High	2.713	2.160	
Low	1.820	1.260	
Closing	2.205	1.896	
Market capitalization (€'000)	8,873,936	7,605,769	
Market multiples			
Earnings per share (EPS) (€)	0.09	0.04	
Book value per share (€)	2.54	2.50	
Price/Book value	0.87	0.76	
Price/earnings ratio (P/E)	23.88	52.12	
Assuming conversion of mandatory convertible bonds			
Total number of shares including those arising from conversion	4,289,732,386	4,298,634,476	
Earnings per share (EPS) (€)	0.09	0.03	
Book value per share (€)	2.38	2.34	
Price/Book value	0.93	0.81	

The Bank's share price appreciated by 16.3% in 2014, the IBEX-35 by 3.66% and the average for all listed banks by 6.27%.

b) Dividend policy

Historically the Bank had applied a dividend policy in which the payout was in the region of 50% of the profit for the year. On some occasions in the last few years, the distribution of profit in the form of a dividend has been supplemented by a distribution out of the share premium account.

In recent years, given the sector's need to strengthen its capital, the Supervisor recommended that credit institutions limit cash dividend payments to 25% of 2013 attributable profit. The Bank has a comfortable level of capital, as can be seen in the results of the ECB's comprehensive assessment in 2014. In view of this, and as the above-mentioned circumstances return to normal, the Bank can resume its previous policy of distributing approximately 50% of its profit.

c) Managing the credit rating

Banco Sabadell's credit rating and actions by credit rating agencies during the year:

In 2014, the three agencies rating Banco Sabadell's credit quality were Standard & Poor's, Moody's and DBRS. The current ratings, and the last dates on which they were affirmed, are as follows:

	Long term	Short term	Outlook	Last review
Standard & Poor's	BB+	B	Negative	27/11/2014
Moody's	Ba2	NP	Negative	23/10/2014
DBRS	A (low)	R1 (low)	Negative	09/01/2015

After Moody's downgraded the ratings of a number of Spanish banks in the second half of 2013, and as a result of its review of Banco Sabadell that commenced in July 2013, on 14 January 2014 the agency downgraded Banco Sabadell's long-term rating by one notch to Ba2 (from Ba1), with a negative outlook. In spite of the downgrade, Moody's did acknowledge Banco Sabadell's "recurring earnings power", which it said "compared favourably with those of its domestic peers".

On 27 November 2014, Standard & Poor's Rating Services upgraded Banco Sabadell's long-term rating by one notch to BB+ (from BB), and affirmed its short-term rating at B. The negative outlook reflects the possible reduction in government support for European banks when the bank resolution framework is introduced. The rating upgrade was based on the agency's view that Banco Sabadell's credit quality has improved in the context of lower economic risk for the Spanish banking system, which S&P expect will continue to increase capital ratios as a result of the steady improvement in returns in the banking business.

On 18 December 2014, DBRS upgraded Banco Sabadell's mortgage covered bonds by two notches to AA (low), from A. This rating action was the result of implementing DBRS's new methodology, Rating European Covered Bonds, and of the Bank's high level of overcollateralization, its capacity to generate sufficient payment flows for the mortgage covered bonds, and higher recovery prospects.

All the agencies highlighted the improvement in Banco Sabadell's capital position and took a positive view of the stress test results.

In the course of 2014, Banco Sabadell held meetings with the three agencies. Among the topics discussed at the meetings and in conference calls were the Bank's strategy, stress tests, profit performance, capital, liquidity, risk and credit quality, as well as its management of troubled assets.

d) Branch network

At the end of 2014, Banco Sabadell was operating 2,320 branches, 98 less than at the end of 2013, due to the optimization of the branch network following the integration of BMN-Penedès, Banco Gallego and Lloyds Bank.

Of the total number of Banco Sabadell group branches and offices, 1,204 were operating under the SabadellAtlántico brand (including 36 specialist business banking and 2 specialist corporate banking branches); 503 were operating as SabadellCAM (including 11 business banking branches); 178 formed the Banco Herrero network in Asturias and León (including 5 business banking branches); 131 were under the SabadellGuipuzcoano brand (including 5 business banking branches); 12 were operating under the SabadellUrquijo name; 108 were Solbank branches, and the remaining 53 made up the Group's international network, including the 27 operated by Sabadell United Bank and 7 by BancSabadell d'Andorra. Additionally, ActivoBank has two customer service centres. The distribution of the Group's Spanish branches by region was as follows:

Region	Branc	Region	Branc
Andalusia	142	Valencia	392
Aragón	39	Extremadura	6
Asturias	146	Galicia	129
Balearic Islands	65	La Rioja	8
Canary Islands	31	Madrid	216
Cantabria	6	Murcia	149
Castilla-La Mancha	23	Navarra	19
Castilla y León	64	Basque Count	107
Catalonia	723	Ceuta and Mel	2

Country	Branch	Representative office	Subsidiaries and associates
Europe			
Andorra			•
France	•		
Poland		•	
Portugal			•
UK	•		
Turkey		•	
America			
Brazil		•	
USA	•	•	•
Mexico		•	•
Dominican Republic		•	
Venezuela		•	
Asia			
China		•	
UAE		•	
India		•	
Singapore		•	
Africa			
Algeria		•	
Morocco	•		